EXTENSION OF THE EXPIRING TAX CUT PROVISIONS

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EXTENSION OF THE EXPIRING TAX CUT PROVISIONS

TUESDAY DECEMBER 9, 1975

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, D.C.

The committee met, pursuant to notice, at 10 a.m., in room 2221, Dirksen Senate Office Building, Senator Russell B. Long (chairman of the committee) presiding.

Present: Senators Long, Hartke, Ribicoff, Byrd, Jr., of Virginia, Nelson, Mondale, Gravel, Bentsen, Haskell, Curtis, Hansen, Packwood, and Roth, Jr.

The CHAIRMAN. The committee will come to order.

The committee today is holding hearings on the extension of those provisions of the Tax Reduction Act of 1975 due to expire at the end of this year.

These provisions include increases in the standard deduction, a $30 tax credit for each taxpayer and dependent, an earned income credit or "work bonus," and a reduction in corporate taxes on the first $50,000 of taxable income.

The House and Senate conferees on the second budget resolution have agreed to allow $6.4 billion through June 1976 for legislation to extend the expiring provisions so as to keep withholding rates at about their present levels.

For those who may not be aware of this, the Finance Committee has pending before it a bill, H.R. 10612, which in hundreds of pages makes extensive changes in our tax law. That bill is not the subject of this morning's hearings, though it does contain provisions to extend the expiring tax cuts. The Committee on Finance will be turning its attention to that bill next year.

[The press release announcing this hearing follows:]

P R E S S   R E L E A S E

FOR IMMEDIATE RELEASE
December 2, 1975

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 Dirksen Senate Office Bldg.

Finance Committee Schedules Hearing on Extension of Expiring Tax Cut Provisions

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee would hold a day of hearings on extension of provisions of the Tax Reduction Act of 1975 due to expire at the end of this year.

The Honorable William E. Simon, Secretary of the Treasury, will testify before the Committee on Tuesday, December 9, at 10:00 A.M. in Room 2221, Dirksen Senate Office Building.

Senator Long noted that the following provisions of the Tax Reduction Act of 1975 were enacted for this year only and are scheduled to expire at the end of December:

1. Standard deduction. -- For 1975, the percentage standard deduction was increased from 15 percent to 16 percent; the minimum standard deduction was increased from $1,300 to $1,600 for single people and to $1,900 for married couples; and the maximum standard deduction was increased from $2,000 to $2,300 for single people and to $2,600 for married couples.

2. $30 tax credit. -- For 1975, a tax credit of $30 was provided for each taxpayer and for each dependent for whom a taxpayer claims a personal exemption.

3. Earned income credit. -- For 1975, a refundable tax credit was provided equal to 10 percent of earned income up to a maximum of $4,000 (for a maximum tax credit of $400). The amount of the credit is reduced $1 for each $10 of earnings above $4,000 so that the credit is phased out entirely when adjusted gross income is greater than $8,000.

4. Corporate taxes. -- Under permanent law, the first $25,000 of taxable corporate income is taxed at a 22 percent rate, with income in excess of $25,000 taxed at a 48 percent rate. For 1975, the first $25,000 of income is taxed at a 20 percent rate, the next $25,000 is taxed at a 22 percent rate, and income above $50,000 is taxable at a 48 percent rate.

PR #49

The CHAIRMAN. Our first witness will be the Honorable William E. Simon, Secretary of the Treasury.

Mr. Secretary, we are very happy to have you. I would suggest you proceed as you prefer.

STATEMENT OF HON. WILLIAM E. SIMON, SECRETARY OF THE TREASURY, ACCOMPANIED BY CHARLES WALKER, ASSISTANT SECRETARY FOR TAX POLICY; WILLIAM H. GOLDSTEIN, DEPUTY ASSISTANT SECRETARY FOR TAX POLICY; AND DAVID BRADFORD, DEPUTY ASSISTANT SECRETARY FOR TAX POLICY

Secretary SIMON. Thank you, Mr. Chairman. I have a detailed statement which I would like to summarize to the best of my ability, sir.

Mr. Chairman, it is always a pleasure to appear before the Senate Finance Committee, especially on this occasion when you begin your arduous task of deliberating the tax legislation before you. Everyone in the administration considers that the work you must accomplish is critically important to the integrity of our Federal tax system and may significantly affect the future of our national economy.

There are some who hold the view that the most urgent matter before you is timing. Because four of the major provisions of the Tax Reduction Act of 1975 expire on December 31, Federal tax receipts will begin to increase on January 1, 1976, at an annual rate of approximately $10.3 billion in additional accruals of individual and corporation income taxes. And many of those concerned about the impending rise in tax revenues believe that this should not occur because it might retard the rate of economic recovery.

There is reason for giving the calendar attention. Tax changes not synchronized with the calendar year are disruptive. But, I would remind you, the legislation before you includes permanent changes in the Federal income tax structure, and these changes ought to be made only in the context of their consistency with long-range fiscal objectives. If we legislate a permanent reduction in Federal revenues, whenever we do so, unless we simultaneously legislate a reduction in the level of Federal expenditures, we merely delude our constituents that we are providing them a tax cut. We only substitute the capricious tax of inflation for the income tax we seemingly cut.

This is why President Ford proposed on October 6, that $28 billion be permanently cut from the income tax system along with a corresponding cut from the level to which fiscal year 1977 expenditures would climb if fiscal year 1976 programs are allowed to grow as presently projected.

The President does not give this principle of responsible fiscal policy mere lipservice. He said on October 6, that he would consider a tax cut unacceptable that was not accompanied by an explicit expenditure limitation, which would make clear to all whether the intent of the Government is to hold inflationary pressures in check, or to increase them.

From their enthusiastic response to the President's announced policy, we have concluded that the American people overwhelmingly support it. We must be disappointed by the response of the House of Representatives which failed, by a narrow margin, to instruct the Ways and Means Committee to incorporate an expenditure ceiling in its tax legislation. We urge this committee to provide leadership in the Senate by reporting a $28 billion tax cut linked to a fiscal year 1977 spending ceiling of $395 billion.

Before going to the immediate issue of the extension of the expiring 1975 tax cuts, I would like to emphasize the purpose of and thought behind the President's October 6 fiscal package, of which the current tax proposals are only a part. There were two broad objectives of that balanced tax-cut, spending-limitation proposal—to sustain the upward momentum of the current economic advance and, more importantly, to make a start toward regaining control over the excessive rise in budget spending which has been a major force behind the inflation of recent years.

As the table below[1] shows, in fiscal year 1962 the Federal budget exceeded $100 billion for the first time in history. By fiscal year 1971 it exceeded $200 billion. By fiscal year 1975 it exceeded $300 billion, and a figure of $423 billion is in prospect for fiscal year 1977 without some restraint—a fourfold increase in just 15 years. Federal Government outlays increased at an annual rate of 6.6 percent during the period 1961–66, at a 9.4 percent per year during the next 5 years, and at 11.8 percent per year from 1971 to 1976. If fiscal year 1977 expenditures are permitted to grow to $423 billion, the rate of growth will reach 14.3 percent.

For the past 10 fiscal years expenditures grew 175 percent while total GNP increased about 120 percent—that is, the rate of growth in Government outlays was nearly 50 percent greater than that of the economy itself, with all of the attendant inflation and financial consequences.

As the President reviewed these figures in developing the decision which he announced on October 6, he became increasingly convinced that a dramatic and permanent shift in direction was called for. Facing another huge budget deficit in fiscal year 1976 of close to $70 billion, he concluded that without a significant reduction in the growth of Federal spending a high and damaging rate of inflation would reappear, with all of its resulting harm for our economic system and the living standards of our people. Inflation was a major factor in causing the sharp recession from which we are now recovering. A resurgence of inflation, which could readily be spurred by escalating Government spending, will hurt our otherwise brightening economic prospects and could well cause an even more serious recession later on. As President Ford pointed out in speaking of the Federal deficit:

> Over the years, these excesses have played a major role in driving up prices, driving up interest rates, and holding down jobs. We do not have to look far for our underlying problems. Much of our inflation should bear a label: "Made in Washington, D.C."

In designing his proposal, the President realized that the magnitude of the deficit is so great and acceptance of its size and growth so institutionalized that no action could restore a balanced Federal budget in a single year. He therefore chose to attack the program in stages. For fiscal year 1977 he proposed to hold the deficit to $40 to $44 billion. In effect, this would amount to a deficit level in fiscal year 1977 equivalent to the fiscal year 1975 figure. It is noteworthy that if fiscal year 1977 expenditures could be held to $395 billion, the increase over 1976 would be 5.4 percent, about the same rate of increase as prevailed during 1961–66.

If we were able to achieve this goal through cooperation with the Congress, it would be our objective in succeeding years to seek such additional budget reductions as are necessary to achieve a balanced budget in a 3-year period and then to strive for budget surpluses at high employment.

These budgetary goals can be achieved only if we tie tax reductions and expenditure reductions together.

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[1] See p. 37.

THE TAX REDUCTION ACT OF 1975, THE HOUSE BILL (H.R. 10612), AND THE PRESIDENT'S PROPOSALS

The table below presents in summary form a comparison of the income tax provisions in the Tax Reduction Act of 1965, the House bill—H.R. 10612—and, the President's October 6 proposals.[1]

PERSONAL TAX CUTS

These provisions of the President's proposal have two important aims: First, to extend the tax reduction of 1975 for everyone; second, to begin the difficult task of realining the tax rate structure to relieve the middle income taxpayer of onerous tax burdens on industriousness and thrift. Because of rising productivity, but more particularly the effect of inflation on nominal money incomes, families comprising the middle and upper middle classes of society have been moved up the tax scales to positions previously occupied by on the top 1 or 2 percent of American families. As a result, the middle-income taxpayers find that larger and larger tax bites are being taken from their paychecks and entrepreneurial incomes. The rewards to enterprise, to sustained effort, to the accumulation of capital, of this group have been eroded. As we all benefit from the vigor of this group, so are we hurt when its vitality is threatened. The President's program aims to reverse the trend, by providing relief to the middle-income taxpayer while at the same time, more than preserving the gains of the lower income taxpayer.

To accomplish this reversal, the proposal combines carefully balanced changes in the basic elements of the income tax structure—bracket rates, personal exemptions, and standard deductions. Altogether, as you can see in table 4,[2] in all income classes up to $20,000 the share of tax reductions exceeds the share of tax burden under 1975 law. Moreover, taxpayers with incomes under $15,000, who presently pay 28 percent of personal income taxes, will receive 53.3 percent of the additional tax reduction proposed by the President. At the same time, the maximum level of tax-free income is raised for both single and joint returns.

The differences between the President's proposal and the House bill may be seen most clearly in tables 10 through 19 [3] which indicate the tax liabilities under 1974 law, 1975 law, and 1976 law, as proposed, for taxpayers with various income levels and family sizes. The vast differences accorded families with two or more dependents and moderate incomes are particularly striking.

In summary, the President's tax recommendations for individual tax reductions are simple to understand and generous to virtually all taxpayers. I strongly urge the enactment of this comprehensive and equitable package as an important component of the total expenditure restraint and tax reduction program.

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[1] See p. 38.
[2] See p. 48.
[3] See pp. 54–63.

BUSINESS TAX CUTS

Let me turn to the proposed business tax cuts.

The Tax Reduction Act of 1975 increased the nominal rate of the investment credit to 10 percent from 7 percent—4 percent in the case of utilities—for the years 1975 and 1976. H.R. 10612 extends this period for 4 more years, through 1980. The President's proposal would make the increase permanent. It is well known that any tax provision intended to encourage investment is most effective when investors may regard it as permanent, for then they may take it into account over the full range of their investment planning horizons frequently 10 years or longer. As part of a program of structural fiscal change, the investment credit helps to offset the anticapital formation bias of the Federal tax system and should have permanent status.

The Tax Reduction Act, for the year 1975, raised the corporation surtax exemption to $50,000 from $25,000, and lowered the tax rate on the first $25,000 of taxable income from 22 to 20 percent. H.R. 10612 extended this tax reduction 2 additional years. Again, the President's proposal would make this change permanent.

In addition to this modification of the corporation tax schedule, the President proposes to reduce the top rate two points so that the maximum applicable tax rate would be 46 percent. Until we, working with the committees of Congress, can effect integration of the corporation and personal income taxes, this modest relief of the extra burden of tax should cause beneficial increases in the rate of capital formation.

Finally, the President's proposals include a six-part tax incentive program for electric utilities to accelerate the replacement of facilities now made obsolete by the higher costs of fossil fuels and to encourage the application of more adequate capital cost pricing formulas by utility commissions.

WITHHOLDING TAXES

As you are aware, not only will the applicable tax rates change as of January 1, 1976, if Congress takes no action, but also employers will be required to use once again the withholding tax tables in effect prior to May 1975. The Internal Revenue Service has notified employers to this effect and they will shortly be incurring considerable expense to reprogram their systems to implement the higher rates of withholding. If, as we strongly recommend, the President's tax cut proposals are adopted by Congress, prompt notice will be given with regard to the publication of new withholding tables which will take the place of those presently in effect; such prompt notification should be able to spare employers the burden of a double change in the levels of withholding.

The problems of designing a set of withholding tables should not be underestimated, particularly when tax laws are changed in midyear, or when credits in lieu of, or in addition to, exemptions are provided.

THE ECONOMIC IMPACT OF THE RECOMMENDATIONS

Your committee is no doubt concerned about how its action on the matters discussed here today may affect the economic recovery from the recent serious recession. A further concern will undoubtedly be

the long-term implications of any such program with regard to the continuing major problem of inflation. The President's program of tax cuts and spending limitations was designed with these two problems very much in mind.

In considering these matters, you may very well take note of the fact that certain economic indicators have declined in the most recent 2-month report. I recently had occasion to discuss such matters in my testimony on November 7 before the Joint Economic Committee, and I think it appropriate to include my remarks on this subject in the record before you here today.[1]

I then repeat what I said to the Joint Economic Committee that the goals of our economic policy are to slow down the upward momentum of Government spending and to return more of the decisionmaking power and more of the direction of our fiscal policies to the American people. I end by stating:

> Therefore, the President's program must be judged in terms of its long-term benefits since economic forecasts indicate that there will not be significant economic stimulus or restraint in the immediate future as a result of the President's policy recommendations.

CONCLUSION

Certain aspects of our mutual task are clear. The tax cuts which have been proposed by the President in his October 6 message should be adopted. But that is really only the beginning. By simultaneously limiting spending for the fiscal year 1977 to $395 billion, we have the unique opportunity to turn the tide of fiscal irresponsibility which has been engulfing our Nation for at least 15 years.

The President has pointed the way. He has made it clear that if we are ever to provide for stable economic growth and really defeat the extreme economic vice of regressive taxation via inflation, we must immediately join together in imposing a limitation on Federal spending. If this committee will take the lead, I am confident that the Senate as a whole will follow and that of the House of Representatives, if presented with a full opportunity to consider the matter, will join in the required effort to bring an acceptable piece of tax reduction legislation to the President's desk.

Please do not miss this opportunity. Each year that we fail to stem the tide, the task becomes more difficult. Those who misguidedly find it the "easy way" will grow ever more accustomed to turning to Washington for fiscal bounty to attempt to solve every conceivable human problem. We must begin now to halt this trend for the good of those very people who ill-advisedly support its continuance and for the good of the country as a whole.

As always, I thank you for the opportunity of appearing before you and sharing with you my views on these important subjects.

Mr. Chairman and gentleman, I have with me Charles Walker, my Assistant Secretary for Tax Policy, and other members of our technical staff who will be delighted to respond to any questions you might have.

The CHAIRMAN. Thank you very much. Without objection, your statement in full will be placed in the record.

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[1] See p. 42.

I'm going to ask each Senator to limit himself to 5 minutes on the first round of questioning and call on Senators in the order in which they entered the room. Since I was here first, I will ask my questions first.

Mr. Secretary, it looks very much to me as though what we are doing here may be just a complete exercise in futility. The President has said he won't sign an extension of the tax cuts unless we have a spending ceiling for fiscal 1977. Now, this committee has no jurisdiction over that. You can add anything except a constitutional amendment to a revenue bill under the rules of the Senate and the law, but we established a Budget Committee and we passed a law creating a budgetary process whereby the President's budget would be studied and that procedure would enable the Congress to come up with the figure that would be appropriate for 1977. Now, unless I miss my guess, this Congress is going to back the Budget Committees and they are going to say that we gave those people a hard, tough job and we expect them to do it. They in turn have told you and we will continue to say that when they see the President's budget, they will come up with a figure that they think is the amount that this Government should spend in 1977.

Now, the President's spending cuts in any event would not go into effect until October of next year. I thought we could bypass this confrontation by simply saying that we would extend these tax cuts up to the 1st of July and by doing that we could have the President's budget before us, we could see what the Budget Committees recommend, and we could know what we are talking about instead of starting from an arbitrary figure, as far as we are concerned, and working down. Instead of doing that, we would start with a suggested amount for each department and add up that total. Now, the President is not willing to settle for that. He advised his advisers against agreeing to that. I understand all of that.

That being the case, I will be happy to consult with every Senator who wants to consult with me and see what they think about it. My guess is they are going to say that we passed a law to restrain ourselves, to control the amount of spending we are going to authorize up here, and we are going to apply that law to ourselves and do business the way it is set forth in that law.

Now, I can only anticipate that the Senate will say what the House has said already, namely, we are not going to do business that way. That means that the President will veto. His people think they can sustain the veto. And if that is the case, then according to Chase's econometric studies that means that 500,000 more people will be out of work than would have been out of work otherwise. That study also indicates this tax cut would have virtually no impact on inflation during 1976 at all. So, I find myself in a rather difficult position. I could live with the figure the President recommended but it is completely at odds and at variance with the way the Congress has elected to restrain spending. I believe that you are going to find that after we talk it over, almost all Democrats are going to say we ought to proceed in an orderly fashion that we ourselves have provided by law to control our own spending tendencies. And if we do that, it will be a confrontation where either someone will have to back down or the Nation will suffer. And I for one have tried to avoid that kind of confrontation. I'm sorry that my efforts have not prevailed. I don't

think you're the one who created it, but that is how it must be I suppose, and we are just headed in that direction.

Now I usually have taken the view this sort of thing is like playing a game of chicken when two people drive down the center of the highway and whoever moves away from the center line hears the other fellow shout "chicken" as the other car zooms away triumphantly holding the center of the highway. Now I don't think you ought to challenge somebody to a game of chicken if you are going to be the chicken. [Laughter.]

The CHAIRMAN. Now I think I could advise you in a day or two whether Congress is going to call the President's hand and, if they do, either he is going to have to be the chicken or the Nation is going to suffer. That is what is at stake, it seems to me.

Secretary SIMON. Mr. Chairman, I never like to use that term "confrontation" because I like to think we can disagree on issues or disagree on the tactics even though we might agree on what we are trying to accomplish. So I think that basically we can all agree as to the importance of getting our fiscal policy in this Government under control. We don't share the view of some that the economic impact of a veto of a tax reduction of the extension of the tax reduction is that great. A $12 billion tax increase has only a small economic impact in a $1½ trillion economy.

We also haven't felt, Mr. Chairman, that we are destroying or even bruising the integrity of the budget process because consistent with the process, Mr. Chairman, preliminary determinations could be made in advance of the detailed budget analysis, which we are going to be going through starting the time the President submits his budget to Congress in January. All we are asking the Congress to do is to pass a joint resolution to limit the growth in spending. We are not asking for an absolute cut. It is still going to go up by $25 billion. I can just report to you, and it is no surprise that I agree strongly with this and no single issue has dominated more of my time, that the importance of getting the explosion in the growth of spending under control is of paramount concern. And if we don't begin to do it now, we are going to be looking toward some very, very severe problems in this country in the future.

The CHAIRMAN. Senator Fannin?

Senator HANSEN. He had to leave the room.

The CHAIRMAN. Then Senator Mondale.

Senator MONDALE. Mr. Secretary, would it be fair to say that, if I ask you where the $28 billion was going to be cut, you wouldn't tell me?

Secretary SIMON. Well let's say, Senator that I couldn't tell you because I haven't seen the specifies. They worked on a lot of them over——

Senator MONDALE. Are they classified?

Secretary SIMON. No, it is not clasified. In the budget process, if I can explain it to you for a second, the President this year set $395 billion and the OMB set certain targets. They then passed it out to the various departments and we negotiate with the OMB on where we think the tax cuts or spending cuts should be. And at that point in the negotiations, the President makes the ultimate decision. It is not classified. It is a matter of pulling them altogether. That process is going on right now.

Senator MONDALE. So you don't know what goes into the $28 billion?

Secretary SIMON. Not at this particular point. I don't know all of the specifics but as it gets——

Senator MONDALE. But, in other words, you don't know?

Secretary SIMON. Well the OMB worked over the summer, Senator Mondale, on the possibility, on the practicality, if you will, of achieving $28 billion in cuts. And, indeed, they identified areas that could readily be cut as far as the growth in spending is concerned. That is why we picked the $28 figure.

Senator MONDALE. As you are probably aware, the Budget Committees up here spent some time with Mr. Lynn trying to get him to identify where that mysterious $28 billion cut came from. We were unable to get any answers. So finally the ranking member of the committee on the minority side, Mr. Bellmon, asked him this question, and maybe you will try to answer it——

Secretary SIMON. Will you give me his answer too?

Senator MONDALE. He said this. Mr. Bellmon said:

> If I had an evil political mind, which I have, I might come to the conclusion that it was very convenient to have a tax cut early in an election year and a cut in spending later in that same year.

Now is there some other explanation?

Secretary SIMON. Well, I don't have an evil political mind. Maybe I ought to after having been down here 3 years, but I don't. But the point of the matter on this proposal as to a dollar-for-dollar cut, Senator Mondale, is that this proposal was developed in the Treasury Department in about May or June of 1974. We could never get the mechanics to work out perfectly. There was always a lag involved due to the budget submission and the fiscal year problem. This was compounded by the additional 3 months in the fiscal year this year plus the all-important fact that the President had to get down to a tax reduction extension in October, which he did. And as it came down to just deciding yes or no about a tax reduction, the President's clear vote was no, he didn't want a tax reduction in the absence of getting our growth in spending under control. Mechanically there is no other way to do it. If you can find a way that would start the expenditure cuts sooner, why, that would be fine. There is a small positive effect economically in the first 9 months. But I think we have to look more at the long-term benefits of these proposals and not worry about what will happen in 6 or 7 months but rather——

Senator MONDALE. Don't you think the administration would be on much stronger ground if, in proposing their cuts, they said where they are? Commonsense tells you that, if someone has a list of $28 billion, either it is a totally irresponsible figure or it is not. Yet, after weeks of this shell game, the Budget Bureau still refused to say where the cuts are coming from. Now, you indicated today you don't know. Despite the fact that we have a new budget control process and despite the fact that no one in the U.S. Senate on either side of the aisle even offered a cut of the kind you are suggesting because no one knows what it involves, you are telling us the President is saying: "although I won't tell you where the cuts should come from, I want you to impose this draconian $28 billion spending cut?"

Secretary SIMON. May I just say that I don't consider the $28 billion, Senator Mondale, as draconian when one considers that if present trends continue we will have almost a 15-percent increase in budget expenditures in 1977 over 1976. Even the $28 billion cut, still allows us $25 billion growth in spending. The fact of the matter is that OMB found that the cuts of $28 billion were indeed feasible but then would give various agencies the opportunity to protest, if you will, in some of these areas replaced by other areas of cuts. And that is the process we are going through right now. It all gets pulled together. That is what will happen in the next couple of weeks.

Senator MONDALE. But, in fact, there are some very severe internal debates going on concerning this. There is probably good evidence that Secretary Schlesinger lost his job over this dispute. Don't you think we ought to be privy to these budgetary issues in order to know the wisdom of the Executive?

Secretary SIMON. Oh, Congress is privy to this when the President sends his budget up to the Congress in January——

Senator MONDALE. But we haven't gotten that.

Secretary SIMON. No; but it will be up in January.

Senator MONDALE. But you are asking for the cut now.

Secretary SIMON. We are asking for a joint resolution that would limit the growth in spending to $395 billion and then let us debate what the specifics of the issues are in January.

Senator MONDALE. I think Senator Bellmon's question remains unanswered.

The CHAIRMAN. Senator Bentsen.

Senator BENTSEN. Thank you very much, Mr. Chairman.

Mr. Secretary, I have been around the country quite a bit during the last few months. One thing that is clear to me is that the public is tired of political confrontations between the President and the Congress. They are looking for some responsibility on both sides. I think everyone on this committee wants to see some cuts in Government expenditures, and I want to see them too, but I want to see them done with responsibility. In the past this Congress has not had a way to correlate income to outgo. Finally we have a Budget Reform Act that I strongly support and I want to see it implemented. I want to know where those cuts will be. It doesn't seem to me that it is responsible for us to arrive at some major figure in the way of cuts without knowing where those cuts will be. I want very much to bring about those cuts but I want to know the specifics of the cuts. I want the advantage of having the President's counsel on where he thinks those cuts should be.

You tell me they will be forthcoming in the budget message next year. I want to see the Budget Reform Act in operation. And the Congress with its responsibilities in this matter, the Congress finally is implementing what it is supposed to do in cutting spendng and having responsble spending by this country.

Secretary SIMON. You know, Senator Bentsen, again as I said to the chairman at the outset, I think we are all in agreement. We have to get our spending under control. One thing we tried to do since this proposal was made on October 6, is change the erroneous impression that the President is cutting the budget by $28 billion in fiscal 1977. He is cutting the growth, the increase in Federal spending and he is

trying to limit the increase in spending to $25 billion. That is after an explosion of 40 percent in the last 2 fiscal years. We satisfied ourselves in our preliminary work that $28 billion is feasible as far as an expenditure cut in growth is concerned for fiscal year 1977. Later, we can work out the specifics together.

And I agree with you and with the other people that would like to see the Congress and the executive branch work together in identifying these areas. That is what we are willing to do. We want to do this with the Budget Committees so that we can retain the integrity of these committees, Senator.

Senator BENTSEN. Mr. Secretary, you brought up last Wednesday a point on substantial reduction in tax credits and simplification of the tax code. I think that has considerable merit. Today we have an estimated 6,000 pages in our revenue code and regulations. Two out of five taxpayers have to have outside counsel to assist them in some way in preparing their tax returns. If we could remove many unnecessary tax incentives and loopholes, I think we could cut taxes where the top bracket might be as low as 35 to 40 percent and the bottom bracket might be as low as 10 percent. I think that is one thing we ought to really explore in this committee and see if we can bring it about.

Secretary SIMON. Boy, I would love to see it, Senator Bentsen. I think that this, while it is not a new idea, I think it is an idea whose time has come. If we can indeed have a tax system that does exactly what it was designed to do, that is to be administered with neutrality, simplicity, and equity—and God knows that Americans don't believe it is an equitable system for they believe everyone is not paying their fair share of the taxes—but if we can have that, I think it would be an idea whose time has come. But I will tell you this. This is going to be an explosive political issue because of the self-interests who are protected by subsidies and all of the rest of the so-called loopholes or subsidies that have been enacted by the Congress over the years are going to land with a vengeance. But I would love to see this process——

Senator BENTSEN. I would like to see simplification given a try.

Secretary SIMON. So would I.

Senator BENTSEN. And see if we can't then get our taxes where we would have economic fairness to all the people under the tax system. And people don't believe that anymore about our system.

Secretary SIMON. I agree with you, Senator. I participated in tax reform both as a citizen and banker and now as a Treasury official for the past 10 years. I am convinced myself that really economically speaking we are not going to get tax reform by sending up ad hoc measures because we can't beat the special interests that they effect. Why don't we make it equitable and do it right across the board?

Senator BENTSEN. I think we can get the public behind it.

Secretary SIMON. So do I.

Senator BENTSEN. I think that is a political force we can look for.

Secretary SIMON. So do I.

Senator BENTSEN. Would the Treasury consider sending up that kind of major reform?

Secretary SIMON. Oh, I intend to be discussing this with the President in some detail. We've got an awful lot of computer work to do on this program because as you know, there are many ways to skin a cat

Senator BENTSEN. Is it realistic to say we could get the tax brackets down to the point where we have it at 10 percent at the lowest level and perhaps no more than 35 or 40 percent at the highest level?

Secretary SIMON. Our preliminary computer work is that if you just maintain the standard reduction, just wiping everything else out like special treatment for capital gains and all the rest, you would go from 12 to 35 percent. That is our preliminary computer work. But we've got a lot more mathematical work to do on this program.

Senator BENTSEN. Mr. Chairman, I know you supported this idea in years past, Mr. Chairman. I think the time has come to take another serious look at this about the simplification of the——

The CHAIRMAN. If I might just comment on that? We tried that in 1969. We had a modest beginning in that direction. What happened was the reformers in the Congress took out everything that was going to give business a reduction in the rates to offset a loss of their deductions and tax credits. The reformers took that out. So by the time it got through they had lost their deductions. They had lost their tax credits, and they were stuck with the same high rate they had to begin with.

Now when Mr. Walter Wriston from First National City Bank and those people get through with all of this, they will find themselves paying the same 70 percent that they are paying now without any 25 percent rates. Somebody will say: "25 percent is too much for that little widow to pay with three children so let her pay 5 percent and let Mr. Wriston pay more". Then somebody will say: "that is too much for a working man with five children to pay so let him pay 10 percent and let Mr. Wriston pay more". Then somebody will say: "that is altogether too much for that young couple struggling to get started to pay and trying to go to college at the same time so let Mr. Wriston pay more." And so by the time they get through he will be paying 70 percent again with no deductions simply because he wants no deductions. He ought to be glad the code is 6,000 pages. [Laughter.]

The CHAIRMAN. But that is something we can struggle with later on. We have enough problems to deal with this morning. We will continue this debate at the proper time. Are you through with your questions?

Senator BENTSEN. Yes.

[Senator Bentsen's news release follows:]

BENTSEN CALLS FOR END TO CONFRONTATION, URGES COMPROMISE TO EXTEND TAX CUT

December 9, 1975.

WASHINGTON, D.C.—Senator Lloyd Bentsen (D-Tex.), a member of the Senate Finance Committee, Tuesday said it is time to end the confrontation and seek a compromise that will prevent taxes from going up January 1.

"I've travelled throughout this country and I'm convinced the people are tired of political confrontation," Bentsen said.

"It is important that the President and Congress look beyond the conflict and the controversy and concentrate instead on what it will mean to the individual American if we allow this tax cut to lapse."

"We should seek a compromise with the President to avoid a veto that will cause everyone's taxes to go up at the first of the year."

Senator BENTSEN said that he feels a temporary extension of the 1975 tax cut—perhaps six months—is a workable compromise that could avoid a confrontation.

"Failure to extend the tax cut would impose an unnecessary tax increase on the American taxpayer and threaten economic recovery."

65-992—76——2

"We need to make substantial cuts in spending, but Congress should have the benefit of the President's specific recommendations on cuts so that we can establish a meaningful spending ceiling," Senator Bentsen said.

The CHAIRMAN. Senator Packwood.

Senator PACKWOOD. Bill, ever since last March or April when it was obvious we were going to have $60 billion to $80 billion deficit and coupled with the prospective tax cuts that many of us thought might be extended into the next year there has been a continuing hue and cry about this is going to lead to 10 to 15 percent inflation and extremely high-interest rates. Now I did not support the tax reduction. But that has not come to pass and I'm curious why not. The timetable is off six months. It should have started August and September.

Secretary SIMON. That is not true, Senator Packwood. Let's look what is happening here. Let us just revisit for a moment, (a) what was said and (b) what has happened. What was said was that the real danger of all of these expenditures that we are making occur when the economic recovery commenced and the private demands with business and the consumer and all the rest commenced. Also our extraordinary demands would not allow interest rates to decline as much as they ordinarily would during a recession, during this most severe recession in a generation.

But what happened? Let's not look at the time rate, which is an administered rate, or the short-term bill rate, which reflects monetary policy, because that is a temporary rate if you will. Let's look at the long-term borrowing rate of corporations. Here we have an economic recovery that is about 5 months underway right now with interest rates that are more illustrative of the terminal stage of a boom than a commencement of an economic recovery. You can go back to the record here in this committee and in the House as well and see many economists questioning the Secretary of the Treasury as to "doesn't the Secretary know that interest rates decline if demand declines during a period of severe economic slack, and during this the severest recession?". Well they didn't decline or declined a half of 1 percent at most. And this is extraordinary for any contraction in our economy of the severity that we are having now.

And as the Fed must moderate and surely it must, its monetary policy as economic activity commences, then interest rates, of course, must respond and other people are crowded out. Bells don't go off in the marketplace. People are crowded out every day. All you have to do is look at the statistics of B, AA, and under borrowers who were able to borrow in the second quarter of this year in the long-term capital market. You see 2.7 percent versus 16 percent in 1971, which was a comparable period economically. Nothing has been done to take care of the illiquidity which so many of these corporations suffer from. So that is a short-form answer to what you said. I could develop it in greater detail but indeed we created great damage in the fissures that we put into the system through the tenures of policies that we have had, whether it is REIT's or what have you, and we have created damage through the abuse that was allowed through the creation of those corporations, the pension funds, the illiquidity of the financial and nonfinancial institutions. Yet, we continue to blithely go on and think we will do no damage at all in the system. When I tell you we are heading for big trouble, Senator Packwood. It is probably going

to be after I'm gone, but then you are going to hold hearings for a year to try to find what has happened, and nobody will ever remember what was said. It is just like energy.

Senator PACKWOOD. We are always looking back trying to see what happened. But I can recall you about 18 months ago sitting at this table and your statements and I can recall all the banking economists we have had from Brookings and MIT and Harvard and California and every place, and I can recall statement upon statement from some that we would be in a much worse place right now than we are in terms of high interest rates and inflation.

Secretary SIMON. We are. We have a 10-percent interest rate on the prime rate of corporations and——

Senator PACKWOOD. I'm aware of that. But we were going to be worse off than that, and I don't understand why.

Secretary SIMON. Oh, I don't know anybody or any body of opinion that thought we were going to be worse off than that. I never said that.

Senator PACKWOOD. I have no further questions, Mr. Chairman.

The CHAIRMAN. Senator Haskell? Senator Curtis.

Senator CURTIS. Mr. Secretary, I have listened with interest about the impossibility of cutting the budget because of the timing of the resolution in the Budget Committee. I do not think that should be the dominating thinking. I believe what we need here in the Congress is a will to cut, and the flexibility of the Senate rules is such that we could enact any spending cut that a majority of the Senators wanted to have.

I might make a suggestion as a starter, Mr. Secretary, that if we took the rate of expenditures for fiscal 1974 and added to that the increases already voted in social security and retirement and other disability programs so that none of those would be cut back, we would have a rate of expenditures far below what the President requested.

And the Government didn't stop and the heavens didn't fall in 1974 when our expenditures were $268 billion. We could say to every agency: "You will have to live on the level of your 1974 budget." We could grant them latitude to decide what is the most important. We could still add to that social security benefits and other retirement disability programs that to my mind constitute a valid moral obligation of Government not to cut. I think it also has a moral obligation not to pay them in worthless dollars. But that is a rather disagreeable thing to talk about.

I have a few questions. How many would be removed from the tax roles if we raised the personal exemption up to $1,000?

Secretary SIMON. The President's program anticipates about 2 million people are removed from the roles under that program.

Senator CURTIS. How many people are there over 18 in the United States now?

Secretary SIMON. Well, that can be supplied. I don't know.

Senator CURTIS. That can be supplied?

Supply also the number of individual taxpayers there are and the number there would be afterward. I would like to have that.

Secretary SIMON. I can supply all of that for the record, Senator Curtis.

[The following material was subsequently supplied by the Department of the Treasury:]

The Bureau of the Census estimates that on July 1, 1974, there were 144.6 million persons in the United States 18 years old or over, and that on July 1, 1976, there will be approximately 149.7 such individuals.

Source: U.S. Bureau of the Census, *Current Population* Report, p. 25. No. 601 (October, 1975).

Number of returns with tax liability in 1975

	Millions
1974 law	69.6
1975 law, *without* earned income credit	65.0
1975 law, *with* earned income credit	64.0
House bill, *without* earned income credit	65.0
House bill, *with* earned income credit	64.0
President's plan, *without* earned income credit	62.5
President's plan, *with* earned income credit	61.5

Senator CURTIS. Now, if there is no legislation, when will the existing investment credit expire or revert back to a previous level?

Secretary SIMON. December 31, 1976.

Senator CURTIS. All right. I favor making the investment credit permanent. I think this up-and-down business is unfair to businesses for they are hit at times they cannot improve their plant and their competitor can and vice versa. But we have a year to do that. There is nothing going to happen in 1976, is that right?

Secretary SIMON. No. sir.

Senator CURTIS. Now, if the Congress would agree to limit spending for fiscal 1977 by $28 billion, would the Treasury be amenable to some variation from the administration's proposal as to what should be included in the $28 billion tax cut?

Secretary SIMON. Well, we thought that we put up the most equitable tax proposals for the President recognizing that the 1975 proposal was heavily weighted on the low end and that the middle income, if you will, were neglected, and they are the people that really suffered. We thought that was the fairest proposal. Having said that, Senator Curtis, I also realize that any tax proposal sent up to the Congress is a negotiable instrument. And fine, we would be glad to debate all of these issues.

Senator CURTIS. In other words, if I'm stating the administration's position correctly, is it not negotiable to entertain a tax reduction with a dollar-for-dollar reduction in expenses?

Secretary SIMON. That is correct, Senator Curtis.

Senator CURTIS. But how the tax cut would be distributed after the committees hold hearings and consider these various matters would be a matter that some negotiation and accommodation could be made on?

Secretary SIMON. Yes, Senator Curtis, I would like to have an opportunity to come up and explain in detail why we think ours is the best way. But I recognize that there will always be differences of opinion on that.

Senator CURTIS. Mr. Chairman, I'm not prepared to say that I agree with every detail of the President's proposed cut or anything like that, but I do stand firmly in back of the proposal that you can't cut taxes unless you cut expenditures. I think to do otherwise would lose the confidence of the great majority of the people back home. That is all.

The CHAIRMAN. Senator Ribicoff.

Senator RIBICOFF. Mr. Chairman, I believe that at the beginning you stated a position that the Senate would take. The failure of the administration to take your position is done at their peril and the peril of the American economy. I believe Senator Mondale posed the question that concerns most of the Senators and the American people. We are unwilling to buy a pig in a poke giving any President of the United States, whether it is Mr. Ford or anyone else, a blank check for $28 billion as to where expenditures will be cut. If this administration is not playing politics, then this administration owes the American people and the Congress the obligation for a bill of specifics as to where that $28 billion is coming from. It is unfair to expect that the American people and Congress will tell the President that he can cut expenditures $28 billion, to give him that blank check in the next few days, and then not have the President's point of view until the end of January. So there is a basic obligation on the President's part to tell us where that $28 billion of cuts will come from.

Now Senator Long in his usual fertile mind has given the President an out. In other words if I understand the chairman, he is saying to you that since we have this time difference of mid-December and the end of January, can't we get the same result by continuing the tax reductions for the first 6 months of 1976 and then during that period the President will submit his budget? Our budget committees will go over that budget and the Congress will have the opportunity of examining that budget. And both of us together, both executive and the legislative bodies, can determine where cuts will come from and to what extent.

Frankly, Mr. Simon, as I examine President Nixon's and President Ford's economic decisions and as I look over the statements of his economic advisers, I believe they have been consistently wrong. And for the economy of this country I am unwilling to give the President and his economic advisers a blank check for $28 billion. I would like your comment on that.

Secretary SIMON. We don't feel that asking for a slowdown in the growth of spending from 15 percent to 6 percent roughly is a blank check; $25 billion of growth of spending is still a very large amount.

The President doesn't consider this, as you said at the outset, Senator Ribicoff, an out, if you will. The President feels very deeply, as many people do, that the overriding problem in this country today is getting control over spending. And I think the American people would like the Congress and the administration to work together for the joint resolution, if you will, that can be made for spending $395 billion in fiscal 1977.

Senator RIBICOFF. Well, we are asking you to tell us where that will come from.

Secretary SIMON. As I say, we are going through the budget process right now. I explained to Senator Mondale. I explained that the specifics are not indeed available at this time.

Senator RIBICOFF. If that is a fact, then why don't you take the chairman's suggestion? Since you are going through it and haven't reached any decisions or conclusions, how do you expect us to reach any conclusions? And the chairman has said to you that under those circumstances let's extend this for 6 months to 1976 and then during the period between January 1 and July 1, 1976, together we will dis-

cuss where those expenditures are coming from and you can make your case and Congress can make its case.

The chairman has offered you a proposal that in my opinion is the only proposal that can pass. The failure of the President to accept the proposal of Senator Long means defeat of the President's proposal and the American people will be the ones that will be the losers.

Secretary SIMON. I, Senator Ribicoff, spoke to the President for a long time yesterday afternoon on the possibility of a 6-month extension and otherwise. As I said a little while ago, the President in the absence of an expenditure limitation is opposed to an extension of the tax reduction. Our economic analysis of the impact is negligible. So there we have some——

Senator RIBICOFF. Mr. Chairman, you commented you would talk to different Senators as to how they feel. I'm telling you right now how I feel, Mr. Chairman. You don't have to talk with me in a cloakroom. I will tell you publicly. I back you 100 percent and the other point of view will not have my support.

The CHAIRMAN. Senator Hansen.

Senator HANSEN. Thank you, Mr. Chairman. Despite the fact that it has been mentioned several times already, it seems clearly evident to me that we need to understand one thing. The President is talking about reducing the rate of growth in the Federal budget. I think we need to have that in mind.

I'm amazed that the Senators would have difficulty in agreeing upon this sort of concept, that is, that we ought to be able I think to agree that the Congress of the United States will commit itself to seeing that the growth in the budget does not exceed a certain amount. The Secretary has talked about $28 billion. I think it is simply dragging a red herring across the path of Congress and in front of the administration now to say: "Precisely where do you intend to make these cuts?"

I know that you cannot keep spending more money all the time and not get into deep trouble if you do not increase taxes commensurate with your increases in spending. It is just that simple.

Now it is a very popular thing to get up and say: "We will fund this program and that program." We always choose great names for these programs so that when somebody wants to know how you voted, they don't say you voted to cut back on an HEW program because it happened to be a little too costly. Instead they say: "You voted to deny schoolchildren lunches." They say: "You are for letting little kids go home hungry." That is the way things are couched.

And I have great admiration for Senator Byrd, as I do for every member of this committee, because he has had the courage to say: "Let's face the issue." And he has voted as I think a responsible person must vote in facing up to the fact that if we continue to spend more money than we raise in taxes, we are making it tougher on the poor people of this country to get along. I know a little bit about what I am talking about.

I have seen this happen. I have seen the guy who is in the 70-percent tax bracket, I've seen him get along perfectly all right. You don't need to worry about him. But the person upon whose shoulders most heavily falls the burden of inflation, that person is a person who writes to

Senator Byrd and me and says my $141 social security check won't go around. So then we have to increase those security payments from time to time but we never seem to come to grips with the issues that brings it about.

Now I don't see anything wrong with the Congress of the United States passing a concurrent resolution which says: "We will bite the bullet and we will come forward with a determination upon our part to see that the growth in the budget does not exceed a certain amount of money." We can talk the details over later but the reason we need to agree now upon this basic issue, which I understand is exactly what you are calling for in essence, Bill, is because it is important. And I understand, Bill, that what you are saying is that we are going to see that the amount of the tax cuts that we extend to the people for another year will be offset by a reduced amount in the growth—and I underscore the word "growth"—of the Federal budget.

Let's look at New York City. It is a great thing to say you are for education but almost one out of every three persons on the payroll of the Department of Education in New York City weren't teaching. They were doing something else.

Japan is in deep trouble today. It is going to have to make some tough decisions and they know that. There is a lot of trouble in Japan today. England is in deep trouble. And the one interesting thing about every one of these examples I have cited has been the failure to take the hard position that I think now is called for and that the Secretary is calling for, namely, that they get us out of this morass. And if we don't turn around, if we don't say that we are willing to make the cutbacks on the 1977 budget and commit ourselves to do that now, somebody not too many years from now will probably be trying to analyze what accounts for the decline and fall of the American Republic. And I suspect that on our shoulders certainly will fall a part of that blame.

Mr. Secretary, have I fairly understood the thrust of your testimony here when I say that you are not saying we ought to cut back and spend less money in 1977 than 1976 but rather to slow the rate of growth that you think can be supported and will be economically feasible in the 1977 budget in order to compensate for what we are proposing now to give the people in terms of tax cuts now?

Secretary SIMON. Yes, Senator Hansen. You stated it very elegantly. Could I just add to what you said? I would just add that a tax cut at this point without a simultaneous cut in the growth in spending is an invitation to more inflation and more unemployment. I was taken by an article this morning in the Wall Street Journal because everybody in the Congress and many economists talk about our taking $1 billion a month out of our economy, well, in the Wall Street Journal there was a very interesting editorial this morning, which I would commend to your reading in that they talk about the erroneous economic assumptions that growth is spurred by spending and not by permitting the productive sector, the private sector of our economy, to keep more of what it produces instead of taxing away its output. And then it talks about this erroneous $1 billion a month out of the economy. This is the important part that people just continue to miss, Senator. It doesn't seem to be understood. This $1 billion a month has to be borrowed. And borrowing merely takes the money out of one person's hands and puts it into the hands of another.

So the tax cut extension would keep our economy from faltering, they say, only to the degree that further spending commitments are reduced. Otherwise—and this is one of the points you make, Senator—the Nation is merely postponing with taxes and interest—and I underline "taxes and interest"—what New York City tried over the last decade with uphappy results. So let's just keep piling the debt burden on the American people and then finally you are going to have a collapse, which is what you implied.

Senator HANSEN. Thank you.

The CHAIRMAN. Senator Hartke.

Senator HARTKE. Mr. Secretary, since I completely endorse what Senator Ribicoff has said, it is not necessary that Senator Long must poll me on this matter. Most people will recognize that Congress is not going to do anything except merely extend the present tax cuts. I don't think anybody is being fooled about that.

Anyway, Bill, the fact is that you talked about these erroneous economic theories that the Wall Street Journal refers to and I quite agree with you. After all, Samuelson puts out a book that my kids are forced to study, and he is a Nobel Prize winner, but he doesn't even mention the words "multinational" in his latest edition. He is still back in the 19th century, which shows how up to date these economists are. So I'm not persuaded at all by these economic people.

Now you talk about theories. Senator Curtis asked you a question a moment ago. He referred to a statement you made the first of the year that Government borrowing would crowd out private borrowing. You said that the interest rate is now maintained at a level which is actually unconscionable in a period of economic recovery, and that the rate ought to be consistent with economic prosperity. Is that a fair assessment of your remarks?

Secretary SIMON. Well what I said—well I didn't use the term "unconscionable." Interest rates are determined in the free marketplace by supply, demand, inflation and other factors. What I said—I believe this is what I said—was "that the interest rates in the long-term sector of our corporate market are more illustrative of a terminal state of a boom than the commencement of an economic recovery."

Senator HARTKE. The reason that people are not getting loans is not because of the interest rates, which have dropped significantly. The banks tell us they are loaded with money. The problem very simply is that there is no respectable credit in the marketplace in a period of economic recession. Isn't that true? That is what the banks tell me.

Secretary SIMON. Not really. Again as far as the prime rate is concerned, it is an administered rate. It is a following rate. If we want to use short-term rates, which are even lower, the Treasury bill rates most recently was 5.66 at our auction yesterday. These are responsive to monetary expansion on the part of the Federal Reserve versus the contraction a year ago. And as the recovery commences, obviously everyone knows what happens to short-term interest rates as private demands grow. But when private demands grow, look at what happens to the long-term sector which is where everyone must borrow for their permanent needs for expansion. In paying 10 percent a prime corporation can afford that, even though that inflicts a high cost on the consumer, but think what happens to the lesser borrowers at that

time because the spreads have widened in the flight to quality. You see 12 percent, 13 percent, or not at all.

Senator HARTKE. Well, I have heard this theory entirely.

Secretary SIMON. It is not theory. It is what goes on in the marketplace.

Senator HARTKE. Well, let me contend that it is a theory because you have to guess, and as long as you have to guess, it is a theory. That is a basic fact. That is, if it is not a fact——

Secretary SIMON. Well, I didn't say "if."

Senator HARTKE. "If" is a theory. All I'm saying is that bankers today tell you there is plenty of money. What they tell you is that the creditworthiness out there is too shaky to loan it to the people.

Let us touch on another matter. You said that 2 million people who are presently on the tax rolls would be removed by the President's program. Is that not right?

Secretary SIMON. I think it was 1.5 million.

Senator HARTKE. All right.

Secretary SIMON. Yes, sir.

Senator HARTKE. Two million roughly. The fact of it is that if you take the House bill or any other alternative that is proposed in front of the Congress today, 4 million people would be removed from the tax rolls as a net result. Don't you agree?

Secretary SIMON. No.

Senator HARTKE. No? Well, Larry Woodworth says yes. He is my expert. Who is yours?

Secretary SIMON. Our figure is that it is in excess over the House bill——

Senator HARTKE. Let's put his name in the record so we will have that.

Secretary SIMON. Bill Goldstein.

Senator HARTKE. Bill Goldstein versus Larry Woodworth.

Mr. Secretary, what really disturbs me is——

Secretary SIMON. Here comes Larry back again.

Senator HARTKE. Larry, remember what you told me about the 4 million people?

Mr. WOODWORTH. 4.6 million.

Senator HARTKE. Pardon me, I meant 4.6 million. The one thing that really disturbs me is the fact that I see in the Congress and the administration this perpetuation of a myth: That is, very simply, that the Congress spending is the cause of inflation.

Secretary SIMON. May I get back to the——

Senator HARTKE. Oh, we will argue that later.

I wanted to refer you to a report, which I don't think can be controverted, that the Federal debt has consistently gone down every single year since 1946 percentagewise in relation to the gross national product. Individual and corporate debt has gone up every single year. State and local debt has gone up every single year. In view of that situation how can you really contend that it is the Federal Government that is at fault?

Senator HANSEN. Mr. Chairman, reserving the right to object, and I won't object but only let me ask you one question. Percentages always confuse me. Now when I was in school, if you reduce a figure of 12 down to 7, it wasn't really a 100-percent reduction; it was nearer 40

percent. I don't know whether we figure on the same percentages basis but——

Secretary SIMON. If I may, Mr. Chairman, and recognizing the time, but I don't want to miss this point. I had a paper prepared in the Treasury, which I would like your permission to submit for the record.

Senator HARTKE. On what?

Secretary SIMON. On this percentage business.

Senator HARTKE. On the debt?

Secretary SIMON. Yes.

Senator HARTKE. These are your figures.

Secretary SIMON. I know and it is on the simplistic assumptions that you make as a result, is not out of line indeed. I want to submit this because it ignores the financial implications, which as Paul McKracken has said, academic economists have traditionally done[1] and——

Senator HARTKE. Let me tell you that this is not nearly as simplistic as the approach that the President used in Grand Rapids. Just for your own information, the figures I gave you on the number of people removed from the tax rolls comes from Treasury's computers, according to Mr. Woodworth.

Secretary SIMON. As compared to what? As compared to the 1974 law? Is that what we are talking about?

Senator HARTKE. Mr. Woodworth said any alternate plan. I just accept his statement. He has been pretty good around here.

But let me come down to this. The present rate on the gross government and private debt related to gross national product at this time in 1946 was 107 percent. It is now down to 35.4 percent in 1976. The individual private debt went from 73 percent to 173 percent, while the State and local debt went from 7.9 percent to 14.7.

And all I want to say to you is that if you put people back to work, or half of the people back to work, you would reduce all of this question that you have about a deficit. And I just think the emphasis is in the wrong place. I would like to go on further but my time is up.

The final passage of the ERDA bill conference report is on the floor. Do you want to start, Senator Roth?

Mr. Chairman, you are back. Senator Roth is next. Do you want to proceed Mr. Chairman or not?

The CHAIRMAN. I suggest we just go on ahead if we can. The Senate is voting all the time anyhow. You go and vote if you want and we will just play musical chairs.

Senator ROTH. Should I proceed, Mr. Chairman.

The CHAIRMAN. Yes.

Senator ROTH. Mr. Secretary, as I'm sure you are aware, I am a strong supporter of the idea of trying to get a balanced budget and the increase in the budget under control. I do have some concerns. You were good enough to be in Delaware last night. You probably had an opportunity to talk to a number of people there. One of my concerns is the state of our recovery rate at the current time. I understand in your earlier testimony that you don't feel that the continuation of the tax cut would have that great of an impact. I'm not an economist but it

[1] See p. 67.

does seem to me that we have a question of confidence at the present time.

In my own State, for example, at least one large corporation has been trying to cut out the large Christmas bonus for all of its employees. It bothers me to hear it said the tax cut will have no impact today. And for that reason, particularly when you have people like the Chase-Manhattan Bank and other economists disagreeing, don't you feel that the tax cut would be at least one measure to help build confidence in the consumers and others?

Secretary SIMON. Senator Roth, I must admit I never worry about economists disagreeing. I would be worried if they didn't. I think that confidence is a critical factor. But in weighing both sides of the equation, let's look at what it means from a strictly economic point of view as far as real growth and inflation are concerned and, indeed, what will happen if we increase or, I should say, extend the reduction and just continue to spend as usual. A $53 billion deficit is where we stand now and that assumes that nothing else is going to happen for the next 1½ years. Now, what happens to the American people and the confidence of the American people? Today, our society has deeply ingrained inflationary expectations. I believe it would refuel the inflationary expectations and refuel inflation and just bring us to even worse economic problems and another recession and even higher unemployment.

Senator ROTH. Well I'm for the budget cuts. I don't quarrel with that. I think it has been improperly called a budget cut and is more properly a slowdown in growth. I'm all for that.

But it does bother me, as one who has been very active in the creation of the budgetary process, that we can't work some way out of this confrontation, if that indeed is what it is going to be. The chairman has made one proposal. I'm curious as to what the President's reaction would be if our legislation included some kind of a concurrent resolution that directed the Budget Committee to come up with a budget at the level requested by the President. Would that satisfy the requirements of the executive branch? In other words, to extend the tax bill for 6 months and direct our Budget Committee to come back with a budget at the level the President has requested. This would force the Budget Committee to come forward with recommendations as to major cuts in spending.

Secretary SIMON. The President has said, Senator Roth, that this would not satisfy him. All he is asking for is an expression of congressional intent via a joint resolution of Congress.

Senator ROTH. Well, this bothers me, frankly. Last year I won approval for a 10-percent cut in travel across the board and the executive branch came back and said they couldn't live with that. So we are going to propose this afternoon to a supplemental appropriation bill that a concurrent resolution be passed directing the executive branch to come up with a plan for cutting 10 percent of travel costs.

I just feel that one of the problems in the economy now is the uncertainty, and that somehow we ought to try to work out of this economic uncertainty. Let me ask you a question along a different area. Very frankly, I am very concerned about the middle-income people. I think that this country could very well face a revolt in the near

future if we don't do something about the tax burden on middle income taxpayers. It is not business really, it is not the wealthy, it is certainly not the disadvantaged that are paying the taxes. It is the middle-income people. They get none of the benefits under Federal programs when it comes to colleges, houses, and all the other things. They are not the ones that are the beneficiaries. I think as we talk about tax cutting, we ought to pay a great deal more attention to relief for these people. I wonder what your views are. I know you have some reference to this in your statement. I think it is worthwhile to go over that again.

Secretary SIMON. Yes; I did, Senator. When we testified initially on the tax reduction, the President set a cap, if you will, on the reduction at that time, and the headlines, the next day, said: "Simon proposes a tax cut for the rich." You know that is the perspective everybody gets as a result of it. And we feel strongly that the middle income has borne the brunt. They have borne the brunt of the inflation problem by being pushed into higher brackets and having their real earnings eroded. And our tax proposal, Senator Roth, will direct itself to that. By making sure that the 1975 tax reduction does not penalize the lower end, and indeed assists most of them, but that the additional moneys are put into that $10,000 to $25,000 class.

Senator ROTH. If we don't act, I think that is where the next revolt will come from.

I have one final question, Mr. Chairman. Amongst my own taxpayers at home there have been considerable complaints on the part of the individual taxpayers that they aren't receiving adequate help from the Internal Revenue Service and that when it comes to an audit, they aren't told what their rights are. I feel very strongly, Mr. Chairman, that something should be done in this area. I wonder if you would care to comment on this proposal? There was a study made recently by the Administrative Conference of the United States that charged that the Internal Revenue Service's treatment of the American taxpayers is: "frequently whimsical, inconsistent, contradictable, and highly impersonal." For that reason, they come out in support of legislation along the same thrust which I have introduced to expand taxpayers' assistance. I notice they recommended that it be independent of the IRS. I wonder if you would care to comment?

Secretary SIMON. It is pretty difficult really to make them independent because the fellows who are trying to help the American people with a complex tax form ought to have a great knowledge of the subject. I think it would be just the opposite.

Senator ROTH. I hate to interrupt but I do have a vote. I would like to call a 5-minute recess and reconvene at the end of 5 minutes.

[A short recess was taken.]

Senator HASKELL. How are you, Mr. Simon?

Secretary SIMON. Very good. How are you?

Senator HASKELL. I gather that Senator Long would like us to proceed and ask any questions that we have. Actually, Mr. Secretary, I only have one question. I have to go over to the floor because the ERDA budget bill is on the floor. I won't ask you whether the President is going to veto that because that isn't on the agenda here today. Did you in your testimony indicate where the administration would like the Congress to cut $28 billion out of the budget?

Secretary SIMON. No; as I explained, Senator Haskell, this has been one of the problems due to timing. In October, the President had to address the economic aspects of extending the tax reduction. He clearly favored not having an outright extension for economic reasons. If we were to have an extension it should be made permanent for certain reasons, he suggested, because recognizing the inflation problems and the terrible economic problems the American people have, it could only be done accompanying it with a like cut in expenditures. And that is going on now. That process is going on in the executive branch of Government right now as all of the various agencies are identifying the areas to achieve $395 billion limit the President is going to send to the Congress.

Senator HASKELL. I'm sure—and I'm saying this for the record because sometimes I think we go through a medieval ballet in this hearing process—but let me say this.

Really, Mr. Secretary, just for the record, it seems to me a little bit—well, I don't know whether presumptuous is the kind of word you should use in referring to the President of the United States or not, but I can't think of another one. It seems presumptuous to say we are going to have a huge tax cut, and that is going to be keen, but at the same time to say we are going to have a $28 billion expenditure cut and then not let us know where. Now that is a statement and not a question, Mr. Secretary. I realize your position.

Senator Mondale, do you have a question?

Senator MONDALE. Was I hearing earlier in your testimony something that could properly leave me to believe that there is a question in your mind as to whether a tax cut is even wise? The reason I ask that is that I thought I heard, and I recall stories that speculated that one of the reasons for this scenario we are going through is to provide a justification for blocking an extension of the temporary tax cuts?

Secretary SIMON. No; I would like to see, Senator Mondale, an extension and indeed the inclusion of the additional amount for all of the reasons I mentioned to Senator Haskell; for not only the outright economic reasons, the inflation of recent years, the fact that I basically believe the decisionmaking should be given back to the American people and all of the things you heard me say before. But I think the overriding consideration is that in the absence of a cut in the growth of spending, and not an absolute cut again, but I think it would be extremely dangerous to have an extension of the reduction. Because while it might show a very slight increase in real growth if you will, versus nonextension of same, I think we are flirting with the resurgence again of the inflation and the inflationary expectations and all the problems we have had in the last couple of years.

Senator MONDALE. One of the perplexing aspects of the President's proposal is that as a member of the Budget Committee, we worked on the President's budget, we worked off the President's budget. That was our point of departure. We spent weeks of hearings. We spent days inquiring of the administration and other witnesses. We went through the process, which you know will probably be completed tonight. And the Congress under the new Budget Act which the President has placed, will have set budgetary feelings for the coming fiscal year including what remains of fiscal year 1976. If someone offered the amendment that you are asking here on the floor, he would be subject

to a point of order. I mean we have gotten that far. So I don't see how you can take the position that you are taking without really at the same time demanding a fundamental reform of the Budget Act and the budget process.

Secretary SIMON. Well there is a difference of opinion——

Senator MONDALE. No, no, there is no difference of opinion on a point of order at all. That happens to be the law. I happen to know what I am talking about.

Secretary SIMON. I brought that up and it was explained to me that there is a difference of opinion on that, Senator Mondale.

Senator MONDALE. No there is not. Does anybody argue that it——

Secretary SIMON. All right, Senator Mondale, let's assume that your statement is correct. The President considers the issue of the growth of spending—that explosion in spending—as by far such an overriding issue that in this instance a joint resolution the part of Congress, even assuming that that is correct, is indeed called for because it is in the best interest of our country.

Senator MONDALE. Well it is interesting then that while we hear the talk of the budget cut, during this same process practically every week we receive supplementary requests, judgments, upward in the request for budget ceilings from the administration. So we seem to have one system demanding that the budget say, accommodate several billion dollars for the Middle East or several billion dollars for New York or several billion dollars for ERDA, tremendous pressure to try to resist cuts in the Defense budget, and that is the specific kind of pressure we get from the administration and that is what we have to deal with on the budget committees. Now how do you explain that two-track system?

Secretary SIMON. You notice there is always going to be difference of opinion obviously where spending should or should not occur. There are always going to be events that are going to happen, such as New York City events that are going to change priorities, if you will. That is just part of the spending process and it always will be.

Senator MONDALE. Why are you capable of being so specific on spending increases? And incapable of being specific on budget cuts?

Secretary SIMON. Because you are talking about specific events as far as the spending increases are concerned and we will be specific as far as the expenditure reductions are concerned and that is what we are working on right now. And when the President makes all of those decisions, he makes them with the help of the Congress.

Senator MONDALE. One final point. What is the reason for the consistent opposition of the administration toward the low-income workers' supplement? It seems to me this ought to be something you should support. We have millions of people in this country that are working at incomes that are right at the welfare level. And if they took a pencil, they would find that they would be better off just to quit working and go on welfare. So what we decided to do, and a few of us in the Senate have taken a strong stand on this, is to return to those low-income workers with families the equivalent of the payroll tax to create an incentive for them to continue to work. And if the administration gets away with its point of view in the extension, we will increase the taxes on those same low-income workers. Somewhere between $300 and $400. Does that make sense to you?

Secretary SIMON. You know, you have to make sure when addressing the administration's position, and what you are talking about is the earned income credit, in remembering that the earned income credit is not in the Ways and Means bill. The President has felt the earned income credit should be dealt with as part of the whole subject of welfare reform, rather than on the tax side of it.

Senator MONDALE. No, they are not on welfare. They are working. They are trying to work——

Secretary SIMON. It is a payment and not a reduction in revenues, which taxes, of course, are. We want to deal with the earned income credit, which we think can rightfully be called a welfare payment. We want to deal with that in the overall context of welfare reform.

Senator MONDALE. But you are taking it away and are creating a disincentive for Americans to work and you are imposing a cruel hardship on Americans I think, who ought to have the greatest respect of all because they continue to work, even though at most marginal incomes. That is why I cannot understand how you square the rhetoric of work versus welfare with a policy that I think is telling people to quit working.

Secretary SIMON. Well again, we want to deal with this issue as part of the overall issue of welfare and not in the tax structure.

Senator MONDALE. I won't get into a debate as to why a tax preference for business is considered a tax cut and why a tax preference for working people is considered welfare. That is another debate.

Secretary SIMON. When one looks at the total welfare program, the overlapping one that you alluded to at the outset, then we have to remember also that business in this country still provides 85 percent of the jobs.

Senator MONDALE. Oh, yes, and I'm all for it. But I can't understand this rhetoric by which we shift taxes in order to encourage people to work and that has to be called welfare. For example this 10-percent tax credit, that is a business incentive because everyone knows welfare is the worst word in America. Well thank you, Mr. Chairman.

The CHAIRMAN. Senator Byrd.

Senator BYRD. Thank you, Mr. Chairman.

Mr. Secretary, what is the estimate of revenue for fiscal 1977?

Secretary SIMON. We will find it. It is in one of these books, Senator Byrd. I hope you don't get penalized on your time limitation—$350 billion.

Senator BYRD. Now is that with or without the tax reduction?

Secretary SIMON. That is assuming the resident's program goes through and that it is consistent with the $395 billion spending ceiling—$40 billion to $45 billion deficit we spoke of.

Senator BYRD. That is assuming a ceiling. Well, that doesn't have anything to do with the ceiling but it is assuming that the President's program of a $28 billion tax reduction is offset?

Secretary SIMON. That is extension, and I'm told by my experts, of the present law, Senator Byrd.

Senator BYRD. The extension of what?

Secretary SIMON. The revenues would be the $350 billion.

Senator BYRD. Now if the present law is not extended, what would be the estimate of revenue?

Secretary SIMON. Between $10 billion and $12 billion more. We are looking for the exact figure now out of the revenue estimate.

Senator BYRD. Well then if I understand it correctly, the administration proposes outlays of $395 billion?

Secretary SIMON. Yes, Sir.

Senator BYRD. And it proposes revenues of $350 billion?

Secretary SIMON. Yes, Sir.

Senator BYRD. So that the administration envisions and is prepared to recommend, as I understand those figures, a deficit of $45 billion.

Secretary SIMON. That is correct, sir. Approximately recognizing that revenue estimates are tenuous at best.

Senator BYRD. And the only figure I need, which you can supply later, is the one that you are looking for. Thank you. That is my only question, Mr. Secretary.

[The Department of the Treasury subsequently submitted the following information:]

FISCAL YEAR 1977 RECEIPTS

In fiscal year 1977, receipts are estimated to be $354.6 billion under the President's program and $367.9 billion under the extension of the Tax Reduction Act of 1975, a difference of $13.3 billion.

Senator BYRD. Mr. Chairman, I would like to ask unanimous consent to insert in the record at this point or the appropriate point the editorial from the Wall Street Journal which the Secretary mentioned earlier.

The CHAIRMAN. Without objection.

[The Wall Street Journal editorial referred to follows:]

[From the Wall Street Journal]

THE KREMLIN AND KAPITAL HILL

The Soviet Union is blaming its horrendous harvest on bad weather, but even the record Soviet crops in the years of glorious weather aren't as bountiful as failed crops in the United States. As part of our policy of giving free advice to countries with whom we are peacefully coexisting, we recommend that when the 25th Soviet Party Congress convenes in February it consider a change in agricultural tax policy.

The problem the Russians have, similar to that of the British and the liberal Democrats of the 94th Congress, is that they do not understand the incentive effects of marginal tax rates. The Russians produce 75% of their food on their collective farms, which have an effective marginal tax rate of about 90%. That is, the collective that produces 1,000 bushels of wheat gets to keep 100. If it works like the devil and produces 2,000 bushels, it only gets to keep 200, even though the first 1,000 are easy and the second 1,000 are tough. The Russians produce 25% of their food in private plots, backyard gardens that the collective farmers work in their spare time. They can keep all of what they produce in these plots.

The obvious solution, it is clear at least to us, is for the Soviets to permit an increase in the size of the private plots and a reduction in the size of the collectives. The net effect is to cut the marginal tax rate for farm production in the aggregate. For every acre the government gives up, there is a "revenue" loss of 90% of what would have been produced on it, but so much more food will be produced on the plot that there will be that much less the Kremlin will have to buy from us.

We offer the same advice to the British. They must increase the size of their private plots, figuratively speaking. Workers in the lowest taxable income classes now pay a marginal tax rate of 35% on wages, and this goes to 83% for the highest income classes. The marginal tax rate on interest and dividends rises

steeply to a top of 98%. The country is smothering incentive and growth with these incredibly high rates, and should be aggressively turning over public acreage (reducing government spending) to private plots (lower marginal tax rates).

The United States economy to a lesser degree is being depressed by high marginal tax rates, and the problem is being intesified by the failure of Congress to appreciate the importance of their adverse incentive effects. President Ford has proposed the correct solution, cutting $28 billion in taxes and reducing projected government spending by $28 billion, which by our analysis would spur non-inflationary economic growth by converting public, collective disincentives into private incentives.

The liberals in Congress, though, act on the erroneous economic assumption that growth is spurred by spending, not by permitting the productive sector to keep more of what it produces by taxing less output away from it. The tax bill the House passed last week extends the 1975 tax reduction on the grounds that failure to do so would withdraw about $1 billion a month from the public's spending power. But because this $1 billion a month has to be borrowed, it merely takes money out of the hands of one group and puts it in another. The tax-cut extension would keep the economy from faltering only to the degree that future spending commitments are reduced, otherwise the nation is merely postponing taxes with interest, which is what New York City tried over the last decade with unhappy results.

The House not only rejected the President's approach, but tacked on some "reform" measures that purport to raise an extra $1.5 billion in taxes by closing loopholes that benefit the "rich." Conceptually, loopholes are similar to the private plots in the Soviet Union, providing incentives for people to put forth extra effort that would otherwise be discouraged by the high marginal tax rates. In the name of "equity," congressional liberals thus close off production incentives to the higher income classes, theoretically the most productive of all income classes. What would be the effect on Soviet agriculture if the Kremlin took away the private plots without reducing the tax rate on the collectives?

These are the reasons President Ford must veto the tax bill, as he said he will, if it comes to him in the form in which it passed the House. Adding up the benefits of the cuts to the absence of a spending ceiling and the disincentives of the reform measures, the net effect of the legislation would be to damage the economy further. It would make the national economy more like New York City's, more like Great Britain's and more like the Soviet Union's. In these terms, President Ford could successfully defend his veto with the public, if not on Capitol Hill, all the way to November.

The CHAIRMAN. Senator Hartke.

Senator HARTKE. Would the Senator yield, Mr. Chairman? I would like to know where the figures came from that you just gave to Senator Byrd?

Secretary SIMON. From the Treasury Department.

Senator HARTKE. Are they in this book [indicating]?

Secretary SIMON. I think so.

Senator HARTKE. I just think they are wrong. That is the only reason I raise the question.

Secretary SIMON. Our revenue estimates? I know you don't mean that they are always wrong, but——

Senator HARTKE. No, I just think you quoted incorrectly from your estimates.

Secretary SIMON. Well, they are looking at the book when they give me the numbers, Senator Hartke.

Senator HARTKE. Well I just think——

Secretary SIMON. Here it is.

[The Department of the Treasury subsequently submitted the following information:]

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FISCAL YEAR 1976 RECEIPTS

Unified budget receipts in fiscal year 1976 are estimated at $296.7 billion under the President's program and $301.2 billion if major provisions of the Tax Reduction Act of 1975 are extended along with changes to maintain the average rate of withholding. Thus the President's program costs an estimated $4.5 billion more than extension of the Tax Reduction Act of 1975, after taking into account secondary effects on the economy.

Senator HARTKE. Oh, no, that is all right, if they are correct.

Secretary SIMON. This is from the OMB Fall Review, from the Unified Budget Receipts.

Senator BYRD. That would mean the receipts are estimated to increase by $50 billion, which is about 15 percent, I guess.

Senator HARTKE. OK. Mr. Chairman, I don't want to delay this, but it is my understanding that you gave an estimate of $350 billion and your report here shows $363 billion. You did say for fiscal year 1977?

Secretary SIMON. I don't have that in front of me right now, but I responded to Senator Byrd. The increase meant no extension and that is what the estimates would be, Senator, approximately $12 billion higher. That would come out to that number.

The CHAIRMAN. Mr. Gravel.

Senator GRAVEL. I would just like to pursue the same point Senator Byrd was making. The figure in the deficit is $45 billion and then this year's deficit is estimated at about $70 billion. Well, why did the administration come up with a figure of $28 billion? In other words, why not $40 billion or $45 billion?

Secretary SIMON. We did not go into this exercise this past summer with the OMB with a specific number in mind as to what we would attempt to cut back. When we looked at the various growth and expenditures that were going to occur through increased interests, through military retirement pay and all the rest of it, we looked at what was reasonable and what was feasible and what possibly could be cut from the growth in spending with an eye toward achieving a balanced budget. And we recognized during this exercise that it couldn't be done with really Draconian cuts, if you will, in a single year. And then on the economic assumptions that our economy would grow by x percent per year, we recognized that it would take us 3 years even if we accomplished the $395 billion spending ceiling.

Senator GRAVEL. To get a balanced budget in 3 years?

Secretary SIMON. Yes, sir.

Senator GRAVEL. Do you feel—and I'm a little confused in your response—that the joint resolution, if we passed it, would be legally binding on the Congress or would it simply be psychologically binding?

Secretary SIMON. Well I'm not a lawyer, Senator Gravel, but the President has asked for a joint resolution that stated $395 billion, which is roughly what we have agreed to in the Congress, and I believe that would be satisfactory. Whether it would be legally binding or not I could not answer.

Senator GRAVEL. The point I raise there is that the administration faces this problem every day of the year. Something comes up and you come in with additional requests. The Congress also faces this in some situations—I mean, we didn't know in January that we were going to

have to come up with $2 billion or more for New York. We didn't know that. We don't know what is going to happen at the end of March.

Secretary SIMON. And, of course, that is a wash program because they pay us out of tax receipts.

Senator GRAVEL. Well, I just use that as an example. We don't know what is going to happen next March or next June. So if you try to play a game of binding either in legal terms or in psychological terms, of binding the Congress it is really to no avail. We have a mechanism, as you are well familiar with, which is the budget mechanism that we have set up. We have sort of an overview of it. Why not just let that work its will as events occur in the course of next year?

Secretary SIMON. You know we are all aware of the contingencies that occur during the course of a year that require joint action on the part of the executive and legislative but that would be just an add-on to an already explosive growth of 15 percent if we didn't attempt to slow down the growth. That is the purpose of this whole exercise. Probably there would be some programs. Hopefully there wouldn't be. But if there were, we could find other areas to cut. What is important is to begin to identify priorities for our spending so that it is out of control.

Senator GRAVEL. You say we must have a resolution but you are dubious about the legal value of it?

Secretary SIMON. No, I didn't say that. I'm not knowledgeable of what the legal value of the joint resolution would be as far as whether it is binding.

Senator GRAVEL. Well, I think we are confused on our side. I wonder if it would be wise just to go through the normal process.

Secretary SIMON. Well there is still a 6-percent growth in spending from 1976 to 1977, of $25 billion spending after the nearly 40-percent growth in spending 2 years prior to that. So we have to get a handle on this.

Senator GRAVEL. I appreciate that the growth is based upon the judgments of the administration. And if the Congress is truly going to be in a position to appropriate the money, we must exercise our judgment also.

Secretary SIMON. Sure.

Senator GRAVEL. So you may have differences of judgment in that regard.

Secretary SIMON. And we do.

Senator GRAVEL. So why should we use your criteria of a certain sum cutback as our criteria when we are charged equally under the Constitution to discharge our fiscal responsibilities?

Secretary SIMON. Of course, it is your responsibility. The point is to attempt to achieve a cooperative agreement on limiting it at a sensible number. Then we can work on the specifics later.

Senator GRAVEL. Could not that be binding concurrently as events develop in the course of 1976?

Secretary SIMON. It would be nicer if it could, yes, and it would be easier, Senator Gravel, if we could do it that way, but unfortunately the President had to make a decision on the tax reduction extension in October. And he had to face the spending level at that time or felt it imperative that he face it at that time.

Senator GRAVEL. Thank you.

Senator HARTKE. Mr. Chairman, I would just like for the Treasury Department to verify the figures again.

Secretary SIMON. Sure.

Senator HARTKE. And all I would like to do is call attention to the figures the Secretary is using on the estimated unified budget receipts for October 3, 1975. My understanding is that your answer probably should stand corrected because, with the present tax cuts in effect, the November 10 current services estimate for fiscal year 1977 show an estimated $372.6 billion figure of revenue for fiscal year 1977. That is in answer to Senator Byrd's figures, and I would think that ought to stand corrected.

Secretary SIMON. Let us reconcile those figures and I will supply those for the record, Senator Hartke.[1]

Senator BYRD. May I——

Senator HARTKE. Mr. Chairman, I do want to ask some more questions if I can.

The CHAIRMAN. Senator, if you will pardon me, I will leave it in your complete charge and I will go vote.

Senator ROTH. Could I just make one comment?

Senator HARTKE. Certainly.

Senator ROTH. I would like to go back and get a chance to have your comments on the question of taxpayer assistance. It is a matter of great concern to me. It seems to me that if the tax system is to work, the public must feel that the law is fair and that the administration of the law is fair. And certainly I must say it has been my experience in Delaware—although I want to say I think the head of the IRS in Delaware tries very hard—that the public is not satisfied that they are being treated equitably. For that reason, Mr. Chairman, I would hope that we could hold hearings on taxpayers' assistance at some point in the near future. I think it is of great importance to the public at large. There is evidence that different offices administer the law differently. If the public is going to support the tax laws, we have to make sure it is equitable.

Secretary SIMON. In the speech I gave the Tax Foundation last week I alluded to this. I think the taxpayers' assistance is probably one of the more difficult problems we face in the administration of the Internal Revenue Code. The idea of courtesy, the idea of efficiency is important. I think it was the Wall Street Journal that sent a man around to several Internal Revenue Service offices and he got a different answer from every one and a different number from every one as to how much tax he owed. There was even a difference of opinion in every single office as to what forms he had to fill out.

Senator ROTH. That comes back in part to the 6,000 pages. I recognize that.

Secretary SIMON. Why sure it does and the complexities.

Senator ROTH. At the same time I would like to have an opportunity to explore further with you this problem and see if we can't come up with some solutions.

Senator HARTKE. Those assurances will be made.

How much did we loan out additionally this year in unemployment compensation benefits for the benefit of the States?

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[1] See information supplied at pages 28 and 34.

Secretary SIMON. I didn't bring any of those numbers.

Senator HARTKE. What I'm trying to find out is how much the unemployment is really costing us.

Secretary SIMON. Unemployment is costing us slightly in excess of $20 billion at the Federal Government level.

Senator HARTKE. How much is that over the estimate of what it was going to be for 1975?

Secretary SIMON. I think we are pretty well on the point as to the estimates as far as fiscal year 1976 was concerned and I believe it was——

Senator HARTKE. I believed they asked for $5 billion in September.

Secretary SIMON. Yes; they wanted $6 billion in 1975 and $20 billion in this year.

Senator HARTKE. I'm talking about additional money beyond that to loan to the States because their funds had expired.

Secretary SIMON. Oh, the additional moneys.

Senator HARTKE. That is right.

Secretary SIMON. I will get that.

Senator HARTKE. Money the President asked for and Congress had to appropriate so the Federal Government could loan it to the State unemployment compensation funds.

Secretary SIMON. I will get the number.

Senator HARTKE. Would you supply that number?

Secretary SIMON. Yes, sir.

[The Department of the Treasury subsequently submitted the following information:]

There was a supplemental request for $5.5 billion in November. The Congress approved a similar request for $5 billion last February.

Senator HARTKE. Do you take the same assumption that for every 1 percent of unemployment there is $16 billion tax revenue figure or factor?

Secretary SIMON. I had had our economists look at that and they come up with number from $12 billion to $15 billion.

Senator HARTKE. $15 billion or $16 billion?

Secretary SIMON. $12 billion to $15 billion. That is a ballpark figure; yes.

Senator HARTKE. Then would you disagree then that if we had full employment, there would be a surplus in the neighborhood of about $60 billion?

Secretary SIMON. This year?

Senator HARTKE. Yes.

Secretary SIMON. Full employment being defined as 4 percent?

Senator HARTKE. I'm talking about full employment. You have 8 percent unemployment now. I'm talking about 8 percent times $16 billion, which is $128 billion.

Secretary SIMON. No; you have to bring it down to 4 percent if you're going to go to full employment.

Senator HARTKE. You consider 4 percent full employment?

Secretary SIMON. That is what I consider the antiquated notion of full employment. I consider full employment today at 5 percent and not 4 percent.

Senator HARTKE. Allright. Even if you have that, even if you have 3 percent times $16 billion, that is $48 billion.

Secretary SIMON. That would still leave you——

Senator HARTKE. You could practically eliminate at least part of the deficit.

Secretary SIMON. That would leave you with a deficit from $68 billion to $73 billion or whatever we end up with.

Senator HARTKE. When Secretary Shultz was Secretary of the Treasury, he came here with a full employment budget. But you have not been giving us a full employment budget deficit.

Secretary SIMON. No.

Senator HARTKE. You have given us an actual deficit.

Secretary SIMON. Yes; and I will provide the full employment deficit or a surplus for the record.

Senator HARTKE. All right.

[The Department of the Treasury subsequently submitted the following information:]

FISCAL YEAR 1976 BUDGET DEFICIT UNDER ACTUAL EXPECTATIONS AND CONDITIONS OF FULL EMPLOYMENT

For fiscal year 1976 the budget dificit is estimated to be approximately $73 billion under the President's program and about $69 billion if the Tax Reduction Act of 1975 is extended. Under conditions of full employment these deficits would decline to about $8 billion and $3 billion, respectively.

UNIFIED BUDGET RECEIPTS, OUTLAYS, AND DEFICITS, ACTUAL AND FULL EMPLOYMENT

[In billions of dollars]

	Fiscal years	
	1976	1977
Receipts:		
President's program:		
Actual path	296.7	354.6
Full employment	351.5	398.4
Increase for full employment	54.8	43.8
Extension of tax cuts:		
Actual path	301.2	367.9
Full employment	356.7	410.2
Increase for full employment	55.5	42.3
Outlays:		
President's program:		
Actual path	370.0	395.0
Full employment	359.7	385.2
Increase for full employment	−10.3	−9.8
Extension of tax cuts:		
Actual path	370.0	423.0
Full employment	359.7	413.2
Increase for full employment	−10.3	−9.8
Deficit (−):		
President's program:		
Actual path	−73.3	−40.4
Full employment	−8.2	+13.2
Increase for full employment	65.1	53.6
Extension of tax cuts:		
Actual path	−68.8	−55.1
Full employment	−3.0	−3.0
Increase for full employment	65.8	52.1

Source: Office of the Secretary of the Treasury, Office of Tax Analysis.

Senator HARTKE. But what I'm trying to say very simply is that this country is involved in a real debate between whether or not there is an overheating of the economy. And the series which the President is espousing is the same theory he espoused about a year ago when he was still asking for a tax increase rather than a tax cut to stem inflation.

It is a theory that all you have to do is cut down on the Government being involved in the private sector as the method of controlling inflation.

Secretary SIMON. I guess I can talk——

Senator HARTKE. I just want to say——

Secretary SIMON. I just want to—oh, I'm sorry.

Senator HARTKE. The result of that has been one of the most severe recessions we have had in this history of this country. It just seems to me that we are on the wrong course. I would hope that we would give as much attention to putting people back to work as we do to going ahead and worrying about the bankers. What we have is a banker-oriented economy instead of a people-oriented economy.

Mr. Secretary, I don't expect you to agree with that. I know you have been here a long time and I think you are a great guy. Thank you for your appearance here today.

Secretary SIMON. Thank you.

Senator HARTKE. One moment please. I have something to say for the record at this time. A number of companies indicated to the committee that there are technical defects in the Tax Reduction Act provision for an additional 1 percent investment credit for the establishment of employees' stock ownership plans. Without the correction of the technical defects, the ESOP provisions in the Tax Reduction Act will be frustrated.

According to the chairman, I understand Mr. Robert Flint, a representative of A.T. & T., is attending these hearings and is prepared to discuss these technical defects. We will recess and reconvene at 1:30 to hear him. Senator Kennedy will be heard tomorrow morning. These hearings are now in recess.

[Whereupon, at 12 p.m. the committee recessed to reconvene at 1:30 p.m. the same day:]

[The prepared statement of Secretary Simon follows:]

STATEMENT BY HON. WILLIAM E. SIMON, SECRETARY OF THE TREASURY

Mr. Chairman, it is always a pleasure to appear before the Senate Finance Committee and especially on this occasion when you begin your arduous task of deliberating the tax legislation before you. Everyone in the Administration considers that the work you must accomplish is critically important to the integrity of our federal tax system and may significantly affect the future of our national economy. As you proceed with your hearings and mark-up sessions, it is our hope you will call on us for active participation and such assistance as you might need. Such cooperative efforts will ensure that the resultant legislation will be mutually acceptable to the Congress and the Administration and thus, in our joint view, in the best interests of the American people.

There are some who hold the view that the most urgent matter before you is timing. Because four of the major provisions of the Tax Reduction Act of 1975 expire on December 31, Federal tax receipts will begin to increase January 1, 1976, at an annual rate of approximately $10.3 billion in additional accrual of individual and corporation income taxes. And many of those concerned about the impending rise in tax revenues believe that this should not occur because it might retard the rate of economic recovery.

There is reason for giving the calendar attention. Tax changes not synchronized with the calendar year are disruptive. But, I would remind you, the legislation before you includes *permanent* changes in the Federal income tax structure, and these changes ought to be made only in the context of their consistency with long-range fiscal objectives. If we legislate a permanent reduction in Federal revenues, whenever we do so, unless we simultaneously legislate a reduction in the *level* of Federal expenditures, we merely delude our constituents that we are providing them a tax cut. We only substitute the capricious tax of inflation for the income tax we seemingly cut.

This is why President Ford proposed on October 6 that $28 billion be permanently cut from the income tax system along with a corresponding cut from the level to which Fiscal Year 1977 expenditures would climb if Fiscal Year 1976 programs are allowed to grow as presently projected. We can control the share of GNP channeled through government only if we discipline ourselves to set tax and expenditure policies in harmony with our goals. This is the intent of the Congressional Budget and Impoundment Control Act of 1974, which is universally endorsed, and this is the spirit in which changes in tax structure which reduce the capacity of the income tax system to generate revenues should be enacted. The President does not give this principle of responsible fiscal policy mere lip service; he said on October 6 that he would consider a tax cut unacceptable that was not accompanied by an explicit expenditure limitation, which would make clear to all whether the intent of the Government is to hold inflationary pressures in check, or to increase them.

From their enthusiastic response to the President's announced policy, we have concluded that the American people overwhelmingly support it. We must be disappointed by the response of the House of Representatives which failed, by a narrow margin, to instruct the Ways and Means Committee to incorporate an expenditure ceiling in its tax legislation. We urge this Committee to provide leadership in the Senate by reporting a $28 billion tax cut linked to a fiscal year 1977 sepnding ceiling of $39 billion as the President has proposed.

THE OVERALL FISCAL CONTEXT

Before going to the immediate issue of the extension of the expiring 1975 tax cuts, I would like to emphasize the purpose of and thought behind the President's October 6 fiscal package, of which the current tax proposals are only a part. There were two broad objectives of that balanced tax-cut, spending-limitation proposal—to sustain the upward momentum of the current economic advance and, more importantly, to make a start toward regaining control over the excessive rise in budget spending which has been a major force behind the inflation of recent years.

As the table below shows, in fiscal year 1962 the Federal budget exceeded $100 billion for the first time in history. By fiscal year 1971 it exceeded $200 billion. By fiscal year 1975 it exceeded $300 billion and a figure of $423 billion is in prospect for FY 1977 without some restraint—a fourfold increase in just 15 years! Federal government outlays increased at an annual rate of 6.6 percent during the period 1961–1966, at 9.4 percent per year during the next 5 years and at 11.8 percent per year from 1971 to 1976. If Fiscal Year 1977 expenditures are permitted to grow to $423 billion, the rate of growth will reach $14.3 percent.

For the past 10 fiscal years expenditures grew 175 percent while total GNP increased about 120 percent—that is, the rate of growth in government outlays was nearly 50 percent greater than that of the economy itself, with all of the attendant inflation and financial consequences.

Furthermore, the growth in spending has far exceeded the growth in revenues. During these same years we have posted a string of budget deficits that are unprecedented in peacetime. The Federal Government (including the agencies) will have been forced to borrow over $350 billion from our private money markets over the decade ending with the current fiscal year. That is over a third of a trillion dollars that might otherwise have been used to build new plants and to create new jobs in the private sector.

It is no wonder the inflation has been a severe problem and interest rates have risen to historic levels, a natural consequence of these policies. Furthermore, an even worse result of such budgetary practices is that continuing deficits tend to undermine the confidence of the public in the capacity of our government to deal with inflation.

CHANGES IN FEDERAL UNIFIED BUDGET OUTLAYS, BY FISCAL YEAR, 1961-76

[Dollars in billions]

	Federal outlays	Increase over preceding year	Percentage increase	Surplus or deficit
Fiscal year:				
1961	$97.8	$5.6	6.1	−3.4
1962	106.8	9.0	9.2	−7.1
1963	111.3	4.5	4.2	−4.8
1964	118.6	7.3	6.1	−5.9
1965	118.4	−.2		−1.6
1966	134.7	16.3	13.8	−3.8
1967	158.3	23.6	17.5	−8.7
1968	178.8	20.5	13.0	−25.2
1969	184.5	5.7	3.2	+3.2
1970	196.6	12.1	6.6	−2.8
1971	211.4	14.8	7.5	−23.0
1972	231.9	20.5	9.7	−23.2
1973	246.5	14.6	6.3	−14.3
1974	268.4	21.9	8.8	−3.5
1975	324.6	56.2	20.9	−43.6
1976 (estimate)	370.0	45.4	13.7	−70.0

Source: Economic Report of the President, February 1975, table C-64, p. 324, for years 1961 through 1974; 1975 figures from Final Monthly Treasury Statement of Receipts and Outlays of the United States Government, for period from July 1, 1974, through June 30, 1975; 1976 estimated figures from the White House Fact Sheet, Oct. 6, 1975.

As the President reviewed these figures in developing the decision which he announced on October 6, he became increasingly convinced that a dramatic and permanent shift in direction was called for. Facing another huge budget deficit in FY 1976 or close to $70 billion he concluded that without a significant reduction in the growth of Federal spending a high and damaging rate of inflation would reappear, with all of its resulting harm for our economic system and the living standards of our people. Inflation was a major factor in causing the sharp recession from which we are now recovering. A resurgence of inflation, which could readily be spurred by escalating government spending, will hurt our otherwise brightening economic prospects and could well cause an even more serious recession later on. As President Ford pointed out in speaking of the Federal deficit:

"Over the years, these excesses have played a major role in driving up prices, driving up interest rates, and holding down jobs. We do not have to look far for our underlying problems. Much of our inflation should bear a label: 'Made in Washington, D.C.'"

In designing his proposal, the President realized that the magnitude of the deficit is so great and acceptance of its size and growth so institutionalized that no action could restore a balanced Federal budget in a single year. He therefore chose to attack the problem in stages. For FY 1977 he proposed to hold the deficit to $40–$44 billion. In effect, this would amount to a deficit level in FY 1977 equivalent to the FY 1975 figure. It is noteworthy that if Fiscal Year 1977 expenditures could be held to $395 billion, the increase over 1976 would be 5.4 percent, about the same rate of increase as prevailed during 1961–1966.

If we were able to achieve this goal through cooperation with the Congress, it would be our objective in succeeding year to seek such additional budget reductions as are necessary to achieve a balanced budget in a 3-year period and then to strive for budget surpluses at high employment.

These budgetary goals can be achieved only if we tie tax reduction and expenditures together.

THE TAX REDUCTION ACT OF 1975, THE HOUSE BILL (H.R. 10612), AND THE PRESIDENT'S PROPOSALS

The table below presents in summary from a comparison of the income tax provisions in the Tax Reduction Act of 1975, the House Bill (H.R. 10612), and the President's October 6 proposals. In addition to the $14.6 billion of "temporary" cuts in personal and business income taxes, the Tax Reducation Act provided $9.8 billion in rebates of 1974 tax liabilities and payments to social security recipients.

The $14.6 billion can be broken down into $4.7 billion of business income tax reductions and $9.9 billion of personal income tax reductions.

COMPARISON OF TAX CUTS RELATIVE TO 1972-74 LAW

[Dollars in billions assumes 1975 income level]

	Tax Reduction Act of 1975	H.R. 10612	President's proposal
Individual cuts:			
Standard deduction changes	$2.5	$2.5	$4.0
Exemption/taxable income credit	5.3	10.2	
Personal exemption			10.1
Rate changes			6.6
Earned income credit[1]	1.5		
House purchase credit	0.6		
Subtotal	9.9	12.7	20.7
Business cuts:			
Investment credit	[2]3.3	3.0	3.0
Small business rate and surtax exemption changes	1.5	1.5	1.5
2-percent corporate rate reduction			2.2
6-point utility package			.6
Subtotal	4.7	4.5	7.2
Total tax cuts	14.6	17.2	27.9

[1] Includes both refundable and nonrefundable portions.
[2] Includes extra 1-percent credit for ESOP's.

Note: (For additional detail see annex tables 21 and 22.)

Of the $9.9 billion of personal tax reductions, approximately $8 billion—the changes relating to personal exemptions and the standard deduction—were taken into account in preparing the withholding tables which have been in effect since May of this year. Since such $8 billion cut was implemented through the withholding tables in only 8 months, the continuance of withholding at approximately the same level would require an adjustment of tax rates that would produce a $12 billion annual tax reduction. Such "temporary" cuts in 1975 income taxes have thus become the base on which the House built its package of revisions for 1976, with one slight modification which I shall note hereafter.

Since withholding tables are not used to calculate periodic business tax payments, the extension by H.R. 10612 of the "temporary" business tax reduction for 1975 did not entail additional revenue loss beyond the simple reduction in liabilities provided for in the 1975 Act.

Thus, altogether H.R. 10612 would increase the income tax revenue loss by $2.6 billion over the 1975 Act. But this time, $2.5 billion of the now $17.2 billion revenue loss is permanent, attributable to a conversion to permanency of the previously "temporary" increase in the standard deduction.

Temporary economic stimuli, such as rebates and onetime direct payments, are appropriate fiscal measures in periods of underutilized capital and human resources, and the tax system often is an efficient mechanism for effecting such countercyclical policy. But I will repeat what I told this Committee last March about "temporary" tax cuts when urging you to eschew tampering with the income tax structure for short-run fiscal purposes.

"Being realistic, one of three things will have to occur under the House approach:

1. The reductions will be temporary and expire by their terms.
2. More realistically, the reductions will be permanent, and since there are no revenues to fund them, greater deficits and greater inflation will result over the long-run . . .
3. A third alternative, then, is to make the reductions permanent while also raising revenues or cutting costs by the same amount . . ."

What I would add to this statement on the basis of legislative experience since then is that, if Congress persists in making expedient "temporary" changes in the tax laws annually, it will have no time to consider the important fundamental reforms we all agree are needed.

The President's program of permanent tax law changes with an expenditure ceiling faces reality squarely. It accomplishes what the House has sought to

do—avoid an increase in tax burdens—and does so in a manner which gives due attention to tax structure, equity and simplicity without running the risk of increased inflationary bias.

PERSONAL TAX CUTS

The Tax Reduction Act of 1975 contains several complicated provisions including a $30 per exemption tax credit in addition to the $750 personal exemption and a standard deduction equal to 16 percent of Adjusted Gross Income, with a range from $1,900 to $2,600 for a joint return and from $1,600 to $2,300 for a single person. H.R. 10612 retains the change in standard deduction, which becomes permanent, but substitutes another temporary credit which is no less than $30 but may be as much as 2 percent of taxable income, with a maximum of $240 for both married couples and for single taxpayers. In contrast the President's proposal recommends a simple personal execption of $1,000 and a flat standard deduction of $2,500 for a joint return and $1,800 for a single person, along with rate reductions (Tables 1A and 1B).

These provisions of the President's proposal have two important aims: First to extend the tax reduction of 1975 for everyone; second, to begin the difficult task of realigning the tax rate structure to relieve the middle income taxpayer of onerous tax burdens on industriousness and thrift. Because of rising productivity, but more particularly the effect of inflation on nominal money incomes, families comprising the middle and upper-middle classes of society have been moved up the tax scales to positions previously occupied by only the top one or two percent of American families. As a result, the middle-income taxpayers find that larger and larger tax bites are being taken from their paychecks and entrepreneurial incomes. The rewards to enterprise, to sustained effort, to the accumulation of capital, of this group have been eroded. As we all benefit from the vigor of this group, so are we hurt when its vitality is threatened. The President's program aims to reverse the trend, by providing relief to the middle-income taxpayer while, at the same time, more than preserving the gains of the lower-income taxpayer.

To accomplish this reversal, the proposal combines carefully balanced changes in the basic elements of the income tax structure—bracket rates, personal exemptions and standard deductions. Altogether, as you can see in Table 4, in all income classes up to $20,000 the share of tax reductions exceeds the share of tax burden under 1975 law. Moreover, taxpayers with incomes under $15,000, who presently pay 28.0 percent of personal income taxes, will receive 53.3 percent of the additional tax reduction proposed by the President (Table 4). At the same time, the maximum level of tax-free income is raised for both single and joint returns as compared to 1975 law (Table 6) with the result that 2.1 million returns are removed from the tax rolls.

The President's proposal is also more progressive than the tax cut recently passed by the House of Representatives in H.R. 10612. Under the House Bill only 38.9 percent of the additional tax cut goes to taxpayers with incomes under $15,000 (Table 8). This is not only a smaller percentage, it is a smaller percentage of a tax cut which is itself smaller by $8 billion. As you can see in Table 9, under the House Bill, taxpayers with incomes of less than $15,000 would pay 27.7 percent of $116.7 billion while they would pay 25.3 percent of $108.7 billion under the President's proposal. Those with income under $15,000 receive some $5 billion less than the President proposed.

Furthermore, aside from the earned income credit which is not a part of either proposal, the very lowest income groups are treated better by the President's tax plan than they are by the House Bill. Since the House Bill does not change the standard deduction or the personal exemption, it does not increase the level of tax-free income for those taxpayers, as does the President's proposal. In sum, the President's plan gives some reduction in tax to almost every taxpayer in every income class.

The differences between the President's proposal and the House Bill ay be seen most clearly in Tables 10 through 19 which indicate the tax liabilities under 1974 law, 1975 law, and 1976 law, as proposed, for taxpayers with various income levels and family sizes. The vast differences accorded families with two or more dependents and moderate incomes are particularly striking. The House Bill, due to the characteristics noted above, provides no tax reduction at all from 1975 for families with two children until adjusted gross income exceeds $10,900 (Table 18) and for families with four children until adjusted gross income exceeds

$16,000 (Table 19). In contrast, the President's proposal gives significant tax reductions for families with two or more dependents and lower incomes. For example, the tax reductions from 1975 for a family with $10,000 adjusted gross income (AGI) and two children is $224 (Table 13) and for a family with $15,000 AGI and four children is $257 (Table 14). We should keep in mind that, because of the way the withholding rates were derived under the Tax Reduction Act of 1975, families with no reduction in annual tax liabilities would experience either a decrease in monthly take-home pay or the need to make a substantial payment at tax settlement time. I shall return to this topic below.

In summary, the President's tax recommendations for individual tax reductions are simple to understand and generous to virtually all taxpayers. I strongly urge the enactment of this comprehensive and equitable package as an important component of the total expenditure restraint and tax reduction program.

BUSINESS TAX CUTS

Let me now turn to the proposed business tax cuts.

The Tax Reduction Act of 1975 increased the nominal rate of the investment credit to 10 percent from 7 (4 percent in the case of utilities) for the years 1975 and 1976. H.R. 10612 extends this period for 4 more years, through 1980. The President's proposal would make the increase permanent. It is well known that any tax provision intended to encourage investment is most effective when investors may regard it as permanent, for then they may take it into account over the full range of their investment planning horizons, which are frequently 10 years or longer. As part of a program of structural fiscal change, the investment credit helps offset the anti-capital formation bias of the Federal tax system and should have permanent status.

The Tax Reduction Act, for the year 1975, raised the corporation surtax exemption to $50,000 from $25,000, and lowered the tax rate on the first $25,000 of taxable income from 22 to 20 percent. H.R. 10612 extended this tax reduction 2 additional years. Again the President's proposal would make this change permanent.

In addition to this modification of the corporation tax schedule, the President proposes to reduce the top rate 2 points so that the maximum applicable tax rate would be 46 percent. Until we, working with the committees of Congress, can effect integration of the corporation and personal income taxes, this modest relief of the extra burden of tax should cause beneficial increases in the rate of capital formation.

Finally, the President's proposals include a 6-part tax incentive program for electric utilities to accelerate the replacement of facilities now made obsolete by the higher costs of fossil fuels and to encourage the application of more adequate capital cost pricing formulas by utility commissions. The program includes:

Increasing the permanent investment credit to 12 percent for all electric utility property except generating facilities fueled by petroleum products or natural gas.

Allowance in full of the investment credit on progress payments for construction of property which takes 2 years or more to build. This would except utilities from the present law 5-year phase-in requirement with respect to credit for progress payments.

Permit a utility to elect a depreciate property during its construction period rather than when it is placed in service. This election, along with the increase in tax credit and allowance of the credit for progress payments, would be available only in those instances in which regulatory commissions include construction work in progress in the utility's rate base.

Extend to January 1, 1981 the period during which pollution control facilities installed in pre-1969 plants may qualify for 5-year amortization.

Permit 5-year amortization of the costs of converting petroleum or natural gas fueled generating facilities to other fuels.

Permit a shareholder in an electric utility to elect to receive dividends in the form of stock and to defer income tax thereon until the stock may be sold. Such stock is deemed sold before other stock in the some company held by an electing stockholder, and the dividend will be taxed as ordinary income when the stock is sold.

As compared with H.R. 10612 the President's proposals for tax reductions on income from business capital would result in revenue losses greater by $2.7 billion. But the ratio of these tax reductions to personal tax reductions is about the same in both H.R. 10612 and the larger program of reductions proposed by the President.

EARNED INCOME CREDIT

A further provision of the Tax Reduction Act of 1975 which is scheduled to expire at the end of this year is the earned income credit, under which taxpayers who maintained a shared residence for a dependent child receive a credit of 10 percent of earned income up to a maximum of $400. The credit is phased out as earnings go from $4,000 to $8,000. This is a refundable credit in that if the credit exceeds tax liability, the balance is paid to the taxpayer.

This provision has represented a significant departure from the traditional structure of our personal income tax. Ostensibly it was designed as an offset to the Social Security tax, at the same time encouraging certain individuals to secure employment. If these are the objectives, we believe the earned income credit in the Tax Reduction Act of 1975 is both ineffective and inequitable in achieving its goals. As an offset to the Social Security tax the credit is inequitable in that many workers, namely unmarried individuals and members of families without children, are not eligible for the offset. Further, a family with children is entitled to but one credit even though two-earner families would appear to be most deserving of relief from Social Security taxes, since in many cases the secondary worker in a family does not receive any additional benefit from the Social Security taxes paid on earnings.

In reality, it appears the earned income credit is but another publicly administered "welfare" provisions, which adds complexity to the system but does not significantly affect the degree to which families are self supporting. We would prefer that consideration of such a wage subsidy be undertaken in connection with a comprehensive overhaul of the entire structure of programs to assist the needy.

WITHHOLDING TAXES

As you are aware, not only will the applicable tax rates change as of January 1, 1976, if Congress takes no action, but also employers will be required to use once again the withholding tax tables in effect prior to May 1975. The Internal Revenue Service has notified employers to this effect and they will shortly be incurring the considerable expense to reprogram their systems to implement the higher rates of withholding. If, as we strongly recommend, the President's tax cut proposals are adopted by Congress, prompt notice will be given with regard to the publication of new withholding tables which will take the place of those presently in effect; such prompt notification should be able to spare employers the burden of a double change in the levels of withholding.

The problem of designing a set of withholding tables should not be underestimated, particularly when tax laws are changed in mid-year, or when credits in lieu of, or in addition to, exemptions are provided. As I noted earlier, one of the reasons why H.R. 10612 provides additional tax cuts as compared with the Tax Reduction Act is that the withholding tables in effect under that Act were designed to reduce in 8 months the tax reduction applicable to the full year. If these same tables were carried forward into 1976 along with the provisions of the Tax Reduction Act of 1975, too little tax would be withheld. Thus, if the provisions of the Tax Reduction Act were simply extended to 1976, new tables providing for more withholding would have to be designed. To avoid this, the House has increased the temporary tax reductions. Notwithstanding the overall reduction in tax effected by H.R. 10612, the substitution thereunder of another kind of credit for the $30 credit in the Tax Reduction Act will result in some families having increased withholding. I noted above that such would be the case for large families with medium and low income.

Thus it is not unlikely that new withholding schedules will be needed in any case.

THE ECONOMIC IMPACT OF THE RECOMMENDATIONS

Your Committee is no doubt concerned about how its action on the matters discussed here today may affect the economic recovery from the recent serious recession. A further concern, will undoubtedly be the long-term implications of any such program with regard to the continuing major problem of inflation. The President's program of tax cuts and spending limitation was designed with these two problems very much in mind.

In considering these matters, you may very well take note of the fact that certain economic indicators have declined in the most recent two-month report. I recently had occasion to discuss such matters in my testimony on November 7 before the Joint Economic Committee and I think it appropriate to include my remarks on this subject in the record before you here today:

"Although economic recovery is well underway, there is concern in some quarters about its sustainability. The American public, labor and business leaders and other nations repeatedly express their concern about long-term prospects. Therefore, the major economic thrust of the President's program is directed at what we perceive to be the long-term economic problems confronting the United States. It has two goals: (1) to slow down the upward momentum of government spending and eliminate the chronic Federal budget deficits that have occurred in fourteen of the last fifteen fiscal years—or, in thirty-eight of the last forty-six years; and (2) to return more of the decisionmaking power to individuals and families in determining how they will use their income. These actions would help to improve the efficiency of the economy and the permanent changes would create additional stability which would enable individuals and business firms to plan for the future with more confidence.

"Turning the basic direction of fiscal policy will not be easy because of the legislative momentum that has been accumulated over the years. Budget experts continually describe the 'uncontrollable nature' of most of the Federal budget which rises each year as the number of programs multiply and the number of participants in those programs increase. It is now estimated that nearly three-fourths of the budget is committed to programs for which payment is required under existing law or contracts. These payments must be made unless substantive changes in the laws occur. The Government payrolls make up an additional one-sixth of the Federal budget and the residual one-tenth involves mainly non-payroll purchases of goods and services. These facts make the job of regaining fiscal control difficult. They do not make it impossible. We have listened to so many economists describe why things cannot change that too many people are beginning to believe them. I do not believe that there is any such thing as an 'uncontrollable' Federal budget commitment because they all depend upon legislative priorities. I do believe that there are different priorities and that all good things are not equally good. There is a solution to the problem if the Congressional Budget Committee discipline will require more careful consideration of these priorities and the elimination or curtailment of ineffective programs during the annual appropriations process. We must correct the historical approach of merely continuing existing outlays so that any new claims are always 'add-ons'. But for that process to occur the underlying discipline of economics in matching priority claims and limited resources must occur. The Joint Economic Committee can provide that economic leadership for the rest of Congress.

"Although the major thrust of the President's program is to emphasize long-term goals, a major policy change of this sort affects the near-term pattern of economic activity as well. In a $1½ trillion economy, there obviously are uncertainties in predicating potential changes in economic activity and the specific impact of fiscal policy recommendations. In preparing the President's balanced package of policy initiatives we analyzed the probable course of economic developments that would result if existing government spending trends were to continue and if the tax relief provided by the Tax Reduction Act of 1975 were to be continued in essentially its present form, except for an upward modification of approximately $4 billion which is necessary to maintain existing personal withholding rates. Since the Administration strongly believes that the existing growth rate of government spending must be curtailed and that changes in the distribution of tax relief should occur, a second forecast based on the President's recommendations was also prepared.

"Under either set of assumptions, economic recovery would move forward over the next year with an annual rate of growth of real GNP of approximately 7 percent, gradual reduction of unemployment to the 7 to 7½ percent zone by year-end 1976 and a continuation of the current pattern of consumer price increases of inflation 6 to 7 percent over the next few quarters. Comparing the two forecasts, we find that under the President's program the quarterly path of "real" GNP is slightly higher between now and mid-1976 and slightly lower subsequently as the government spending restraints take effect. These forecasts are subject to the usual caveats with respect to forecasting errors, particularly when the differences are so small relative to the gross national product. Therefore, the President's program must be judged in terms of its long-term benefits since economic forecasts indicate that there will not be significant economic stimulus or restraint in the immediate future as a result of the President's policy recommendations."

CONCLUSION

Certain aspects of our mutual task are clear. The tax cuts which have been proposed by the President in his October 6 message should be adopted. But that is really only the beginning. By simultaneously limiting spending for the fiscal year 1977 to $395 billion, we have the unique opportunity to turn the tide of fiscal irresponsibility which has been engulfing our nation for at least fifteen years.

The President has pointed the way. He has made it clear that if we are ever to provide for stable economic growth and really defeat the extreme economic vice of regressive taxation via inflation, we must immediately join together in imposing a limitation on Federal spending. If this Committee will take the lead. I am confident that the Senate as a whole will follow and that the House of Representatives, if presented with a full opportunity to consider the matter, will join in the required effort to bring an acceptable piece of tax reduction legislation to the President's desk.

Please do not miss this opportunity. Each year that we fail to stem the tide, the task becomes more difficult. Those who misguidedly find it the "easy way" will grow evermore accustomed to turning to Washington for fiscal bounty to attempt to solve every conceivable human problem. We must begin now to halt this trend for the good of those very people who ill-advisedly support its continuance and for the good of the Country as a whole.

As always, I thank you for the opportunity of appearing before you and sharing with you my views on these important subjects.

Table 1-A

Tax Rate Schedule for President's
October 6, 1975 Tax Reduction Proposals
(Married Taxpayers Filing Jointly)

Taxable income bracket		Present rates (percent)	Proposed rates (percent)
$ 0	$1,000	14	12
1,000	2,000	15	14
2,000	3,000	16	15
3,000	4,000	17	15
4,000	6,000	19	16
6,000	8,000	19	17
8,000	10,000	22	21
10,000	12,000	22	22
12,000	16,000	25	25
16,000	20,000	28	29 1/
20,000	24,000	32	34 1/
24,000	28,000	36	36
28,000	32,000	39	39
32,000	36,000	42	42
36,000	40,000	45	45
40,000	44,000	48	48
44,000	52,000	50	50
52,000	64,000	53	53
64,000	76,000	55	55
76,000	88,000	58	58
88,000	100,000	60	60
100,000	120,000	62	62
120,000	140,000	64	64
140,000	160,000	66	66
160,000	180,000	68	68
180,000	200,000	69	69
200,000	--	70	70

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1/ While two rates are increased in the higher brackets, taxpayers with income taxed in those brackets will benefit from rate reductions in the lower brackets so that on balance the changes in rates reduce taxes even for those affected by the increased rates.

Table 1-B

Tax Rate Schedule for President's
October 6, 1975 Tax Reduction Proposals
(Single Taxpayers)

Taxable income bracket		Present rates (percent)	Proposed rates (percent)
$ 0	$ 500	14	12
500	1,000	15	13
1,000	1,500	16	15
1,500	2,000	17	15
2,000	3,000	19	16
3,000	4,000	19	17
4,000	5,000	21	18
5,000	6,000	21	19
6,000	8,000	24	21
8,000	10,000	25	24
10,000	12,000	27	27
12,000	14,000	29	29
14,000	16,000	31	31
16,000	18,000	34	34
18,000	20,000	36	36
20,000	22,000	38	38
22,000	26,000	40	40
26,000	32,000	45	45
32,000	38,000	50	50
38,000	44,000	55	55
44,000	50,000	60	60
50,000	60,000	62	62
60,000	70,000	64	64
70,000	80,000	66	66
80,000	90,000	68	68
90,000	100,000	69	69
100,000	--	70	70

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Table 2

Distribution of Tax Liabilities and Reductions Under the President's Proposal at 1975 Levels of Income as Compared to 1972-74 Law, by Size of Adjusted Gross Income

(billions of dollars)

Adjusted gross income class	Tax liability based on 1972-74 law	Proposed 1976 tax liability	Tax reduction	Percentage distribution of tax reduction 1/	Percentage reduction in tax liability
0 - $5,000	2.0	0.8	1.2	5.9	59.9
$5,000 - 10,000	14.1	9.1	5.0	24.0	35.3
10,000 - 15,000	23.1	17.6	5.5	26.6	23.8
15,000 - 20,000	23.7	19.5	4.2	20.2	17.7
20,000 - 30,000	28.0	24.7	3.3	16.0	11.8
30,000 - 50,000	16.9	15.9	1.0	5.0	6.1
50,000 - 100,000	12.1	11.7	0.4	1.8	3.2
100,000 +	9.4	9.4	0.1	0.4	1.0
Total	129.4	108.7	20.7	100.0	16.0

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1/ Based on unrounded liability figures.

Note: Detail may not add to totals due to rounding.

Table 3

Distribution of the Components of the President's Tax Reduction Proposal
at 1975 Levels of Income as Compared to 1972-74 Law, by Size of Adjusted Gross Income

(millions of dollars)

Adjusted Gross Income Class	Components			Total
	$1,000 Personal Exemption	Standard Deduction Change	Rate Reduction	
$ 0 - $5,000	515	608	102	1,225
5,000 - 10,000	1,908	1,961	1,098	4,967
10,000 - 15,000	2,548	925	2,040	5,513
15,000 - 20,000	2,056	342	1,788	4,186
20,000 - 30,000	1,867	154	1,287	3,308
30,000 - 50,000	802	31	204	1,037
50,000 - 100,000	330	5	48	383
100,000 +	80	1	10	91
TOTAL	10,105	4,026	6,580	20,711

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Note: Detail may not add to totals due to rounding.

Table 4

Distribution of Tax Liabilities and Reductions Under the President's Proposal at 1975 Levels of Income as Compared to 1975 Law, by Size of Adjusted Gross Income

Adjusted Gross Income Class	Tax Liability based on 1975 law 1/	Proposed 1976 tax Liability	Tax reduction	Percentage distribution of tax reduction 2/	Percentage reduction in tax liability
	(..................billions of dollars		..................)	(............percent	...........)
$ 0 - $ 5,000	1.2	0.8	0.4	3.3	32.3
5,000 - 10,000	11.5	9.1	2.4	20.4	20.9
10,000 - 15,000	21.1	17.6	3.5	29.6	16.5
15,000 - 20,000	21.9	19.5	2.4	20.5	11.0
20,000 - 30,000	26.8	24.7	2.1	17.5	7.7
30,000 - 50,000	16.6	15.9	0.7	5.6	4.0
50,000 - 100,000	12.0	11.7	0.3	2.4	2.3
100,000 +	9.4	9.4	0.1	0.6	0.8
TOTAL	120.5	108.7	11.8	100.0	9.8

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1/ Includes effect of changes in the standard deduction, the $30 exemption credit; the home purchase credit, and the nonrefundable portion of the earned income credit. The refundable portion of the earned income credit is treated as an expenditure item.

2/ Based on unrounded liability figures.

Note: Detail may not add to totals due to rounding. Minor differences may arise in totals appearing on other tables due to the different methods used in estimating these income distributions.

Table 5

Distribution of the Components of the Tax Reduction Act of 1975 at 1975 Levels of Income as Compared to 1972-74 Law, by Size of Adjusted Gross Income

(millions of dollars)

Adjusted Gross Income Class	Tax Reductions				Total Tax Reduction	Refundable Portion of Earned Income Credit (Outlays)	Tax Reduction Plus Outlays
	Standard Deduction Change	$30 Credit	Earned Income Credit	Home Purchase Credit			
$ 0-$5,000	502	298	29	6	835	890	1,725
5,000-10,000	1,062	1,190	250	53	2,555	223	2,778
10,000-15,000	374	1,505	0	144	2,023	-	2,023
15,000-20,000	527	1,079	0	156	1,762	-	1,762
20,000-30,000	240	824	0	176	1,240	-	1,240
30,000-50,000	46	257	0	68	371	-	371
50,000-100,000	8	75	0	- 19	102	-	102
100,000 +	1	15	0	4	20	-	20
TOTAL	2,760	5,243	279	625	8,908	1,113	10,021

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Note: Detail may not add to totals due to rounding.

Table 6

Maximum Levels of Tax-Free Income Under the President's Tax Reduction Proposal and under H.R. 10612

(rounded to nearest $10)

Filing status	Maximum tax-free income		Poverty income levels 1/	
	H.R. 10612	President's Proposal	1975	1976
Single				
no dependents	2,560	2,800	2,790	2,970
Married, joint return				
no dependents	3,830	4,500	3,610	3,840
1 dependent	4,790	5,500	4,300	4,570
2 dependents	5,760	6,500	5,500	5,850
3 dependents	6,720	7,500	6,490	6,900
4 dependents	7,670	8,500	7,300	7,770
Single, over 65				
no dependents	3,310	3,800	2,580	2,740
Married, joint return both over 65				
no dependents	5,330	6,500	3,260	3,460

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1/ Underlying Consumer Price Index assumption: for 1975, 161.2; for 1976, 171.5.

Table 7

Distribution of Tax Liabilities Provided in H.R. 10612
as Compared to 1972-74 Law at 1975 Income Levels,
by Size of Adjusted Gross Income

Income Class	Tax Liability Based on 1972-74 Law	Tax Liability under H.R. 10612	Tax Reduction	Percentage Distribution of Tax Reduction	Percentage Reduction in Tax Liability
($000)	(...............$ billions	....	...............)	(.........percent	......)
Up to 5	2.0	1.2	0.8	6.5	40.6
5 - 10	14.1	11.1	2.9	23.2	21.0
10 - 15	23.1	20.0	3.1	24.5	13 5
15 - 20	23.7	20.8	2.9	22.7	12.2
20 - 30	28.0	25.9	2.1	16.6	7.5
30 - 50	16.9	16.3	0.6	4.9	3.7
50 - 100	12.1	11.9	0.2	1.4	1.4
100+	9.4	9.4	*	0.3	0.4
Total	129.4	116.7	12.7	100.0	9.8

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* Less than $50 million.

Table 8

Distribution of Tax Liabilities Provided in H.R. 10612 as Compared to 1975 Law at 1975 Income Levels, by Size of Adjusted Gross Income

Income Class	Tax Liability Based on 1975 Tax 1/	Tax Liability under H.R. 10612	Tax Reduction	Percentage Distribution of Tax Reduction	Percentage Reduction in Tax Liability
($000)	(................$ billions		.............)	(.........percent	.......)
Up to 5	1.2	1.2	*	-0.2	-0.6
5 - 10	11.5	11.1	0.4	10.3	3.4
10 - 15	21.1	20.0	1.1	28.6	5.2
15 - 20	21.9	20.8	1.1	29.4	5.1
20 - 30	26.8	25.9	0.9	22.8	3.2
30 - 50	16.6	16.3	0.3	6.7	1.5
50 - 100	12.0	11.9	0.1	1.9	0.6
100+	9.4	9.4	*	0.4	0.2
Total	120.5	116.7	3.8	100.0	3.2

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*Tax change of less than $50 million.

Note: Numbers may not add to totals due to rounding.

1/ Includes effects of changes in the standard deduction, the $30 exemption credit, the home purchase credit, and the nonrefundable portion of the earned income credit. The refundable portion of the earned income credit is treated as an expenditure item, rather than a tax reduction.

Table 9

Distribution of Tax Liabilities Provided by H.R. 10612
as Compared to the President's Proposal at 1975 Levels of Income,
by Size of Adjusted Gross Income

Adjusted Gross Income Class	Tax Liability under H.R. 10612	Tax Liability President's Proposal	Higher Tax Liability Under H.R. 10612: Amount	Higher Tax Liability Under H.R. 10612: Percent	Percentage Distribution of Liability: H.R. 10612	Percentage Distribution of Liability: President
	(............$ billions	....	......)	(.........percent	....	......)
$ 0-$ 5,000	1.2	0.8	0.4	5.0	1.0	0.8
5,000- 10,000	11.1	9.1	2.0	25.3	9.5	8.4
10,000- 15,000	20.0	17.6	2.4	30.0	17.1	16.2
15,000- 20,000	20.8	19.5	1.3	16.3	17.8	18.0
20,000- 30,000	25.9	24.7	1.2	15.0	22.2	22.7
30,000- 50,000	16.3	15.9	0.4	5.1	14.0	14.6
50,000-100,000	11.9	11.7	0.2	2.6	10.2	10.7
100,000+	9.4	9.4	0.1	0.7	8.1	8.6
Total	116.7	108.7	8.0	100.0	100.0	100.0

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Note: Numbers may not add to totals due to rounding.

Table 10

President's Proposed Plan

Tax Liabilities for Single Person Without Dependents, with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability			Proposed Reduction from	
	1972-74 Law	1975 Law 2/	Proposed 1976 Law	1972-74 Law	1975 Law
$ 5,000	$ 490	$ 404	$ 307	$ 183	$ 97
7,000	889	796	641	248	155
10,000	1,506	1,476	1,227	279	249
15,000	2,589	2,559	2,307	282	252
20,000	3,847	3,817	3,553	294	264
25,000	5,325	5,295	5,015	310	280
30,000	6,970	6,940	6,655	315	285
40,000	10,715	10,685	10,375	340	310
50,000	15,078	15,048	14,725	353	323
100,000	41,600	41,570	41,155	445	415

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit.

Table 11

President's Proposed Plan

Tax Liabilities for Family with No Dependents, Filing Jointly with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability			Proposed Reduction from	
	1972-74 Law	1975 Law 2/	Proposed 1976 Law	1972-74 Law	1975 Law
$ 5,000	$ 322	$ 170	$ 60	$ 262	$ 110
7,000	658	492	335	323	157
10,000	1,171	1,054	800	371	254
15,000	2,062	2,002	1,750	312	252
20,000	3,085	3,025	2,780	305	245
25,000	4,240	4,180	3,950	290	230
30,000	5,564	5,504	5,328	236	176
40,000	8,702	8,642	8,444	258	198
50,000	12,380	12,320	12,080	300	240
100,000	34,790	34,730	34,440	350	290

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit.

Table 12

President's Proposed Plan

Tax Liabilities for Family with 1 Dependent, Filing Jointly with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability: 1972-74 Law	Tax Liability: 1975 Law 2/	Tax Liability: Proposed 1976 Law	Proposed Reduction from: 1972-74 Law	Proposed Reduction from: 1975 Law
$ 5,000	$ 207	$ 73	$ 0	$ 207	$ 73
7,000	526	386	190	336	196
10,000	1,028	938	640	388	298
15,000	1,897	1,807	1,535	362	272
20,000	2,897	2,807	2,530	367	277
25,000	4,030	3,940	3,660	370	280
30,000	5,324	5,234	4,988	336	246
40,000	8,406	8,316	8,054	352	262
50,000	12,028	11,938	11,630	398	308
100,000	34,355	34,265	33,860	495	405

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit. Also assumes that taxpayer is not eligible for the Earned Income Credit. Taxpayers maintaining a home in the United States for a dependent child are eligible for the Earned Income Credit (EIC) if they earn less than $8,000. If eligible for the EIC under 1975 law, taxpayers with earned income of $5,000 would have no tax liability and would receive $227 in direct payments from the Government. Taxpayers with earned income of $7,000 would have tax liabilities of $286.

Table 13

President's Proposed Plan

Tax Liabilities for Family with 2 Dependents, Filing Joint Return with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability			Proposed Reduction from	
	1972-74 Law	1975 Law 2/	Proposed 1976 Law	1972-74 Law	1975 Law
$ 5,000	$ 98	$ 0	$ 0	$ 98	$ 0
7,000	402	186	60	342	126
10,000	886	709	485	401	224
15,000	1,732	1,612	1,325	407	387
20,000	2,710	2,590	2,280	430	310
25,000	3,820	3,700	3,370	450	330
30,000	5,084	4,964	4,648	436	316
40,000	8,114	7,994	7,664	450	330
50,000	11,690	11,570	11,180	510	390
100,000	33,920	33,800	33,280	640	520

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit. Also assumes that taxpayer is not eligible for the Earned Income Credit. Taxpayers maintaining a home in the United States for a dependent child are eligible for the Earned Income Credit (EIC) if they earn less than $8,000. If eligible for the EIC under 1975 law, taxpayers with earned income of $5,000 would have no tax liability and would receive $300 in direct payments from the Government. Taxpayers with income of $7,000 would have a tax liability of $86.

Table 14

President's Proposed Plan

Tax Liabilities for Family with 4 Dependents, Filing Joint Return with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability			Proposed Reduction from	
	1972-74 Law	1975 Law 2/	Proposed 1976 Law	1972-74 Law	1975 Law
$ 5,000	$ 0	$ 0	$ 0	$ 0	$ 0
7,000	170	0	0	170	0
10,000	603	372	190	413	182
15,000	1,402	1,222	965	437	257
20,000	2,335	2,155	1,816	519	339
25,000	3,400	3,220	2,830	570	390
30,000	4,604	4,424	4,008	596	416
40,000	7,529	7,349	6,896	633	453
50,000	11,015	10,835	10,280	735	555
100,000	33,050	32,870	32,120	930	750

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit. Also assumes that taxpayer is not eligible for the Earned Income Credit. Taxpayers maintaining a home in the United States for a dependent child are eligible for the Earned Income Credit (EIC) if they earn less than $8,000. If eligible for the EIC under 1975 law, taxpayers with earned income of $5,000 would have no tax liability and would receive $300 in direct payments from the Government. Taxpayers with income of $7,000 would have no tax liability and would receive direct payments of $100.

Table 15

H.R. 10612

Tax Liabilities for Single Person Without Dependents, with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability			Proposed Reduction from	
	1972-74 Law	1975 Law 2/	Proposed 1976 Law	1972-74 Law	1975 Law
$ 5,000	$ 490	$ 404	$ 380	$ 110	$ 24
7,000	889	796	733	156	63
10,000	1,506	1,476	1,353	153	123
15,000	2,589	2,559	2,352	237	207
20,000	3,847	3,817	3,607	240	210
25,000	5,325	5,295	5,085	240	210
30,000	6,970	6,940	6,730	240	210
40,000	10,715	10,685	10,475	240	210
50,000	15,078	15,048	14,838	240	210
100,000	41,600	41,570	41,360	240	210

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit.

Table 16

H.R. 10612

Tax Liabilities for Family with No Dependents, Filing Jointly with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability			Proposed Reduction from	
	1972-74 Law	1975 Law 2/	Proposed 1976 Law	1972-74 Law	1975 Law
$ 5,000	$ 322	$ 170	$ 170	$ 152	$ 0
7,000	658	492	480	178	12
10,000	1,171	1,054	982	189	72
15,000	2,062	2,002	1,840	222	162
20,000	3,085	3,025	2,845	240	180
25,000	4,240	4,180	4,000	240	180
30,000	5,564	5,504	5,324	240	180
40,000	8,702	8,642	8,462	240	180
50,000	12,380	12,320	12,140	240	180
100,000	34,790	34,730	34,550	240	180

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit.

Table 17

H.R. 10612

Tax Liabilities for Family with 1 Dependent, Filing Jointly with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability: 1972-74 Law	Tax Liability: 1975 Law 2/	Tax Liability: Proposed 1976 Law	Proposed Reduction from: 1972-74 Law	Proposed Reduction from: 1975 Law
$ 5,000	$ 207	$ 73	$ 29	$ 178	$ 44
7,000	526	386	336	190	50
10,000	1,028	938	854	174	84
15,000	1,897	1,807	1,690	207	117
20,000	2,897	2,807	2,657	240	150
25,000	4,030	3,940	3,790	240	150
30,000	5,324	5,234	5,084	240	150
40,000	8,406	8,316	8,166	240	150
50,000	12,028	11,938	11,788	240	150
100,000	34,355	34,265	34,115	240	150

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit. Also assumes that taxpayer is not eligible for the Earned Income Credit. Taxpayers maintaining a home in the United States for a dependent child are eligible for the Earned Income Credit (EIC) if they earn less than $8,000. If eligible for the EIC under 1975 law, taxpayers with earned income of $5,000 would have no tax liability and would receive $227 in direct payments from the Government. Taxpayers with earned income of $7,000 would have tax liabilities of $286.

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Table 18

H.R. 10612

Tax Liabilities for Family with 2 Dependents, Filing Joint Return with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability: 1972-74 Law	Tax Liability: 1975 Law 2/	Tax Liability: Proposed 1976 Law	Proposed Reduction from: 1972-74 Law	Proposed Reduction from: 1975 Law
$ 5,000	$ 98	$ 0	$ 0	$ 0	$ 0
7,000	402	186	186	216	0
10,000	886	709	709	177	0
15,000	1,732	1,612	1,540	192	72
20,000	2,710	2,590	2,470	240	120
25,000	3,820	3,700	3,580	240	120
30,000	5,084	4,964	4,844	240	120
40,000	8,114	7,994	7,874	240	120
50,000	11,690	11,570	11,450	240	120
100,000	33,920	33,800	33,680	240	120

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit. Also assumes that taxpayer is not eligible for the Earned Income Credit. Taxpayers maintaining a home in the United States for a dependent child are eligible for the Earned Income Credit (EIC) if they earn less than $8,000. If eligible for the EIC under 1975 law, taxpayers with earned income of $5,000 would have no tax liability and would receive $300 in direct payments from the Government. Taxpayers with income of $7,000 would have a tax liability of $86.

Table 19

H.R. 10612

Tax Liabilities for Family with 4 Dependents, Filing Joint Return with Itemized Deductions of 16 Percent of Adjusted Gross Income 1/

Adjusted Gross Income	Tax Liability			Proposed Reduction from	
	1972-74 Law	1975 Law 2/	Proposed 1976 Law	1972-74 Law	1975 Law
$ 5,000	$ 0	$ 0	$ 0	$ 0	$ 0
7,000	170	0	0	0	0
10,000	603	372	372	231	0
15,000	1,402	1,222	1,222	180	0
20,000	2,335	2,155	2,095	240	60
25,000	3,400	3,220	3,160	240	60
30,000	4,604	4,424	4,364	240	60
40,000	7,529	7,349	7,289	240	60
50,000	11,015	10,835	10,775	240	60
100,000	33,050	32,870	32,810	240	60

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1/ If standard deduction exceeds itemized deduction, family uses standard deduction.

2/ Assumes that taxpayer is not eligible for the Home Purchase Credit. Also assumes that taxpayer is not eligible for the Earned Income Credit. Taxpayers maintaining a home in the United States for a dependent child are eligible for the Earned Income Credit (EIC) if they earn less than $8,000. If eligible for the EIC under 1975 law, taxpayers with earned income of $5,000 would have no tax liability and would receive $300 in direct payments from the Government. Taxpayers with income of $7,000 would have no tax liability and would receive direct payments of $100.

Table 20

A Comparison of the Liability Effects
of the Tax Reduction Act of 1975,
President's Tax Cut Proposal, and H.R. 10612 on Business Income 1/
(1975 Levels of Income)

	Tax Reduction Act of 1975	President's Tax Cut Proposal	H. R. 10612
	(................$ billions	....	..................)
Increase the corporate surtax exemption to $50,000 with a 2 percentage point reduction in the normal tax	-1.5	-1.5	-1.5
Increase the rate of the investment tax credit to 10%	-3.3	-3.0	-3.0
2 percentage point reduction in the corporate surtax	--	-2.2	--
Utilities tax relief previously proposed	--	-0.6	--
WIN credit	*	--	--
TOTAL	-4.8	-7.2	-4.5

Office of the Secretary of the Treasury
Office of Tax Analysis
December 6, 1975

1/ These figures show the difference between 1972-74 law liability and the two tax programs as applied to calendar 1975 income.

Note: Detail may not add to totals due to rounding.

* Less than $50 million.

TABLE 21

Comparison of Individual Tax Cuts

($ billions, 1975 levels of income)

1975 Act	
-- increased standard deduction (minimum increased from $1300 per return to $1900 for joint return and $1600 for single person; maximum increased from $2000 to $2600 for joint return and $2300 for single person)	$ 2.5
-- $30 personal exemption credit	$ 5.3
-- earned income credit	$ 1.5 1/
-- house purchase credit	$ 0.6
	$ 9.9
House Bill	
-- increased standard deduction (same as 1975 Act)	$ 2.5
-- tax credit equal to 2% of taxable income (minimum $30 per exemption)	$10.2
	$12.7
President's Proposal	
-- flat amount standard deduction ($2500 for joint return and $1800 for single person)	$ 4.0
-- increased personal exemption deduction ($750 to $1000)	$10.1
-- reduced tax rates	$ 6.6
	$20.7

1/ Includes the refundable portion of the earned income credit.

Note: Numbers may not add to totals due to rounding.

December 8, 1975

TABLE 22

Comparison of Business Tax Cuts
($ billions, 1975 levels of income)

1975 Act	
-- increased investment tax credit for 1975 and 1976 from 7-10% (4-10% for utilities)	$ 3.3 1/
-- corporate tax rate and surtax exemption changes (reduce tax rate from 22% to 20% on first $25,000 of income and provide 22% rate on second $25,000)	$ 1.5
	$ 4.7
House Bill	
-- extends investment tax credit increase for four years, through 1980	$ 3.0 2/
-- extends corporate tax rate and exemption changes two years, through 1977	$ 1.5
	$ 4.5
President's Proposal	
-- Permanent extension of investment credit increase	$ 3.0 2/
-- Permanent extension of corporate tax rate and surtax exemption changes	$ 1.5
-- 2% corporate rate reduction (48-46%)	$ 2.2
-- Six point utilities package	$ 0.6
	$ 7.2

1/ Some permanent structural changes were also provided, as well as an additional 1% credit for ESOPs.

2/ A full year cost at 1975 income levels. Revenue effect not incurred until 1977.

Note: Numbers may not add to totals due to rounding.

December 8, 1975

Review of

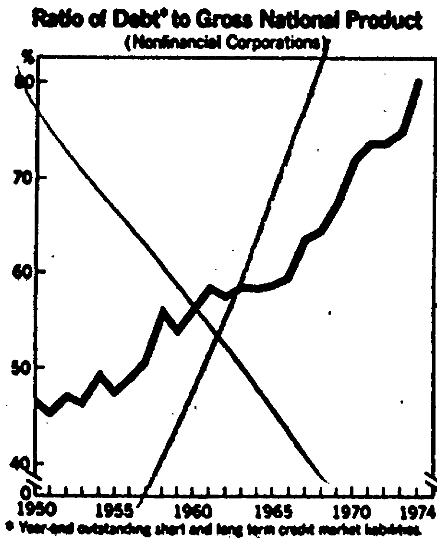
ECONOMIC AND FINANCIAL DEVELOPMENTS

December 17, 1975

THE GROWING DEBT BURDEN IN THE U.S.

Since the 1960's, the growth of debt has become increasingly onerous to U.S. enterprise by raising break-even points which limit profits, making business more vulnerable to cyclical downturns and shortening the magnitude and duration of cyclical expansions. From the standpoint of individual enterprise, it has made more fragile the latter's ability to weather unexpected vicissitudes that are frequently encountered in business.

The mounting burden of debt would seem to have become troublesome only recently in its more dramatic consequences and, perhaps, not even that in the consideration of some. However, serious difficulties posed by the debt explosion have been asserting themselves for a decade or more. They have been averted only because of expansionist economic policies, which have brought in their train an inflationary penalty. When economic policy in recent years was directed toward restraint of the inflation, the increasing fragility of the financial system has quickly emerged and thereby limited the scope of action by the monetary authorities along this line.



A variety of measures show the increasing debt burden of the U.S. economy -- each yielding a different perspective on how borrowing has made both individual enterprise and the economy at large more vulnerable to business cycle swings. These show that:

- The servicing of the debt has become more onerous than formerly as a fixed cost factor to business and thereby provided an additional constraint on profitability.
- Debt financing of business has become increasingly a higher proportion of total sources of business funds -- one which has become costly and sometimes unavailable during periods of credit stringency except to those with the highest credit ratings.

- Debt-equity ratios have risen so high that the buffer of equity that enterprise needs to resist cyclical or other threats to financial well-being, due to fixed claims of creditors, has been eroded.

Though expansion of debt in absolute magnitude might be considered as an associated and necessary feature of a growing economy, it is the more than proportionate increase in recent years in relation to the total value of the output of goods and services that has fostered the several troublesome aspects noted above.

Total outstanding credit market liabilities (bonds, mortgages, bank loans and other credit instruments) as a percentage of gross product originating in nonfinancial business rose to a new high of 75% in 1970-74. This compares with 58% averaged during 1960-64 and as little as 50% in the 1950's (as the chart on the first page shows). While a danger point cannot be established reliably, these increases in outstanding debt as a percentage of output have brought new risks to business.

However, the ability to service the debt out of current production or profit might be considered a more appropriate measure of debt burden -- on the presumption that as long as interest payments are in some favorable relationship with present or potential income, little or no difficulty might be encountered in shouldering the burden. Indeed, if that were so, more debt might be considered a boon rather than a burden, as long as it continued to promote the expansion of business.

However, a number of standards regarding the ability to service the debt indicates that debt has become more burdensome than formerly, rather than promoting stability and growth.

- Interest payments by business as a ratio of the value of output shows a sharply rising trend for the past two decades. Indeed, the ratio that interest payments bear to the value of total output by the 1970's had increased by more than four-fold since the early 1950's. It was 3.0% in 1970-74, which compares with 2.0% in 1965-69; 1.3% in 1960-64; and less than 1% in the 1950's.

- Though these ratios might appear low in relation to total output, even at their increased value for recent years, their potential drag on the ability of firms to survive is placed in better perspective when interest payments are related to profits. Interest payments as a percent of profits before taxes (plus inventory valuation adjustment) were 29% in 1970-74, as compared with a percentage of half that as recently as 1965-69 and one quarter of that in the earlier years. The significance of the interest drag on profits might be viewed in

the following context: in the 1970-74 period, earnings might have been enlarged by about 30% -- in the extreme theoretical case of no interest charges. Presumably, earnings might be considered the beneficiary and hence enterprise might be better able to withstand the impact of other fixed and variable cost increases.

Earlier in 1975, the ratio of interest paid to profits rose dramatically as a consequence of the recession's effects on profits, reaching 35% in the first quarter of 1975. But even after two quarters of recovery in profits, the ratio had declined only to 26% -- about the same as in 1970-74. As the recovery continues, profits may not register the same advances as earlier and so the ratio may be expected to rise again as financing requirements increase and more debt is incurred to meet them. (A rising interest ratio is also apparent when related to that measure of profitability which also includes depreciation allowances -- the so-called "cash flow" measure, as shown in the table.)

Measures of Debt Burden
(Nonfinancial Corporations)

	Debt[1] as Percent of	Net Interest[2] Paid as a Percent of		
	Gross Product Originating	Gross Product Originating	Corp. Profits +IVA2	Corp. Profits +IVA +Depreciation[2]
1950-54	46.8%	.7%	3.6%	2.6%
1955-59	51.5	.9	5.7	3.7
1960-64	57.8	1.3	8.7	5.4
1965-69	62.7	2.0	13.8	8.3
1970-74	74.7	3.0	28.6	14.5

1/ Debt equals outstanding short and long-term Credit Market Liabilities from Federal Reserve estimates.
2/ Data from Bureau of Economic Analysis, Department of Commerce.

The increased debt burden of business over recent years developed in large part because of the growing inadequacy of funds generated from internal corporate sources and because of the tax advantages of debt relative to equity financing, as discussed subsequently. In 1970-74, internally generated funds represented only 72% of the total needed to finance purchases of fixed assets and inventories. (This does not account for financing requirements of such other working capital as receivables, some degree of liquidity, etc.) During 1965-69, internal funds could finance as much as 82% of physical investments and 96% during 1960-64, as shown in the table on the next page.

With recourse to capital markets becoming increasingly heavy in recent years, the acquisition of financial resources through debt instruments rather than equity was strongly favored. This led to a changed balance sheet structure; and to shifts in the relationship of debt to output and to profits, as described above. In part, the tax treatment of interest contributed to use of debt to raise funds. Furthermore, since 1965, the inflation has increasingly favored debt instruments because yields soon incorporated an inflation premium to make them more attractive to the suppliers of funds. At the same time, equities became a less dependable source of external funds because investors increasingly viewed corporate earnings and stock values more vulnerable to business cycle swings.

	Gross Internal Funds as a Percent of:	
	Capital Expenditures	Fixed Investment
1950-54	85%	94%
1955-59	94	100
1960-64	96	105
1965-69	82	94
1970-74	72	79

Note: Calculated from Federal Reserve flow-of-funds estimates of gross internal funds. Capital expenditures include fixed investment plus inventories. Fixed investment includes plant and equipment plus residential construction.

As a result, the debt-equity relationship in the financial structure of U.S. corporations has been transformed substantially. Debt increasingly represented a growing drag on the financial requirements of ongoing enterprise because its associated fixed costs of servicing debt tended to reduce liquidity -- unless even more debt was incurred. Furthermore, a new risk was encountered: in periods of credit stringency, even turnover of debt by corporations may not be easily attainable, let alone securing incremental debt.

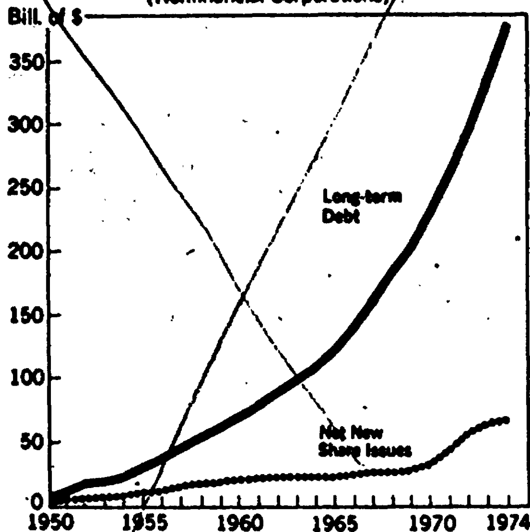
The monetary authorities, of course, may supply financial resources to the credit markets which could permit expansion of debt to business. But, to the extent that this might result in more inflation and thereby reduce the purchasing power of profits and other equity elements, no long-run improvement to liquidity need develop from this source.

All of the several ways of measuring debt-equity relationships point in the same direction of growing distortion.

Of total long-term funds raised in capital markets by nonfinancial corporations in 1950-54, debt instruments in the form of bonds, mortgages and long-term bank borrowings amounted to $24 billion. This was more than 2 1/2 times the funds secured by new net stock issues in this period.

The period subsequent to 1955 shows a rapid rise in this relationship: if the additional amounts of external long-term funds made available to corporations are cumulated over 1955 through 1974, funds raised by debt instruments were 5 1/2 times that of equity sources, as shown in the chart on this page.

This measure accounts for the cumulated annual flows of external funds only. A more comprehensive measure of the status of debt-equity relationship and the ability of enterprise to survive and prosper is found in the balance sheet, on which all funds are represented.



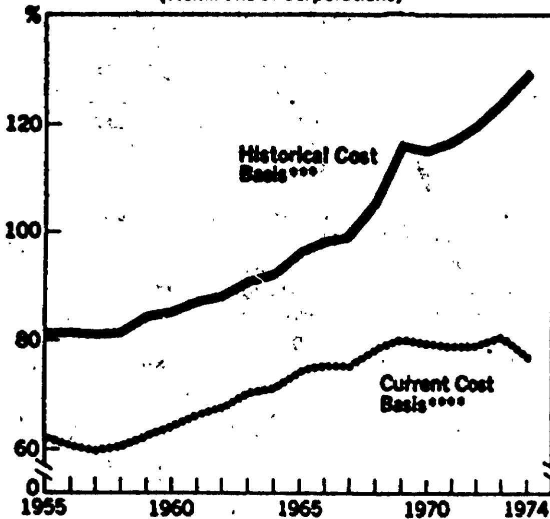
Source: Federal Reserve "flow of funds" estimates.

In this connection, the standard measures of debt-equity relationships are defective --if no adjustment is made for gains to the equity share resulting from inflation.

While book profits should be diminished by taking account of the higher replacement value of inventories and of the higher cost of depreciation charged to fixed assets, that same inflation increases the value of the physical assets already in place. Such an adjustment increases the equity or net worth of enterprise.

(Another adjustment could be made to reflect the reduced burden of debt resulting from the inflation, which favors debtors relative to creditors. Since monetary liabilities are greater than monetary assets, a purchasing power gain to business occurs due to the inflation; this type of adjustment is not attempted here.)

Several different types of measurements which make adjustments to reflect the effects of inflation on corporate accounts are available. Two of these measures, which are shown in the chart on this page and the table on page 7, indicate that the debt-equity ratio has increased to historical highs in both cases. In these measures, total assets are represented by the sum of the book value of financial assets plus (a) physical assets valued at historical costs or (b) physical assets valued at replacement cost; while liabilities are at book values. And since physical assets plus financial assets must equal liabilities plus equity (or net worth), two different measures of equity result -- due to the two different values for physical assets.



As adjusted for current costs, the ratio of total liabilities to equity are reduced substantially, as compared with the historical cost basis. But, even so, the increase since the late 1950's has been substantial -- some 48% in the case of the historical debt-equity ratio and about 30% for the current cost ratio. (If debt is defined narrowly to consist only of credit market instruments, a similar pattern results. In this case, the historical cost ratio has increased about 64% since the late 1950's with the current cost ratio increasing by about 47% over the same period.)

By any of the above standards, debt has increased substantially since the 1960's. It has tended to erode the foundation upon which the financial well-being of the nation rests. A reduction in the inflation, because it brings more advantage than disadvantage, surely would abate this problem to a considerable degree.

But inflation is only part of the problem engendered by rising debt. By introducing another set of rigidities, enterprise becomes more vulnerable to business cycle changes. Important in this regard is the consideration that might be given to shifting the risks and the rewards of enterprise to the owners of capital. By equalizing the rewards to equity and debt sources of funds by tax changes, the increasing brittleness and rigidity that have developed over the past decade can begin to be ameliorated in a way which cannot but lay the basis for more stability and growth in the economy.

Debt[1]-Equity[2] Ratios
(Nonfinancial Corporations*)

	Historical Cost[a]	Current Cost[b]
1955-59	81.6%	60.9%
1960-64	88.6	67.8
1965-69	103.0	76.7
1970-74	121.0	79.1

* Calculated from Federal Reserve Board estimates of assets & liabilities.

1. Debt equals total liabilities.

2. Equity is measured on the basis of: (a) historical cost, which values physical assets at historical prices with straight-line depreciation applied to plant and equipment; and, (b) current cost, which values physical assets at current prices with straight-line depreciation applied to plant and equipment. In both cases, financial assets and total liabilities are at book values.

TABLES ON ESTIMATED GROSS AND NET GOVERNMENT AND PRIVATE DEBT

Table	Subject
1)	Estimated Gross Government and Private Debt, by Major Categories
2)	Estimated Per Capita Gross Government and Private Debt
3)	Estimated Gross Government and Private Debt related to Gross National Product
4)	Estimated Net Government and Private Debt, by Major categories
5)	Estimated Per Capita Net Government and Private Debt
6)	Estimated Net Government and Private Debt related to Gross National Product
7)	Estimated Federal Debt related to Population and Prices
8)	Privately held Federal Debt related to Gross National Product
9)	Changes in Per Capita Real Gross National Product

See footnotes at end of tables.

Office of the Secretary of the Treasury June 5, 1975
Office of Debt Analysis

TABLE ONE

ESTIMATED GROSS GOVERNMENT AND PRIVATE DEBT, BY MAJOR CATEGORIES

(DOLLAR AMOUNTS IN BILLIONS)

DEC.31	PRIVATE(1) INDIVIDUAL	PRIVATE(1) CORPORATE	PRIVATE(1) TOTAL	STATE AND LOCAL	FEDERAL(2) PUBLIC	FEDERAL(2) AGENCY	FEDERAL(2) TOTAL	TOTAL GROSS DEBT	PERCENT FEDERAL OF TOTAL
1929	$ 72.9	$ 107.0	$ 179.9	$ 17.8	$ 16.3	$ 1.2	$ 17.5	$ 215.2	8.1 %
1930	71.8	107.4	179.2	18.9	16.0	1.3	17.3	215.4	8.0
1931	64.9	100.3	165.2	19.5	17.8	1.3	19.1	203.8	9.4
1932	57.1	96.1	153.2	19.7	20.8	1.2	22.0	194.9	11.3
1933	51.0	92.4	143.4	19.5	23.8	1.5	25.3	188.2	13.4
1934	49.8	90.6	140.4	19.2	28.5	4.8	33.3	192.9	17.3
1935	49.7	89.8	139.5	19.6	30.6	5.6	36.2	195.3	18.5
1936	50.6	90.9	141.5	19.6	34.4	5.9	40.3	201.4	20.0
1937	51.1	90.2	141.3	19.6	37.3	5.8	43.1	204.0	21.1
1938	50.0	86.8	136.8	19.8	39.4	6.2	45.6	202.2	22.6
1939	50.8	86.8	137.6	20.1	41.9	6.9	48.8	206.5	23.6
1940	53.0	89.0	142.0	20.2	45.0	7.2	52.2	214.4	24.3
1941	55.6	97.5	153.1	20.0	57.9	7.7	65.6	238.7	27.5
1942	49.9	106.3	156.2	19.2	108.2	5.5	113.7	289.1	39.3
1943	48.8	110.3	159.1	18.1	165.9	5.1	171.0	348.2	49.1
1944	50.7	109.0	159.7	17.1	230.6	3.0	233.6	410.4	56.9
1945	54.7	99.5	154.2	16.0	278.1	1.5	279.6	449.8	62.2
1946	59.9	109.3	169.2	16.1	259.1	1.6	260.7	446.0	58.5
1947	69.4	128.9	198.3	17.5	256.9	0.7	257.6	473.4	54.4
1948	80.6	139.4	220.0	19.6	252.8	1.0	253.8	495.4	51.4
1949	90.4	140.3	230.7	22.2	257.1	0.8	257.9	510.8	50.5
1950	104.3	167.7	272.0	25.3	256.7	1.1	257.8	555.1	46.4
1951	114.3	191.9	306.2	28.0	259.4	0.8	260.2	594.4	43.8
1952	129.4	202.9	332.3	31.0	267.4	0.9	268.3	631.6	42.5
1953	143.2	212.9	356.1	35.0	275.2	0.8	276.0	667.1	41.4
1954	157.2	217.6	374.8	40.2	278.8	0.7	279.5	694.5	40.2
1955	180.1	253.9	434.0	46.3	280.8	1.4	282.2	762.5	37.0
1956	195.5	277.3	472.8	50.1	276.6	1.7	278.3	801.2	34.7
1957	207.6	295.8	503.4	54.7	274.9	3.2	278.1	836.2	33.3
1958	222.9	312.0	534.9	60.4	289.9	2.4	292.3	887.6	32.9
1959	245.0	341.4	586.4	66.6	290.8	5.7	296.5	949.5	31.2
1960	263.3	365.1	628.4	72.0	290.2	6.4	296.6	997.0	29.7
1961	284.8	391.5	676.3	77.6	296.2	6.8	303.0	1056.9	28.7
1962	311.9	421.5	733.4	83.4	303.5	7.8	311.3	1128.1	27.6
1963	345.8	457.1	802.9	89.5	309.3	8.1	317.4	1209.8	26.2
1964	380.1	497.3	877.4	95.5	317.9	9.1	327.0	1299.9	25.2
1965	415.7	551.9	967.6	103.1	320.9	9.8	330.7	1401.4	23.6
1966	444.2	617.3	1061.5	109.4	329.3	14.0	343.3	1514.2	22.7
1967	476.3	672.9	1149.2	117.3	344.7	20.1	364.8	1631.3	22.4
1968	513.8	779.1	1292.9	127.2	358.0	15.1	373.1	1793.2	20.8
1969	548.6	912.7	1461.3	137.9	368.2	13.8	382.0	1981.2	19.3
1970	566.2	997.7	1583.9	149.2	369.2	12.5	401.7	2134.8	18.8
1971	647.6	1084.7	1732.3	167.0	424.1	11.0	435.1	2334.4	18.6
1972	734.3	1230.8	1965.1	181.2	449.3	11.8	461.1	2607.4	17.7
1973	821.9	1413.8	2235.7	193.5	469.9	11.6	461.5	2910.7	16.5
1974	880.1	1584.2	2464.3	209.3	492.7	11.4	504.1	3177.7	15.9

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TABLE TWO

ESTIMATED PER CAPITA GROSS GOVERNMENT AND PRIVATE DEBT(3)

(AMOUNTS IN DOLLARS)

DEC.31	PRIVATE(1)			STATE AND	FEDERAL(2)			TOTAL GROSS
	INDIVIDUAL	CORPORATE	TOTAL	LOCAL	PUBLIC	AGENCY	TOTAL	DEBT
1929	$ 598	$ 878	$ 1477	$ 146	$ 133	$ 9	$ 143	$ 1767
1930	583	872	1455	153	129	10	140	1750
1931	523	808	1331	157	143	10	153	1643
1932	457	769	1227	157	166	9	176	1561
1933	406	735	1141	155	189	11	201	1498
1934	394	716	1110	151	225	37	263	1526
1935	390	705	1096	154	240	44	284	1534
1936	395	709	1105	153	268	46	314	1572
1937	396	700	1096	152	289	45	334	1563
1938	385	668	1053	152	303	47	351	1557
1939	388	663	1051	153	320	52	372	1577
1940	399	671	1070	152	339	54	393	1616
1941	415	728	1143	149	432	57	489	1782
1942	368	785	1153	141	799	40	839	2135
1943	355	803	1159	131	1208	37	1245	2536
1944	364	784	1149	123	1653	21	1681	2954
1945	389	708	1097	113	1979	10	[illegible]	3202
1946	422	770	1192	113	1825	11	1836	3142
1947	479	890	1370	120	1775	4	1780	3271
1948	547	946	1494	133	1717	6	1724	3351
1949	605	936	1540	148	1716	5	1722	3410
1950	684	1101	1786	166	1685	7	1693	3645
1951	738	1239	1977	180	1674	5	1680	3837
1952	821	1287	2109	196	1697	5	1702	4008
1953	893	1329	2223	218	1718	4	1723	4164
1954	964	1334	2299	246	1710	4	1714	4260
1955	1085	1530	2615	279	1692	8	1700	4595
1956	1157	1641	2799	296	1637	10	1647	4743
1957	1207	1719	2927	318	1598	18	1617	4862
1958	1274	1784	3058	345	1657	13	1671	5075
1959	1377	1919	3297	374	1635	32	1667	5339
1960	1457	2020	3478	398	1606	35	1641	5518
1961	1550	2131	3681	422	1612	37	1649	5753
1962	1672	2259	3931	447	1627	41	1668	6047
1963	1827	2415	4242	472	1634	42	1677	6392
1964	1980	2591	4572	497	1656	47	1704	6774
1965	2139	2840	4979	530	1651	50	1701	7212
1966	2259	3140	5400	556	1675	71	1746	7703
1967	2396	3386	5783	590	1734	101	1835	8209
1968	2559	3881	6441	633	1783	75	1858	8934
1969	2706	4503	7209	680	1816	68	1884	9775
1970	2861	4869	7731	728	1899	61	1960	10420
1971	3127	5238	8366	806	2048	53	2101	11274
1972	3516	5893	9409	867	2151	56	2207	12485
1973	3906	6719	10626	919	2233	55	2288	13834
1974	4153	7475	11629	987	2325	53	2378	14995

TABLE THREE

GROSS GOVERNMENT AND PRIVATE DEBT RELATED TO GROSS NATIONAL PRODUCT

DEC. 31	GROSS(4) NATIONAL PRODUCT (BILLIONS $):	PRIVATE(1) INDIVIDUAL	PRIVATE(1) CORPORATE	PRIVATE(1) TOTAL	STATE AND LOCAL	FEDERAL(2) PUBLIC	FEDERAL(2) AGENCY	FEDERAL(2) TOTAL	TOTAL GROSS DEBT
		(RATIOS OF DEBT TO GROSS NATIONAL PRODUCT)							
1929	$56.7	75.4%	110.7%	186.0%	18.4%	16.9%	1.2%	18.1%	222.5%
1930	63.1	86.4	129.2	215.6	22.7	19.3	1.6	20.8	259.2
1931	66.9	97.0	149.9	246.9	29.1	26.6	1.9	28.6	304.6
1932	56.8	100.5	169.2	269.7	34.7	36.6	2.1	38.7	343.1
1933	60.3	84.6	153.2	237.8	32.3	39.5	2.5	42.0	312.1
1934	68.6	72.6	132.1	204.7	28.0	41.5	7.0	48.5	281.2
1935	77.4	64.2	116.0	180.2	25.3	39.5	7.2	46.8	252.3
1936	66.5	58.5	105.1	163.6	22.7	39.8	6.8	46.6	232.8
1937	67.6	58.3	103.0	161.3	22.4	42.6	6.6	49.2	232.9
1938	67.6	57.1	99.1	156.2	22.6	45.0	7.1	52.1	230.6
1939	94.8	53.6	91.6	145.1	21.2	44.2	7.3	51.5	217.8
1940	107.6	49.3	82.7	132.0	18.8	41.8	6.7	48.5	199.3
1941	138.8	40.1	70.2	110.3	14.4	41.7	5.5	47.3	172.0
1942	179.0	27.9	59.4	87.3	10.7	60.4	3.1	63.5	161.5
1943	202.4	24.1	54.5	78.6	8.9	82.0	2.5	84.5	172.0
1944	217.4	23.3	50.1	73.5	7.9	106.1	1.4	107.5	188.8
1945	196.0	27.9	50.8	78.7	8.2	141.9	0.8	142.7	229.5
1946	221.4	27.1	49.4	76.4	7.3	117.0	0.7	117.8	201.4
1947	245.0	28.3	52.6	80.9	7.1	104.9	0.3	105.1	193.2
1948	261.2	30.9	53.4	84.2	7.5	96.8	0.4	97.2	188.9
1949	260.5	34.7	53.9	88.6	8.5	98.7	0.3	99.0	196.1
1950	311.3	33.5	53.9	87.4	8.1	82.5	0.4	82.8	178.3
1951	378.2	33.8	56.7	90.5	8.3	76.7	0.2	76.9	175.6
1952	361.0	35.8	56.2	92.1	8.6	74.1	0.2	74.3	175.0
1953	360.8	39.7	59.0	98.7	9.7	76.3	0.2	76.5	184.9
1954	379.8	41.4	57.3	98.7	10.6	73.4	0.2	73.6	182.9
1955	409.7	44.0	62.0	105.9	11.3	68.5	0.3	68.9	186.1
1956	433.2	45.1	64.0	109.1	11.6	63.9	0.4	64.2	184.9
1957	438.1	47.4	67.5	114.9	12.5	62.7	0.7	63.5	190.9
1958	469.2	47.5	66.5	114.0	12.9	61.8	0.5	62.3	189.2
1959	496.8	49.3	68.7	118.0	13.4	58.5	1.1	59.7	191.1
1960	503.5	52.3	72.5	124.8	14.3	57.6	1.3	58.9	198.0
1961	542.8	52.5	72.1	124.6	14.3	54.6	1.3	55.8	194.7
1962	574.7	54.3	73.3	127.6	14.5	52.8	1.4	54.2	196.3
1963	611.8	56.5	74.7	131.2	14.6	50.6	1.3	51.9	197.6
1964	654.0	58.1	76.0	134.2	14.6	48.6	1.4	50.0	198.8
1965	719.8	57.8	76.7	134.4	14.3	44.6	1.4	45.9	194.7
1966	772.6	57.5	79.9	137.4	14.2	42.6	1.8	44.4	196.0
1967	825.0	57.7	81.6	139.3	14.2	41.8	2.4	44.2	197.7
1968	898.6	57.2	86.7	143.9	14.2	39.8	1.7	41.5	199.6
1969	953.7	57.5	95.7	153.2	14.5	38.6	1.4	40.1	207.7
1970	1009.8	58.1	98.8	156.9	14.8	38.5	1.2	39.8	211.4
1971	1099.1	58.9	98.7	157.6	15.2	38.6	1.0	39.6	212.4
1972	1226.8	59.9	100.3	160.2	14.8	36.6	1.0	37.6	212.5
1973	1351.4	60.8	104.6	165.4	14.3	34.8	0.9	35.6	215.4
1974	1424.0	61.8	111.3	173.1	14.7	34.6	0.8	35.4	223.2

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TABLE FOUR

ESTIMATED NET GOVERNMENT AND PRIVATE DEBT, BY MAJOR CATEGORIES

	PRIVATE(1)			STATE	(5)	TOTAL	PERCENT
				AND		NET	FEDERAL
DEC.31	INDIVIDUAL	CORPORATE	TOTAL	LOCAL	FEDERAL	DEBT	OF TOTAL
191[illegible]	$ 36.3	$ 40.2	$ 76.5	$ 4.5	$ 1.2	$ 82.2	1.5%
191[illegible]	38.7	43.7	82.4	4.8	7.3	94.5	7.7
191[illegible]	44.5	47.0	91.5	5.1	20.9	117.5	17.8
191[illegible]	43.9	53.3	97.2	5.5	25.6	128.3	20.0
192[illegible]	48.1	57.7	105.8	6.2	23.7	135.7	17.5
192[illegible]	49.2	57.0	106.2	7.0	23.1	136.3	16.9
192[illegible]	50.9	58.6	109.5	7.9	22.8	140.2	16.3
192[illegible]	53.7	62.6	116.3	8.6	21.8	146.7	14.9
192[illegible]	55.8	67.2	123.0	9.4	21.0	153.4	13.7
192[illegible]	59.6	72.7	132.3	10.3	20.3	162.9	12.5
192[illegible]	62.7	76.2	138.9	11.1	19.2	169.2	11.3
192[illegible]	66.4	81.2	147.6	12.1	18.2	177.9	10.2
192[illegible]	70.0	86.1	156.1	12.7	17.5	186.3	9.4
192[illegible]	72.9	88.9	161.8	13.6	16.5	191.9	8.6
193[illegible]	71.8	89.3	161.1	14.7	16.5	192.3	8.6
1931	64.9	83.5	148.4	16.0	18.5	182.9	10.1
193[illegible]	57.1	80.0	137.1	16.6	21.3	175.0	12.2
193[illegible]	51.0	76.9	127.9	16.3	24.3	168.5	14.4
193[illegible]	49.8	75.5	125.3	15.9	30.4	171.6	17.7
193[illegible]	49.7	74.8	124.5	16.1	34.4	175.0	19.7
193[illegible]	50.6	76.1	126.7	16.2	37.7	180.6	20.9
193[illegible]	51.1	75.8	126.9	16.1	39.2	182.2	21.5
193[illegible]	50.0	73.3	123.3	16.1	40.5	179.9	22.5
193[illegible]	50.0	73.5	124.5	16.4	42.6	183.5	23.2
194[illegible]	53.0	75.6	128.6	16.4	44.8	189.8	23.6
194[illegible]	55.6	83.4	139.0	16.1	56.3	211.4	26.6
194[illegible]	49.9	91.6	141.5	15.4	101.7	258.6	39.3
194[illegible]	48.8	95.5	144.3	14.5	154.4	313.2	49.3
194[illegible]	50.7	94.1	144.8	13.9	211.9	370.6	57.2
194[illegible]	54.7	85.3	140.0	13.4	252.5	405.9	62.2
194[illegible]	59.9	93.5	153.4	13.7	229.5	396.6	57.9
194[illegible]	69.4	109.6	179.0	15.0	221.7	415.7	53.3
194[illegible]	80.6	118.4	199.0	17.0	215.3	431.3	49.9
194[illegible]	90.4	118.7	209.1	19.1	217.6	445.8	48.8
195[illegible]	104.3	142.8	247.1	21.7	217.4	486.2	44.7
195[illegible]	114.3	163.8	278.1	24.2	216.9	519.2	41.8
195[illegible]	129.4	172.3	301.7	27.0	221.5	550.2	40.3
195[illegible]	143.2	180.9	324.1	30.7	226.8	581.6	39.0
195[illegible]	157.2	184.1	341.3	35.5	229.1	605.9	37.8
195[illegible]	180.1	215.0	395.1	41.1	229.6	665.8	34.5
195[illegible]	195.5	234.1	429.6	44.5	224.3	698.4	32.1
195[illegible]	207.6	249.1	456.7	48.6	223.0	728.3	30.6
195[illegible]	222.9	262.0	484.9	53.7	231.0	769.6	30.0
195[illegible]	245.0	287.0	532.0	59.6	241.4	833.0	29.0
196[illegible]	263.3	306.3	569.6	64.9	239.8	874.3	27.4
1961	284.8	328.3	613.1	70.5	246.7	930.3	26.5
196[illegible]	311.9	353.5	665.4	77.0	253.6	996.0	25.5
196[illegible]	345.8	383.6	729.4	83.9	257.5	1070.8	24.0
196[illegible]	380.1	417.1	797.2	90.4	264.0	1151.6	22.9
196[illegible]	415.7	463.2	878.9	98.3	266.4	1243.6	21.4
196[illegible]	444.2	517.8	962.0	104.8	271.8	1338.6	20.3
196[illegible]	476.3	562.6	1038.9	112.8	286.4	1438.1	19.9
196[illegible]	513.8	653.0	1166.8	122.7	291.9	1581.4	18.5
196[illegible]	548.6	764.8	1313.4	133.3	289.3	1736.0	16.7
197[illegible]	586.2	836.4	1422.6	144.8	301.1	1868.5	16.1
1971	647.6	909.1	1556.7	162.8	325.9	2045.4	15.9
197[illegible]	734.3	1030.8	1765.1	176.9	341.2	2283.2	14.9
197[illegible]	821.9	1185.7	2007.6	189.5	349.1	2546.2	13.7
197[illegible]	860.1	1330.6	2210.7	205.6	360.8	2777.1	13.0

TABLE FIVE

ESTIMATED PER CAPITA NET GOVERNMENT AND PRIVATE DEBT(3)

DEC. 31	PRIVATE(1) INDIVIDUAL	CORPORATE	TOTAL	STATE AND LOCAL	(5) FEDERAL	TOTAL NET DEBT
1916	$ 356	$ 394	$ 750	$ 44	$ 11	$ 806
1917	374	423	797	46	70	915
1918	431	455	886	49	202	1128
1919	420	509	930	52	244	1227
1920	451	541	993	58	222	1274
1921	453	525	978	64	212	1255
1922	462	532	994	71	207	1273
1923	479	559	1038	76	194	1310
1924	488	568	1077	82	184	1344
1925	514	627	1142	88	175	1406
1926	534	649	1183	94	163	1441
1927	557	682	1239	101	152	1494
1928	580	714	1295	105	145	1546
1929	598	730	1328	111	135	1575
1930	583	725	1308	119	134	1562
1931	523	673	1196	128	149	1474
1932	457	640	1098	132	170	1401
1933	406	612	1018	129	193	1341
1934	394	597	991	125	240	1357
1935	390	567	978	126	270	1375
1936	395	594	989	126	294	1410
1937	396	588	985	124	304	1414
1938	385	564	949	124	311	1385
1939	388	561	949	125	325	1400
1940	399	570	969	123	337	1431
1941	415	622	1038	120	420	1578
1942	368	676	1045	113	751	1910
1943	355	695	1051	105	1124	2261
1944	364	677	1042	100	1525	2667
1945	389	607	996	95	1797	2889
1946	422	658	1080	96	1616	2794
1947	479	757	1237	103	1532	2872
1948	547	804	1351	115	1462	2929
1949	603	792	1396	127	1452	2976
1950	684	937	1622	142	1427	3192
1951	738	1057	1795	156	1400	3352
1952	821	1093	1914	171	1405	3492
1953	893	1129	2023	191	1415	3630
1954	964	1129	2093	217	1405	3716
1955	1085	1295	2381	247	1383	4012
1956	1157	1386	2543	263	1327	4134
1957	1207	1448	2655	282	1296	4234
1958	1274	1498	2772	307	1320	4400
1959	1377	1613	2991	335	1357	4684
1960	1457	1695	3152	359	1327	4839
1961	1550	1787	3337	383	1343	5064
1962	1672	1895	3567	412	1359	5339
1963	1827	2027	3854	443	1360	5658
1964	1980	2173	4154	471	1375	6001
1965	2139	2383	4523	505	1371	6400
1966	2259	2634	4894	533	1382	6810
1967	2396	2831	5228	567	1441	7237
1968	2559	3253	5813	611	1454	7679
1969	2706	3773	6480	657	1427	8565
1970	2861	4062	6943	706	1469	9120
1971	3127	4390	7518	786	1574	9879
1972	3516	4935	8451	847	1633	10932
1973	3906	5635	9542	900	1659	12101
1974	4153	6279	10432	970	1702	13105

TABLE SIX

ESTIMATED NET GOVERNMENT AND PRIVATE DEBT RELATED TO GROSS NATIONAL PRODUCT

DEC. 31	GROSS(4) NATIONAL PRODUCT	PRIVATE(1)			STATE AND LOCAL	(5) FEDERAL	TOTAL NET DEBT
		INDIVIDUAL	CORPORATE	TOTAL			
	(BILLION $)	(RATIOS OF DEBT TO GROSS NATIONAL PRODUCT)					
1929	$ 96.7	75.4%	91.9%	167.3%	14.1%	17.1%	198.4%
1930	83.1	86.4	107.5	193.9	17.7	19.9	231.4
1931	66.9	97.0	124.8	221.8	23.9	27.7	273.4
1932	56.8	100.5	140.8	241.4	29.2	37.5	308.1
1933	60.3	84.6	127.5	212.1	27.0	40.3	279.4
1934	68.6	72.6	110.1	182.7	23.2	44.3	250.1
1935	77.4	64.2	96.6	160.9	20.8	44.4	226.1
1936	86.5	58.5	88.0	146.5	18.7	43.6	208.8
1937	87.6	58.3	86.5	144.9	18.4	44.7	208.0
1938	87.6	57.1	83.7	140.8	18.4	46.2	205.4
1939	94.8	53.6	77.5	131.1	17.3	44.9	193.4
1940	107.6	49.3	70.3	119.5	15.2	41.6	176.4
1941	138.8	40.1	60.1	100.1	11.6	40.6	152.3
1942	159.0	27.9	51.2	79.1	8.6	56.8	144.5
1943	202.4	24.1	47.2	71.3	7.2	76.3	154.7
1944	217.4	23.3	43.3	66.6	6.4	97.5	170.5
1945	196.0	27.9	43.5	71.4	6.8	123.8	207.1
1946	221.4	27.1	42.2	69.3	6.2	103.7	179.1
1947	245.0	28.3	44.7	73.1	6.1	90.5	169.7
1948	261.2	30.9	45.3	76.2	6.5	82.4	165.1
1949	260.5	34.7	45.6	80.3	7.3	83.5	171.1
1950	311.3	33.5	45.9	79.4	7.0	69.8	156.2
1951	338.2	33.8	48.4	82.2	7.2	64.1	153.5
1952	361.0	35.8	47.7	83.6	7.5	61.4	152.4
1953	360.8	39.7	50.1	89.8	8.5	62.9	161.2
1954	379.8	41.4	48.5	89.9	9.3	60.3	159.5
1955	409.7	44.0	52.5	96.4	10.0	56.0	162.5
1956	433.2	45.1	54.0	99.2	10.3	51.8	161.2
1957	438.1	47.4	56.9	104.2	11.1	50.9	166.2
1958	469.2	47.5	55.8	103.3	11.4	49.2	164.0
1959	496.8	49.3	57.8	107.1	12.0	48.6	167.7
1960	503.5	52.3	60.8	113.1	12.9	47.6	173.7
1961	542.8	52.5	60.5	113.0	13.0	45.5	171.4
1962	574.7	54.3	61.5	115.8	13.4	44.1	173.3
1963	611.8	56.5	62.7	119.2	13.7	42.1	175.0
1964	654.0	58.1	63.8	121.9	13.8	40.4	176.1
1965	719.8	57.8	64.4	122.1	13.7	37.0	172.8
1966	772.6	57.5	67.0	124.5	13.6	35.2	173.3
1967	825.0	57.7	68.2	125.9	13.7	34.7	174.3
1968	898.6	57.2	72.7	129.8	13.7	32.5	176.0
1969	953.7	57.5	80.2	137.7	14.0	30.3	182.0
1970	1009.8	58.1	82.8	140.9	14.3	29.8	185.0
1971	1099.1	58.9	82.7	141.6	14.8	29.7	186.1
1972	1226.8	59.9	84.0	143.9	14.4	27.8	186.1
1973	1351.4	60.8	87.7	148.6	14.0	25.8	188.4
1974	1424.0	61.8	93.4	155.2	14.4	25.3	195.0

TABLE SEVEN

ESTIMATED FEDERAL DEBT RELATED TO POPULATION AND PRICES

DEC.31	OUTSTANDING FEDERAL DEBT			PER CAPITA FEDERAL DEBT(3)			REAL PER CAPITA FEDERAL DEBT(6)		
	GROSS(2)	NET(5)	PRIVATELY HELD NET(6)	GROSS(2)	NET(5)	PRIVATELY HELD NET(6)	GROSS(2)	NET(5)	PRIVATELY HELD NET(3)
1929	$ 17.5	$ 16.5	$ 16.0	$ 143	$ 135	$ 131	$ 434	$ 409	$ 397
1930	17.3	16.5	15.8	140	134	128	452	431	413
1931	19.1	18.5	17.7	154	149	142	547	530	507
1932	22.0	21.3	19.4	176	170	155	698	676	616
1933	25.3	24.3	21.9	201	193	174	794	763	687
1934	33.3	30.4	28.0	263	240	221	1016	929	856
1935	36.2	34.4	32.0	284	270	251	1067	1014	943
1936	40.3	37.7	35.3	314	294	275	1167	1091	1022
1937	43.1	39.2	36.6	334	304	284	1203	1094	1022
1938	45.6	40.5	37.9	351	312	291	1299	1154	1060
1939	48.8	42.6	40.1	372	325	306	1366	1210	1139
1940	52.2	44.8	42.6	393	337	321	1449	1244	1163
1941	65.6	56.3	54.0	489	420	403	1644	1411	1353
1942	115.7	101.7	95.5	840	751	705	2579	2307	2166
1943	171.0	154.4	142.9	1245	1125	1041	3709	3345	3099
1944	233.6	211.9	193.1	1681	1525	1390	4902	4447	4052
1945	279.6	252.5	228.2	1990	1797	1624	5675	5125	4632
1946	260.7	229.5	206.1	1836	1616	1452	4418	3889	3493
1947	257.6	221.7	199.1	1780	1532	1376	3940	3391	3045
1948	253.8	215.3	192.0	1724	1462	1304	3721	3156	2815
1949	257.9	217.6	197.7	1722	1452	1320	3765	3193	2901
1950	257.8	217.4	196.6	1693	1427	1291	3515	2965	2681
1951	260.2	216.9	193.1	1680	1400	1246	3293	2745	2443
1952	268.3	221.5	196.8	1702	1405	1249	3308	2731	2427
1953	276.0	226.8	200.9	1723	1415	1254	3325	2732	2420
1954	279.5	229.1	204.2	1714	1403	1252	[illegible]	2724	2428
1955	282.2	229.6	204.8	1700	1383	1234	3224	2672	2363
1956	278.3	224.3	199.4	1647	1326	1180	3093	2493	2216
1957	278.1	223.0	198.8	1617	1296	1155	2948	2363	2106
1958	292.3	231.0	204.7	1671	1320	1170	[illegible]	2365	2096
1959	296.5	241.4	214.8	1667	1357	1207	[illegible]	2395	2131
1960	296.6	239.8	212.4	1641	1327	1175	[illegible]	2308	2044
1961	303.0	246.7	217.8	1649	1343	1185	2851	2321	2049
1962	311.3	253.6	222.8	1668	1359	1194	2849	2321	2039
1963	317.4	257.5	223.9	1677	1360	1183	2817	2286	1967
1964	327.0	264.0	227.0	1704	1375	1183	2829	2284	1964
1965	330.7	266.4	225.6	1702	1371	1161	2772	2233	1691
1966	343.3	271.8	227.5	1746	1362	[illegible]	2752	2179	1824
1967	364.8	286.4	237.3	1835	1441	1194	2808	2204	1826
1968	373.1	291.9	238.9	1858	1454	1190	2715	2124	[illegible]
1969	382.0	289.3	232.1	1884	1427	1145	2594	1964	1576
1970	401.7	301.1	239.0	1960	1469	1166	2556	1917	1522
1971	435.1	325.9	255.1	2101	1574	1232	2652	1987	1555
1972	461.1	341.2	269.9	2207	1633	1292	2695	1994	1577
1973	481.5	349.1	268.6	2288	1659	1276	2567	1861	1432
1974	504.1	360.8	280.1	2378	1702	1321	2378	1702	1321

TABLE EIGHT

PRIVATELY HELD FEDERAL DEBT RELATED TO GNP

(DOLLAR AMOUNTS IN BILLIONS OF DOLLARS)

DEC.31	GROSS NATIONAL PRODUCT(4)	PRIVATELY HELD DEBT(6)	RATIO OF DEBT TO GNP	YEAR TO YEAR PRICE CHANGES(7)
1929	$ 96.7	$ 16.0	16.5 %	
1930	83.1	15.8	19.0	-6.0 %
1931	66.9	17.7	26.5	-9.5
1932	56.8	19.4	34.2	-10.3
1933	60.3	21.9	36.3	0.5
1934	68.6	28.0	40.8	2.0
1935	77.4	32.0	41.3	3.0
1936	86.5	35.3	40.8	1.2
1937	87.6	36.6	41.8	3.1
1938	87.6	37.9	43.3	-2.8
1939	94.8	40.1	42.3	-0.5
1940	107.6	42.6	39.6	1.0
1941	138.8	54.0	38.9	9.7
1942	179.0	95.5	53.4	9.3
1943	202.4	142.9	70.6	3.2
1944	217.4	193.1	88.8	2.1
1945	196.0	228.2	116.4	2.3
1946	221.4	206.1	93.1	18.5
1947	245.0	199.1	81.3	8.7
1948	261.2	192.0	73.5	2.6
1949	260.5	197.7	75.9	-1.8
1950	311.3	196.6	63.2	5.8
1951	338.2	193.1	57.1	5.9
1952	361.0	196.8	54.5	0.9
1953	360.8	200.9	55.7	0.7
1954	379.8	204.2	53.8	-0.4
1955	409.7	204.8	50.0	0.4
1956	433.2	199.4	46.0	2.9
1957	438.1	198.8	45.4	3.0
1958	469.2	204.7	43.6	1.7
1959	496.8	214.8	43.2	1.5
1960	503.5	212.4	42.2	1.5
1961	542.8	217.8	40.1	0.6
1962	574.7	222.8	38.8	1.2
1963	611.8	223.9	36.6	1.6
1964	654.0	227.0	34.7	1.2
1965	719.8	225.6	31.3	1.9
1966	772.6	227.5	29.4	3.3
1967	825.0	237.3	28.8	3.0
1968	898.6	238.9	26.6	4.7
1969	953.7	232.1	24.3	6.1
1970	1069.8	239.0	23.7	5.5
1971	1099.1	255.1	23.2	3.4
1972	1226.8	269.9	22.0	3.4
1973	1351.4	268.6	19.9	8.8
1974	1424.0	280.1	19.7	12.2

TABLE NINE

CHANGES IN PER CAPITA REAL GROSS NATIONAL PRODUCT

DEC.31	GNP IN BILLIONS OF 1958 DOLLARS	GNP PER CAPITA CONSTANT 1958 DOLLARS(3)	GNP PER CAPITA, CHANGE FROM YEAR AGO: CONSTANT 1958 DOLLARS	GNP PER CAPITA, CHANGE FROM YEAR AGO: PERCENT
1929	$203.6	$1672		
1930	183.5	1491	$ -181	-10.8%
1931	169.3	1365	-126	-8.5
1932	144.2	1155	-210	-15.4
1933	141.5	1127	-28	-2.4
1934	154.3	1221	94	8.4
1935	169.5	1332	111	9.1
1936	193.0	1507	175	13.2
1937	203.2	1577	70	4.7
1938	192.9	1486	-91	-5.8
1939	209.4	1600	114	7.7
1940	227.2	1714	114	7.1
1941	263.7	1969	255	14.9
1942	297.8	2200	231	11.7
1943	337.1	2456	256	11.6
1944	361.3	2601	145	5.9
1945	355.2	2529	-72	-2.8
1946	312.6	2202	-327	-12.9
1947	309.9	2142	-60	-2.8
1948	323.7	2199	57	2.7
1949	324.1	2164	-35	-1.6
1950	355.3	2333	169	7.8
1951	383.4	2475	142	6.1
1952	395.1	2508	33	1.3
1953	412.8	2577	69	2.8
1954	407.0	2497	-80	-3.1
1955	438.0	2640	143	5.7
1956	446.1	2641	1	0.1
1957	452.5	2631	-10	-0.4
1958	447.3	2558	-73	-2.8
1959	474.9	2671	113	4.4
1960	487.7	2699	28	1.1
1961	497.2	2707	8	0.3
1962	529.8	2840	133	4.9
1963	551.0	2912	72	2.5
1964	581.1	3028	116	4.0
1965	617.8	3180	152	5.0
1966	658.1	3348	168	5.3
1967	675.2	3398	50	1.5
1968	706.6	3521	123	3.6
1969	725.6	3580	59	1.7
1970	722.5	3527	-53	-1.5
1971	746.3	3605	78	2.2
1972	792.5	3795	190	5.3
1973	839.2	3989	194	5.1
1974	821.2	3875	-114	-2.8

FOOTNOTES

1) Private corporate debt includes the debt of certain Federally sponsored agencies in which there is no longer any Federal proprietary interest. The debt of the following agencies are included beginning these years: FLBs in 1949; FHLBs in 1951; FNMA-Secondary market operations, FICBs and BCOOPs in 1968. The total debt for these agencies amount to $0.7 billion on 12/31/47, $3.5 billion on 12/31/60, $38.8 billion on 12/31/70, $59.8 billion on 12/31/73, and $76.4 billion on 12/31/74.

2) Total Federal securities includes public debt securities and budget agency securities.

3) Per capita debt is calculated by dividing debt figures by population of conterminous U. S. Beginning 1949, population includes armed forces overseas, Hawaii and Alaska.

4) Implied level of GNP for end of year. Calculated as an average of the fourth and first calendar quarters at seasonally adjusted annual rates for the years 1939 through present. Prior to 1939, averages of two calendar year figures are used as the best approximation of December 31 levels.

5) Borrowing from the public equals gross Federal debt less securities held in government accounts, (a unified budget concept).

6) Borrowing from the public less Federal Reserve holdings.

7) Measured by all item consumer price index, December to December basis.

8) Per capita debt expressed in December 1974 prices (consumer price index for all items).

Source: Federal debt, Treasury Department; other data, Bureau of Economic Analysis, Commerce Department.

Note: Detail may not add to totals because of rounding.

AFTERNOON SESSION

The CHAIRMAN. The meeting will come to order. I hope that we will have some other Senators present in a few minutes. Meanwhile to try to move on schedule, I'm going to call on the Senator from Massachusetts, Mr. Kennedy. We are very pleased to have you with us. Please proceed

STATEMENT OF HON. EDWARD M. KENNEDY, A U.S. SENATOR FROM THE STATE OF MASSACHUSETTS

Senator KENNEDY. Thank you very much, Mr. Chairman.

It is an honor to be here again this morning before this distinguished committee and to have the opportunity to testify on the pending House-passed tax legislation and the questions of tax reduction and tax reform now waiting action by the Senate.

I appreciate the time pressures on the committee and I am therefore especially grateful for the chance to outline my views on the directions we should take.

I believe there are two twin principles that ought to guide us in our Senate action on tax legislation in the immediate future and for the next session of Congress that convenes in January.

First, with the exception of the President's most unreconstructed economic advisers, there are few who deny the need today for an extension of the tax reductions enacted last March. The economy is slowly recovering from the worst and deepest recession since the depression. The last thing the country needs today is another game of New York chicken by the administration, with the health of the economy at stake. The price of the current impasse is a $13 billion tax increase for Americans on January 1—a shock that could easily stop the recovery in its tracks and tip the economy into an unwanted new recession.

There is broad bipartisan agreement that the 1975 tax cuts should be continued at the $13 billion level for individuals high enough to prevent an increase in withholding rates next year. I urge all sides in the present debate to insure that this extension is enacted into law, without further White House brinksmanship that is jeopardizing the economy.

It seems to me that the President got his calendars mixed up when he asked Congress to turn the tax reductions for 1976 into a hostage for spending cuts in 1977. In my view, the administration's 28–28 proposal was untenable from the beginning, both in terms of economic policy and on practical budgetary grounds. The economy needs to have the tax cuts in place 3 weeks from now, on January 1, 1976, long before fiscal year 1977 begins. And by next May, under the congressional budget reform procedures, the first budget resolution for fiscal year 1977 will have been adopted, and the central issues of the appropriate 1977 budget deficit and spending cuts for the fiscal year will be resolved.

Obviously, there is scope for flexibility, in order to accommodate the views of the President and others who believe that tax reductions should be tied to a spending ceiling—perhaps a 5-month extension of current withholding rates would be appropriate as a compromise. But such a step would be a tortured compromise—having little to do with

sound economics and the merits of tax reductions. Taxpayers ought to be able to plan ahead. The credibility of both Congress and the administration will suffer another blow, if next spring finds millions of ordinary taxpayers facing yet another round of needless uncertainty over their withholding rates and take home pay for the rest of 1976.

My view, especially in light of the President's adamant resistance yesterday, to even the reasonable compromise on withholding, is that Congress should enact the full year 1976 tax reductions now, and then override the President's veto if it actually materializes. And we should put the administration's $28 billion spending cut proposal out to pasture with the WIN buttons, the 1974 tax increase, the opposition to New York aid, and all the other examples of prehistoric economics and non-negotiable demands we have suffered from the administration over the past 15 months.

The second basic principle to guide us is the remarkable achievement of the House of Representatives in enacting what I regard as the most significant beginning on comprehensive tax reform since 1969 and possibly since 1954. For too many years, Congress in general and the Senate in particular, have been the graveyard of responsible tax reform. Because of the successful House action in many areas—particularly the start on reform of tax shelters—the Senate now has the best opportunity it has had in many years to deliver on the promise of tax reform.

In some ways, the lateness of the present session may be a blessing in disguise. If we had a little more time, we might be tempted to rush this legislation through and lose the chance for tax reform again. Experience clearly teaches that Senate action on tax reform in the waning hours of a session, as in 1969 or 1971, is unsatisfactory. The present schedule leaves us no choice but to defer action on the far-reaching House reform provisions until next year.

My hope, therefore, is that this committee will report out the House-passed extension of tax reductions as a separate measure for immediate Senate action now, while reserving decision on almost all of the vital tax reform provisions of H.R. 10612 until next year. I also hope that the committee will agree to report these tax reform provisions to the Senate by a date certain early next spring, under conditions that will promote a thorough and thoughtful debate on the many important sections of the bill.

TAX REFORM

I do believe, however, that the Senate ought to vote on at least two specific and significant tax reforms at this time, before adjournment—the minimum tax and capital gains at death.

The full Senate is ready to vote—again—on the minimum tax. We have voted on this issue on the floor several times in the past 6 years, since the minimum tax was first adopted in 1969. The full Senate actually approved this reform in January 1974 by a vote of 47–32, before the underlying bill was sent back to this committee. And last Thursday, by the overwhelming margins of 334–35 and 314–107, the House of Representatives voted, respectively, to reject a weakening amendment to the minimum tax and to adopt a significantly strengthening amendment.

The reasons for delay on other tax reforms do not apply to the minimum tax. The Senate is thoroughly familiar with this reform. I urge that it be included in the bill the committee sends to the Senate, as a first installment on more significant tax reform to come next spring.

As the chairman is aware, the minimum tax is the imaginative technique enacted by Congress to insure that all citizens with substantial economic income pay at least some tax, regardless of the various loopholes and deductions that might otherwise reduce their tax. The goal of the minimum tax was to end the flagrant inequity by which thousands of wealthy taxpayers are able to use the loopholes in existing law to avoid large amounts of taxes they ought to pay, or even to avoid paying any tax at all.

I also urge the committee at this time to amend the pending legislation to include a provision for the taxation of capital gains at death.

The existing loophole discriminates in favor of persons who bequeath large amounts of accumulated wealth to others in the form of capital gains. And it discriminates against persons whose estates are accumulated out of salaries, wages, dividends, or interest, which are taxed at ordinary income rates each year as they are earned, the estate which such taxpayers pass on to their heirs is the remainder left after income taxes have been paid.

The unfair advantage created by the capital gains at death loophole is obvious. Often, the preference is worth hundreds of thousands or even millions of dollars to wealthy taxpayers whose assets have substantially appreciated in value during their lifetime.

In addition, the existence of the loophole has deleterious economic consequences for the flow of capital, because of the so-called lock-in effect. The absence of a tax on capital gains at death is a strong incentive for taxpayers to retain appreciated property until death, in order to take advantage of the loophole. As a result, capital assets are locked in; taxpayers are reluctant to sell such assets, because they will be required to pay an income tax on their gains. By reducing this tax preference, Congress could unlock billions of dollars for future investment in the Nation, dollars that are now frozen because of the undeserved tax advantage that come into play when property is held until death.

This reform I favor is not a large revenue raiser, at least in the early years; the so-called tax expenditures for capital gains at death is $4.5 billion, the amount of revenue lost each year because of the existence of this loophole. But the revenue gain from the proposal, based on 1975 income levels, would be only $45 million in 1976, rising to $660 million in 1985, when the various provisions would be fully phased in.

Too often, in the current capital formation debate, we hear a great deal about the need for new tax subsidies for capital, such as reductions in the corporate tax rate, reductions in the tax on dividends, or still more favorable tax rates for capital gains. But we hear very little about the need to eliminate unfair and uneconomic existing subsidies such as capital gains at death. It is time to close this loophole, which impairs the flow of capital and makes a mockery of the principle of equity in our tax laws.

TAX REDUCTIONS

Mr. Chairman, as I have stated, I welcome the tax reduction provisions of the House bill as essential fiscal policy to maintain the health of the economy. But there are four areas of the tax cuts where I believe the committee should consider specific modifications:

First, I am confident that the chairman and the committee will take the steps necessary to continue the low-income credit, or "work bonus," enacted last March. The absence of this tax relief for low-income workers is a glaring omission in the House-passed bill. It is enough to say here that the omission almost certainly occurred because the House was deferring on this important question to the distinguished chairman of this committee, who has pursued the issue so effectively in the Senate.

Although the work bonus has been an important innovation in the tax laws, its effect has been blunted to a serious extent by the action of HEW and many States in treating the credit as an offset to benefits under the medicaid, AFDC, SSI, and other Federal and federally assisted income security programs. In adopting the work bonus, I would urge the committee to remedy this defect, as the House did, by requiring the work bonus to be disregarded in determining eligibility for such assistance programs.

Second, with respect to the individual tax reductions, I would urge the committee to substitute a flat refundable $50 or $55 tax credit for the complex formula proposed to the House. The House bill offers a 2-percent credit on the first $12,000 of taxable income, or a credit of $30 for the taxpayer and each dependent, whichever is greater. It is my understanding that a credit of approximately $50 could be substituted for the House bill without causing any additional revenue loss at about $10.9 billion.

The current House approach is no more satisfactory than the defective percentage rebate with minimums and maximums enacted into law last March. I believe that a flat $50 credit is advantageous for several reasons:

It keys the rebate to the size of a taxpayer's family. Under the House bill, for example, taxpayers at the $12,000 income level will receive the same $240 rebate—$240 if they are single persons, $240 if they are married couples, $240 if they have no children, $240 if they have one child, $240 if they have two children, and still be the same $240, even if they have three, four, five, or six children.

The House version obviously discriminates unfairly against married taxpayers and taxpayers with children. At this income level, the alternative $30 credit comes into play only if the taxpayer has seven children or more.

By contrast, with a $50 per person credit, the revenue loss would be the same, but the credit would produce a much fairer distribution of the tax reductions between single persons and families at the same income level. It would also provide more substantial tax relief for persons at lower income levels. But most important, it would end the House bill's surprising discrimination against the average American family.

Third, with respect to the investment credit, I urge the committee to adopt a provision to increase the 10-percent investment credit now in the tax code and in the House bill to 15 percent for a taxpayer's "net new investment." Net new investment would be defined as the amount of investment that exceeds the taxpayer's average investment over the 3 preceding years. The proposed change would provide an important additional antirecession and anti-inflation incentive to business, by rewarding firms that continue to grow.

A major drawback of the flat 10-percent investment credit in current law is that it is no incentive at all for many firms—it is simply a tax windfall that rewards them for investments they would be making anyway. A "net new investment" credit has an important advantage; it rewards only those firms that are growing, and it encourages growing firms to engage in even greater growth.

The cost of the proposed legislation is estimated at $500 million in 1976, which is a modest price for what I regard as an important long-run innovation in the tax laws and a helpful stimulus to real growth in our economy.

Fourth, with respect to tax reductions for small business, I urge the committee to modify the House-passed provisions dealing with the corporate surtax exemption, so as to tailor the $2 billion in tax relief more effectively to help small business.

The House provision continues the present 20-percent tax rate on the first $25,000 of taxable business income and 22 percent on the second $25,000. But since the tax benefits designed for smaller corporations are also available to all other corporations, including the Nation's business giants, much of the tax cut designed for small business goes instead of the Nation's larger enterprises. Yet the vast majority of the Nation's small business are at the bottom of this income scale—625,000 corporations have taxable incomes of $25,000 or less, and another 97,000 have incomes in the $25,000–$50,000 range, compared to much smaller numbers of corporations with larger incomes.

Given the current budget constraints, perhaps the most promising approach for tailoring these benefits to small business would be to phase out all or part of the surtax exemption for large corporations, and use the revenues saved to reduce the normal tax on the first $25,000 or $50,000 of taxable income for small business. Alternatively, the $50,000 surtax exemption could be increased to $75,000 or $100,000 with the increase phased out for larger corporations to minimize the revenue loss. Various other combinations of tax relief are possible here with the same overall revenue loss as in the House-passed bill, and I urge the committee to consider them.

It is time for Congress to insure that small business tax relief is genuinely directed to small business, and is not siphoned off for the benefit of large corporations that do not qualify for such relief under any reasonable definition of small business.

Finally, of the $13 billion in individual tax cuts for 1976, the House bill makes $2.9 billion permanent, and $10.5 billion is made temporary for 1976 only. Obviously, if the House bill is enacted, the Senate and House will be required to deal with these temporary tax cuts again a year from now, before the final adjournment of Congress for the 1976 elections. Conceivably, Congress will find itself dealing with tax

cuts for the fourth time in 18 months. Such stop-and-go tax laws are not wise policy. There is ample economic justification to make all the individual tax cuts permanent now at their 1975 levels, and I urge the committee to consider this course as an alternative to the split timing reductions in the House bill.

In sum, Mr. Chairman, what I am proposing to the committee is a combination of measures that will enable the Senate to deal effectively and fairly with the vital issues of fiscal policy and tax reductions, while preserving the significant opportunity we now have to make a meaningful downpayment on tax reform. I look forward to the report of the committee, and the enactment by the Senate of legislation that fully meets these goals.

I ask unanimous consent that a fuller version of my statement be included.[1]

The CHAIRMAN. Without objection that is agreed to.

Senator, my thought about this is that it is not very far apart from what you are here saying. I find myself facing the facts of life that the President is going to veto this tax. If there is anything I can say for certain at this moment, it is that he is committed to do that and that is what he is going to do. Now apparently the President seems to think that he can be sustained on a veto of the tax cut no matter how we try to accommodate ourself to his views and that he eventually will be forced to add to that a spending cut at the figure that he thinks appropriate for 1977. Otherwise he won't find any continuation of this tax cut.

Now I think the kindest thing we could do for him and the best thing we could do for the country would be to override that veto. But if we add these new items, as meritorious as many of them are, that makes it more difficult for us to override that veto. You get a few people who are against this feature and a few against that feature, and that adds to the votes against the veto. So that if one looks at the votes on the House side, maybe some people would think that a veto could be sustained but that is largely because a lot of those people are voting against some of these provisions that the sponsors regard as reforms. It would seem to me that we are going to need to just pass something extending what we have and just try to muster the strongest possible vote that we can given that we are confronted with what I am positive is going to be a veto. And I would look forward to working with you on these other items next year. I think you've got some very good ideas here. I think many of them I agree with. And I would hope that we could achieve a great deal of that work next year, but I don't think we are going to be successful in what little time remains of this session in doing much more than just keeping the tax cuts that we presently have in affect. I hope that after we discuss it and look at your legislation and look at the practical situation, I hope you might agree that that would be the best procedure to follow.

Senator KENNEDY. My own feeling is that I would hope that the committee would consider these various items, the two major reforms that I mentioned. As regards the minimum tax, that has been debated and was developed here within this committee, as you well know, with your strong support, modified by our former colleague from Iowa.

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[1] See p. 94.

You and I have debated that issue on a number of different occasions, and the Senate has voted on it frequently and with increasing support over that time. I also hope the committee will consider the capital at death proposal and the various modifications that I made with regard to the items which you are very familiar with, namely the investment credit and the work bonus and the $50 credit.

It seems to me, Mr. Chairman, that with the extraordinary vote in the House of Representatives to strengthen the minimum tax, the proposal ought to be part of the Senate's action. The Ways and Means Committee voted to deny only half of the deduction for taxes paid, but the full House strengthened that to deny the whole deduction. That was passed by virtually a three to one majority in the House.

My own view is that at least with the minimum tax, we should use this opportunity to enact this important reform.

I think that there is a sufficient awareness and understanding and importance of at least a bare minimum step on tax reform by the American people that we would actually be in a stronger position to override the veto than a weaker position.

So I would hope that that feature would be necessarily included in any event.

The CHAIRMAN. Well I have to draft that minimum tax and I'm convinced we can draft a much better tax than that. That is an add-on tax; and add-on in addition to what you are paying. It seems to me that the minimum tax should be an alternative.

In other words, have a simple method of computing how much we think you made the way your banker would look at it if you wanted to borrow money. Then if you didn't pay as much as 20 or 30 percent of that figure or some figure in that area, then that is what you owe us.

In other words, assuming you have done all kinds of desirable things like contributing to education and putting a lot of people to work and all of that, it seems to me as though we ought to say that, not withstanding all of that, we think everybody ought to pay a certain amount of tax so that you owe us the higher of two tax computations: one, the figure a very simple computation, or the other computed with all the complexities that are in the tax laws, whichever is higher. So we ought to say that is what you owe us.

I would like a chance to work on that. Now we won't get that chance if we vote this thing right now. I would like to study what the House has done also. I think we can improve on it. That is what we will do if my views prevail.

Now we ought to be voting on all of these proposals I think plus all of the others you have suggested here sometime in the spring of next year or early summer. It seems to me it would be an appropriate time then to be voting on all of these at that point. I believe we may have some very good suggestions and even improve on some of those that you are making.

Senator Haskell?

Senator HASKELL. Thank you, Mr. Chairman.

Senator Kennedy, you spoke of course on the minimum tax. My view is that the minimum tax is there because we have such glaring other gaps in the Internal Revenue Code that this is kind of a catch-all. I would appreciate it if you and your staff would take a look at a bill I have introduced, S. 512. This bill actually abolishes the minimum tax.

The reason it does that is because it starts with repealing 27 sections of the Internal Revenue Code and then repeals others further on and then it goes back to the simple proposition of let's tax income.

I have a friend—and I realize I'm making a speech and not asking a question but I will at the end—who has practiced tax law for about 30 years. His legal philosophy is somewhat to the right of almost any member of this establishment. He made the observation to me the other day that: "Boy, the Internal Revenue Code is really an absurdity. We start out with a principle that we tax on a progressive basis and then we do everything possible to erode the progressivity of the income tax law." And I don't know, Senator, whether you would generally agree with that thrust but I might ask for your comments and——

Senator KENNEDY. The chairman of the committee probably remembers a proposition made by the majority leader some 3 or 4 years ago, which talked about terminating each tax preference as of a fixed date, as a way of requiring a justification for each of the these areas of tax expenditures. These tax subsidies now amount to over $100 billion a year. They are rising faster than the regular budget spending. We made an attempt to bring some reductions in the defense budget, which I know you were a part of, to save $7 billion in the expenditure levels. But still we have done virtually nothing to control tax expenditures, which have been growing dramatically over the last 2 or 3 years and which continue to grow.

It seems to me an entirely worthwhile and valuable and justifiable effort to consider starting over again and saying, "What are the public policy needs and considerations for any of these tax expenditures," and require that they be justified before they are allowed to continue. It would be much wiser if we could do that. But quite frankly, Senator, it seems to me that, as the chairman has pointed out, it is going to be a Herculean task. I don't see that in the wind at the present time. The purpose of the minimum tax was to put a basket under the sieve, to catch what is falling through the loopholes at this time. But as the chairman understands, the minimum tax was modified and weakened in such a way as to make it a sieve under a sieve.

Until the time comes when we are able to give the kind of thoughtful review required by sound public policy for all these tax expenditures, it seems to me that the minimum tax is a useful reform.

But I have no trouble agreeing with your central approach on what ought to be done in terms of policy toward the tax preferences which now exist.

Senator HASKELL. Well I would very much appreciate it if the Senator would take a look at this bill S. 512. It is not as ambitious as some, but it does raise $20 billion. But by eliminating many of the exemptions it obviates the necessity for a minimum tax. And so if the Senator would look at it——

Senator KENNEDY. Fine.

The CHAIRMAN. Senator Packwood?

Senator PACKWOOD. If there are still loopholes left after your bill, then I might say there is a need for a minimum tax. It seems to me though this is ring around the rosy. I mean we pass these deductions and at the time we say we think they are valid. Later on we say, "Well maybe we should never have passed them to begin with so we should put a minimum tax underneath it because we are unable to unpass these deductions." That basically is the philosophy you are driving at.

Senator HASKELL. Well maybe it is, Bob. The philosophy is that the tax laws as applied to commercial transactions should be neutral. For example in our markup session 6 months ago we had people come in to ask for a special treatment because other people, entirely different, had a special treatment. This goes on ad infinitum. And all I am trying to do is end this pyramiding of tax subsidies as far as the commercial transaction is concerned. You see my bill doesn't touch such things as most overage people use, such as the charitable deduction. It doesn't touch that. It doesn't touch mortgage interest. But as far as commercial transactions go, it tries to tax income as under normal accounting practices.

Senator PACKWOOD. Eliminating things like the investment tax credit?

Senator HASKELL. It would eliminate the investment tax credit and accelerated depreciation and that sort of thing.

Senator PACKWOOD. On your new suggested minimum tax would you just tell me how it would work if you have $100,000 of income from municipal bonds and no other income but just that? How do you figure your minimum tax would work? I don't understand it.

Senator KENNEDY. Under the existing provisions of the minimum tax, you reduce your tax preferences by the amount of regular income taxes that you pay. You also subtract another $30,000. And then you pay at the rate of 10 percent.

Senator PACKWOOD. Well let me ask a few questions to see if I can understand. You have a 14-percent tax rate. On $100,000 municipal bond income you got a $14,000 tax. Then you reduce that by $10,000, is that correct, in your proposal? So it takes you down to $4,000. I don't quite understand how——

Senator KENNEDY. Of course, interest on State and local bonds is not a tax preference, so the example would not apply in this case. But the example illustrates the operation of the minimum tax in general.

Senator PACKWOOD. You would not include as a tax preference?

Senator KENNEDY. That is right. Probably, it ought to be included, as a matter of tax policy. But to do so would be disruption of the municipal bond market at this delicate time.

Senator PACKWOOD. OK. So then we are back to this argument again about what should and should not be a tax preference or a loophole or call it what you will.

Senator KENNEDY. There are a number of them listed in the Internal Revenue Code.

Senator PACKWOOD. And you make no effort in your bill to change the preferences? You simply change the method of computing the tax on the preferences?

Senator KENNEDY. Yes. Basically we are almost going back to what was initially reported out of the Finance Committee in 1969 but was altered on the Senate floor. In my proposal, we eliminate the deduction for taxes paid and we reduce the $30,000 exemption to $10,000.

Senator PACKWOOD. Why not include municipal bonds in the preference?

Senator KENNEDY. Well I think there are substantial policy reasons, apart from tax policy relating to the consequences for the municipal bond market and the ability of State and local governments to raise capital.

We have to try and provide new methods of capital formation for the cities. Municipal bonds are obviously a key method used at the

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present time. I favor a proposal to offer a Federal interest subsidy to encourage States and cities and counties to issue taxable bonds.

Senator PACKWOOD. I have no further questions.

The CHAIRMAN. Thank you very much, Senator Kennedy. We will certainly consider your very thoughtful presentation.

Senator KENNEDY. Thank you very much.

[The prepared statement of Senator Kennedy follows:]

TESTIMONY OF SENATOR EDWARD M. KENNEDY

It is an honor to be here again this morning before this distinguished committee and to have the opportunity to testify on the pending House-passed tax legislation and the questions of tax reduction and tax reform now awaiting action by the Senate.

I appreciate the time pressures on the committee and I am therefore especially grateful for the chance to outline my views on the directions we should take.

I believe there are two twin principles that ought to guide us in our Senate action on tax legislation in the immediate future and for the next session of Congress that convenes in January:

First, with the exception of the President's most unreconstructed economic advisers, there are few who deny the need today for an extension of the tax reductions enacted last March. The economy is slowly recovering from the worst and deepest recession since the depression. The last thing the country needs today is another game of New York chicken by the Administration, with the health of the economy at stake. The price of the current impasse is a $13 billion tax increase for Americans on January 1—a shock that could easily stop the recovery in its tracks and tip the economy into an unwanted new recession.

There is broad bipartisan agreement that the 1975 tax cuts should be continued at the $13 billion level for individuals, high enough to prevent an increase in withholding rates next year. I urge all sides in the present debate to insure that this extension is enacted into law, without further White House brinksmanship that is jeopardizing the economy.

It seems to me that the President got his calendars mixed up when he asked Congress to turn the tax reductions for 1976 into a hostage for spending cuts in 1977. In my view, the Administration's 28-28 proposal was untenable from the begining, both in terms of economic policy and on practical budgetary grounds. The economy needs to have the tax cuts in place three weeks from now, on January 1, 1976, long before fiscal year 1977 begins. And by next May, under the Congressional Budget Reform procedures, the First Budget Resolution for fiscal year 1977 will have been adopted, and the central issues of the appropriate 1977 budget deficit and spending cuts for the fiscal year will be resolved.

Obviously, there is scope for flexibility, in order to accommodate the views of the President and others who believe that tax reductions should be tied to a spending ceiling—perhaps a five month extension of current withholding rates would be appropriate as a compromise. But such a step would be a tortured compromise—having little to do with sound economics and the merits of tax reductions. Taxpayers ought to be able to plan ahead. The credibility of both Congress and the Administration will suffer another blow, if next spring finds millions of ordinary taxpayers facing yet another round of needless uncertainty over their withholding rates and take home pay for the rest of 1976.

My view, especially in light of the President's adamant resistance yesterday, to even the reasonable compromise on withholding, is that Congress should enact the full year 1976 tax reductions now, and then override the President's veto if it actually materializes. And we should put the Administration's $28 billion spending cut proposal out to pasture with the WIN buttons, the 1974 tax increase, the opposition to New York aid, and all the other examples of prehistoric economics and non-negotiable demands we have suffered from the Administration over the past fifteen months.

The second basic principle to guide us is the remarkable achievement of the House of Representatives in enacting what I regard as the most significant beginning on comprehensive tax reform since 1969 and possibly since 1954. For too many years, Congress in general and the Senate in particular, have been the graveyard of responsible tax reform. Because of the successful House action in many areas—particularly the start on reform of tax shelters—the Senate now has the best opportunity it has had in many years to deliver on the promise of tax reform.

In some ways, the lateness of the present session may be a blessing in disguise. If we had a little more time, we might be tempted to rush this legislation through and lose the chance for tax reform again. Experience clearly teaches that Senate action on tax reform in the waning hours of a session, as in 1969 or 1971, is unsatisfactory. The present schedule leaves us no choice but to defer action on the far-reaching House reform provisions until next year.

My hope, therefore, is that this committee will report out the House-passed extension of tax reductions as a separate measure for immediate Senate action now, while reserving decision on almost all of the vital tax reform provisions of H.R. 10612 until next year. I also hope that the committee will agree to report these tax reform provisions to the Senate by a date certain early next spring, under conditions that will promote a thorough and thoughtful debate on the many important sections of the bill.

TAX REFORM

I do believe, however, that the Senate ought to vote on at least two specific and significant tax reforms at this time, before adjournment—the minimum tax and capital gains at death.

The full Senate is ready to vote—again—on the minimum tax. We have voted on this issue on the floor several times in the past six years, since the minimum tax was first adopted in 1969. The full Senate actually approved this reform in January 1974 by a vote of 47–32, before the underlying bill was sent back to this committee. And last Thursday, by the overwhelming margins of 334–85 and 314–107, the House of Representatives voted, respectively, to reject a weakening amendment to the minimum tax and to adopt a significantly strengthening amendment.

The reasons for delay on other tax reforms do not apply to the minimum tax. The Senate is thoroughly familiar with this reform. I urge that it be included in the bill the committee sends to the Senate, as a first installment on more significant tax reform to come next spring.

As the committee is aware, the minimum tax is the imaginative technique enacted by Congress to insure that all citizens with substantial economic income pay at least some tax, regardless of the various loopholes and deductions that might otherwise reduce their tax. The goal of the minimum tax was to end the flagrant inequity by which thousands of wealthy taxpayers are able to use the loopholes in existing law to avoid large amounts of taxes they ought to pay, or even to avoid paying any tax at all.

In effect, the minimum tax is a "bucket under a sieve." It is a modest tax on income that slips otherwise untaxed through the many loopholes and special preferences in the existing Revenue Code. If the minimum tax fulfills its function, no one with substantial income would be able to avoid paying a fair share of taxes on his income.

Under the present minimum tax, individuals and corporations are taxed at the rate of 10% on the sum of their income from a large list of tax preferences. These preferences include most, but not all, of the major tax loopholes, less a $30,000 exemption and less the amount of regular income taxes owed.

Because of the loopholes in the minimum tax itself—principally the deduction for taxes paid and the $30,000 exemption, the minimum tax has never fulfilled its function. Even under the minimum tax, as the preliminary figures published by the IRS for the 1973 tax year make clear, there are still many extremely wealthy individuals who pay no federal income tax at all. According to these figures, as the following table indicates, the ranks of "zero taxpayers" included seven individuals with incomes over $1 million who paid no federal income tax in 1973; there were 3,000 persons with incomes over $50,000 and 10,000 persons with incomes over $30,000 who paid no such tax.

Adjusted gross income class	Zero taxpayers	Cumulative
Over $1,000,000	7	7
$500,000 to $1,000,000	15	22
$200,000 to $500,000	142	164
$100 000 to $200,000	458	622
$50,000 to $100,000	2,466	3,088
$30,000 to $50,000	7,312	10,400

And these figures are only the tip of the iceberg. For every "zero" taxpayer in the table, there are dozens more waiting in the wings in each income class, who use the loopholes in the minimum tax to reduce their taxes to near zero, paying only a small proportion of the taxes they reasonably ought to owe.

Because of the exemptions and deductions written in at the beginning and in subsequent years, the minimum tax is itself a loophole ridden tax. As such it is the most aptly named provision in the tax laws—minimum in impact as well as name. Instead of being a "bucket under a sieve," it is simply another sieve under the existing sieve.

The most serious loophole in the present minimum tax is the deduction for taxes paid. In the past, I have called this particular deduction the "Executive Suite" loophole, because it allows highly paid executives and other wealthy persons to use the taxes they pay on their large salaries to shelter large amounts of tax preference income against the minimum tax. Similarly, wealthy doctors and lawyers are able to escape the minimum tax by using this deduction to offset their tax preference income from various investments and other sources.

But simply because a wealthy individual pays taxes on his salary just like everybody else, it does not follow that the taxes he pays should give him free entry to the "loophole club" by allowing him to amass large amounts of sheltered income, free not only from the regular tax, but from the minimum tax as well. The deductions for taxes paid should be eliminated. I regard this as the most important of the reforms in the minimum tax the Senate ought to pass.

In addition the Senate should make two other important changes in the minimum tax:

First, it should reduce the current excessive $30,000 exemption to $10,000 for all taxpayers. By analogy to the House passed bill, the exemption should be phased out dollar for dollar as tax preferences rise above $10,000, so that those with tax preferences in excess of $20,000 receive no exemption at all. The House bill provided a phase out of the exemption over the $20,000–$40,000 range, but the Senate has already approved a $10,000 limit and that is the level we should adopt again.

In addition, in accord with the House-passed bill, the rate of the minimum tax should be increased from its present level of 10% to a new level of 14% for individuals. The current statutory tax rate for ordinary taxpayers is 14% at the lowest income level. It is entirely appropriate that at least this same low 14% rate should be applied to wealthy individuals subject to the minimum tax.

As the Chairman is aware, the reforms of the minimum tax will raise approximately $1 billion in new revenues in calendar year 1976—a significant benefit not only in terms of tax reform, but also in easing the budget constraints under which the committee and the Senate are now operating as we endeavor to allocate scarce Federal revenues among our priorities for spending and tax relief.

CAPITAL GAINS AT DEATH

I also urge the committee at this time to amend the pending legislation to include a provision for the taxation of capital gains at death.

Now that the successful effort to deal with the percentage depletion allowance is largely history, I see two candidates for the honor of "most wanted tax loophole"—the syndicated tax shelter mechanisms, and capital gains at death. It is not possible for the Senate to deal adequately before adjournment with tax shelters and to strengthen the complex but partial reforms in the House-passed bill. But I do believe that it is both possible and desirable for the Senate to deal now with capital gains at death.

Last September, I introduced legislation, S. 2345, now pending before this committee, to deal with capital gains at death. Under present law, such gains escape the income tax altogether if assets are held until death. The heirs receive a "stepped up" basis for the assets—the fair market value at the time of death becomes the new basis of the assets in the hands of the heirs, and gains realized on a subsequent sale are measured only from this basis.

The loophole for capital gains at death is, in effect, a loophole on top of a loophole. Capital gains are already taxed at extremely favorable rates, compared to the rates applicable to "ordinary" income such as wages or salaries. But if property is held until death, no income tax is paid at all, not even at the favorable rates of capital gains tax.

The existing loophole discriminates in favor of persons who bequeath large amounts of accumulated wealth to others in the form of capital gains. And it dis-

criminates against persons whose estates are accumulated out of salaries, wages, dividends or interest, which are taxed at ordinary income rates each year as they are earned; the estate which such taxpayers pass on to their heirs is the remainder left after income taxes have been paid.

The unfair advantage created by the capital gains at death loophole is obvious. Often, the preference is worth hundreds of thousands or even millions of dollars to wealthy taxpayers whose assets have substantially appreciated in value during their lifetime.

In addition, the existence of the loophole has deleterious economic consequences for the flow of capital, because of the so-called "lock in" effect. The absence of a tax on capital gains at death is a strong incentive for taxpayers to retain appreciated property until death, in order to take advantage of the loophole. As a result, capital assets are locked in; taxpayers are reluctant to sell such assets, because they will be required to pay an income tax on their gains. By reducing this tax preference, Congress could unlock billions of dollars for future investment in the nation, dollars that are now frozen because of the undeserved tax advantages that come into play when property is held until death.

To avoid any retroactive effect on gains already accrued, and to avoid disruption of existing estate plans, the tax would apply only to appreciation in value after December 31, 1975. For similar reasons, property transferred to a spouse or to a charity would be exempt from the tax, and a ten-year averaging provision would be applied to reduce the burden on gains subject to such tax. And, to prevent avoidance of the new tax on capital gains at death, a similar tax would be applied to transfers of property by gift.

This reform I favor is not a large revenue raiser, at least in the early years, the so-called tax expenditures for capital gains at death' is $4.5 billion, the amount of revenue lost each year because of the existence of this loophole. But the revenue gain from the proposal, based on 1975 income levels, would be only $45 million in 1976, rising to $660 million in 1985, when the various provisions would be fully phased in.

Too often, in the current capital formation debate, we hear a great deal about the need for new tax subsidies for capital, such as reductions in the corporate tax rate, reductions in the tax on dividends, or still more favorable tax rates for capital gains. But we hear very little about the need to eliminate unfair and uneconomic existing subsidies such as capital gains at death. It is time to close this loophole, which impairs the flow of capital and makes a mockery of the principle of equity in our tax laws.

TAX REDUCTIONS

Mr. Chairman, as I have stated, I welcome the tax reduction provisions of the House bill as essential fiscal policy to maintain the health of the economy. But there are four areas of the tax cuts where I believe the Committee should consider specific modifications:

First, I am confident that the Chairman and the Committee will take the steps necessary to continue the low income credit, or "work bonus", enacted last March. The absence of this tax relief for low income workers is a glaring omission in the House passed bill. It is enough to say here that the omission almost certainly occurred because the House was deferring on this important question to the distinguished Chairman of this Committee, who has pursued the issue so effectively in the Senate.

Although the work bonus has been an important innovation in the tax laws, its effect has been blunted to a serious extent by the action of HEW and many states in treating the credit as an offset to benefits under Medicaid, AFDC, SSI and other federal and federally-assisted income security programs. In adopting the work bonus, I would urge the Committee to remedy this defect, as the House did, by requiring the work bonus to be disregarded in determining eligibility for such assistance programs.

Second, with respect to the individual tax reductions, I would urge the Committee to substitute a flat refundable $50 or $55 tax credit for the complex formula proposed by the House. The House bill offers a 2% credit on the first $12,000 of taxable income, or a credit of $30 for the taxpayer and each dependent, whichever is greater. It is my understanding that a credit of approximately $50 could be substituted for the House bill without causing any additional revenue loss at about $10.9 billion.

The current House approach is no more satisfactory than the defective percentage rebate with minimums and maximums enacted into law last March. I believe that a flat $50 credit is advantageous for several reasons:

It keys the rebate to the size of a taxpayer's family. Under the House bill, for example, taxpayers at the $12,000 income level will receive the same $250 rebate—$240 if they are single persons, $240 if they are married couples, $240 if they have no children, $250 if they have one child, $240 if they have two children, and still the same $240, even if they have three, four, five, or six children or seven.

The House version obviously discriminates unfairly against married taxpayers and taxpayers with children. At this income level, the alternative $30 credit comes into play only if the taxpayer has seven children or more.

By contrast, with a $50 per person credit, the revenue loss would be the same, but the credit would produce a much fairer distribution of the tax reductions between single persons and families at the same income level. It would also provide more substantial tax relief for persons at lower income levels. But most important, it would end the House bill's surprising discrimination against the average American family.

In addition, unlike the House bill, the $50 per person credit should be "refundable," so that it would also help those who work but whose income is so low that they are unable to use the credit fully. In the House bill, a taxpayer with zero tax liability gets no benefit. Those with low tax liability get only a partial benefit. Under the refundable approach, they would get the full benefit of the credit, so long as they have earned income.

The test of refundability would be the same as in the "earned income credit" provisions of the Tax Cut Law enacted last March. The 1976 tax cut should be fair to all. Low income workers are also entitled to participate in the broad based economic stimulus that Congress is providing.

Third, with respect to the investment credit, I urge the Committee to adopt a provision to increase the 10% investment credit now in the Tax Code and in the House bill to 15% for a taxpayer's "net new investment." Net new investment would be defined as the amount of investment that exceeds the taxpayer's average investment over the three preceding years. The proposed change would provide an important additional anti-recession and anti-inflation incentive to business, by rewarding firms that continue to grow.

In general, under present law, as adopted by the Tax Reduction Act last March, a credit equal to a flat 10% of investment in plant and equipment is allowed against income taxes—the so called "investment tax credit."

Under the measure I am proposing, a "bonus" of 5% on the investment tax credit would be available to firms that exceed their prior growth record. The extra 5% credit would provide an immediate anti-recession stimulus to the economy by encouraging additional investment in plant and equipment. And it would also provide an important long run anti-inflation incentive, by ecouraging firms to develop the capacity the country needs to meet the growing demand for goods in the future and prevent the shortages that have fed inflation in the past.

A major drawback of the flat 10% investment credit in current law is that it is no incentive at all for many firms—it is simply a tax windfall that rewards them for investments they would be making anyway. A "net new investment credit has an important advantage, it rewards only those firms that are growing, and it encourages growing firms to engage in even greater growth.

Thus, under the proposal, every firm will receive the regular 10% investment credit for its investment in new plant and equipment. But firms that exceed their prior three-year average investment will qualify for a 5% bonus, or a total credit of 15% on their incremental new investment.

The cost of the proposed legislation is estimated at $500 million in 1976, which is a modest price for what I regard as an important long run innovation in the tax laws and a helpful stimulus to real growth in our economy.

Fourth, with respect to tax reductions for small business, I urge the Committee to modify the House-passed provisions dealing with the corporate surtax exemption, so as to tailor the $2 billion in tax relief more effectively to help small business.

The House provision continues the present 20% tax rate on the first $25,000 of taxable business income and 22% on the second $25,000. But since the tax benefits designed for smaller corporations are also available to all other corporations, including the nation's business giants, much of the tax cut designed for small business goes instead to the nation's larger enterprises. Yet the vast major-

ity of the nation's small business are at the bottom of this income scale—625,000 corporations have taxable incomes of $25,000 or less, and another 97,000 have incomes in the $25,000–$50,000 range, compared to much smaller numbers of corporations with larger incomes.

A number of alternatives are available here. Several members of this Committee are also members of the Senate Small Business Committee, which has studied these provisions, and which has done such an effective job in laying the groundwork for small business tax reform. Congress is beginning to reach a deeper understanding of the economic impact of tax changes on small business, and I believe we can do a better job on these provisions before adjournment.

The benefits of small business tax relief are derived from a combination of the increase in the surtax exemption and the reduction in the so called "normal" tax rate on corporations. Given the current budget constraints, perhaps the most promising approach for tailoring these benefits to small business would be to phase out all or part of the surtax exemption for large corporations, and use the revenues saved to reduce the normal tax on the first $25,000 or $50,000 of taxable income for small business. Alternatively, the $50,000 surtax exemption could be increased to $75,000 or $100,000 with the increase phased out for larger corporations to minimize the revenue loss. Various other combinations of tax relief are possible here with the same overall revenue loss. Various other combinations of tax relief are possible here with the same overall revenue loss as in the House-passed bill, and I urge the Committee to consider them.

It is time for Congress to insure that small business tax relief is genuinely directed to small business, and is not siphoned off for the benefit of large corporations that do not qualify for such relief under any reasonable definition of small business.

Finally, of the $13 billion in individual tax cuts for 1976, the House bill makes $2.9 billion permanent, and $10.5 billion is made temporary for 1976 only. Obviously, if the House bill is enacted, the Senate and House will be required to deal with these temporary tax cuts again a year from now, before the final adjournment of Congress for the 1976 elections. Conceivably, Congress will find itself dealing with tax cuts for the fourth time in 18 months. Such stop-and-go tax laws are not wise policy. There is ample economic justification to make all the individual tax cuts permanent now at their 1975 levels, and I urge the Committee to consider this course as an alternative to the split timing reductions in the House bill.

In sum, Mr. Chairman, what I am proposing to the Committee is a combination of measures that will enable the Senate to deal effectively and fairly with the vital issues of fiscal policy and tax reductions, while preserving the significant opportunity we now have to make a meaningful downpayment on tax reform. I look forward to the report of the Committee, and the enactment by the Senate of legislation that fully meets these goals.

The CHAIRMAN. I would like to call a witness from the American Telephone & Telegraph Co. Is that gentleman in the room? His name is Robert Flint.

Mr. Flint, you directed a letter to me as chairman of this committee informing me that A.T. & T. has considered the 1 percent tax credit for employee stock ownership. I believe they find it appealing except from their point of view there are technical problems that would simply have to be overcome if they were going to adopt such a plan. As I understand this, to correct those technical defects involves practically no cost to the Treasury. It is just a matter of providing that the company, for example, would not have to pay for the start-up costs out of funds which are beyond the amount of the tax credit provided for plan contributions. And, in the event that credit were disallowed in whole or in part, you would want to recapture that money out of future contributions. But if the law were not extended, there wouldn't be any future contributions and you don't feel that you would be in a position to recapture these funds from employees after you put the money or the stock in their hands, correct? Also you have the matter of redetermination and that involves substantially the same problem.

Is my understanding correct that if we could clear up these technical problems, your company would like to participate, as we hoped you would, in the investment tax credit for the benefit of your employees?

STATEMENT OF ROBERT N. FLINT, VICE PRESIDENT AND COMPTROLLER, AMERICAN TELEPHONE & TELEGRAPH CO.

Mr. FLINT. Mr. Chairman, I will say that we are certainly in complete agreement. We think that employee ownership of stock is great. We are very much in favor of that. As you know, there are many ways in which it could be done. Perhaps we would like to have them be done in some different way. But in any of these four items to which you have alluded, which I covered in my letter, if they were able to be cured, than I'm confident that we would go ahead and adopt ESOP using the 1-percent investment credit. There was an item you did not mention. It is the regulatory problem that we would have. That would prevent the money being used to purchase stock for employees and at the same time being used for distribution to customers over the balance of the life of the plant which generated the credit. We can only spend the dollar once.

The CHAIRMAN. You can't have your cake and eat it, too. That is included in these amendments that you are talking about?

Mr. FLINT. That is included.

The CHAIRMAN. Now would the same problem apply with regard to most regulated public utilities like the electric companies and people of that sort?

Mr. FLINT. I believe that is right, yes. There are a couple of ways in which the regulatory process handles the investment tax credit I'm talking about the basic 10-percent credit. But in either event the customer ends up having the benefit from the credit. And so you would need protection to be sure you didn't have the money used both to buy stock for the employee and at the same time pass the money onto the customer. That would be on the first point. On the other points I'm sure other utilities and nonregulated industries would have the same problems. Namely, if you have to pay the Government back the investment tax credit after you paid the money over to the trust, that is, if it is subject to recapture, it is our view we should not have to pay that money back to the Government if it is going to stay in the trust. On redetermination, that is where you redetermine whether or not you were eligible in the first instance, we feel that if amounts are still being paid into the trust, there ought to be some sort of offset or, as a minimum in the latter instance, there ought to be a deduction.

The CHAIRMAN. I will ask that your letter appear in the record at this point.

[The document referred to follows:]

AMERICAN TELEPHONE AND TELEGRAPH CO.,
New York, N.Y., December 5, 1975.

Hon. RUSSELL B. LONG,
Chairman, Committee on Finance,
U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: This statement is submitted by American Telephone and Telegraph Company in connection with the hearings of the Senate Finance Committee on HR. 10612, the Tax Reform Act of 1975, which was passed by the House on December 4, 1975.

My comments relate to four obstacles we have encountered in considering the establishment of an employee stock ownership plan utilizing the additional 1% investment tax credit, as provided by Section 46(a)(1)(B) of the Internal Revenue Code. These obstacles, which are essentially technical in nature, are enumerated below.

1. *Special problem for Utilities.*—Under present law (i.e., Section 46(f) of the Internal Revenue Code) a regulatory commission may treat the investment tax credit as a cost reduction to be flowed through to utility customers, in some cases immediately and, in others, over the life of new business plant associated with the tax credit. This is a reasonable treatment for the 10% tax credit (allowed by Section 46(a)(1)(A)), where the benefit is intended to be shared by a utility's existing shareholders and its customers. But this would not be appropriate treatment for the ESOP credit allowed by 46(a)(1)(B) where the additional 1% tax credit is intended to be used to acquire capital stock for employees. If a regulatory commission were to seek to flow through the additional 1% ESOP tax credit in reduced rates to customers, the utility company would find itself in the position of having issued stock for which no permanent capital was received. In other words, the utility company would be paying out the ESOP credit twice, once to its employees and once to its customers. This situation would be injurious to existing shareholders whose interest would eventually be diluted by the full amount of these new shares.

Legislation should be enacted to provide specifically that the portion of the tax credit going to the ESOP be treated as equity capital for the employees, with regulatory flow-through prohibited.

2. *"Recapture" of Additional 1% ESOP Tax Credit.*—Section 301(d) of the Tax Reduction Act of 1975 sets out several conditions relative to eligibility for the ESOP tax credit. One of these conditions appears to be that a corporation should make its contribution to an ESOP at the time it files its return based on the amount of qualified investment *claimed* at the time it files its return, but that no adjustment may be thereafter made to ESOP contributions even though the amount of the tax credit to which the corporation ultimately is determined to be entitled may be lower than the amount claimed on its return if business plant happens to be removed from service prior to its initially anticipated life. In such a case, a portion of the tax credit would be subject to the "recapture" provisions of Section 47 of the Internal Revenue Code, but the employer would not be allowed to make a compensating adjustment in the amount contributed to an ESOP plan. See paragraphs (6) and (8) of Section 301(d) of the Tax Reduction Act of 1975. This would put the company in the position of having issued stock to its employees for which no equity capital was received, and would result in a corresponding dilution of the interests of existing shareholders.

The law should be changed to prohibit the recapture of any portion of the investment tax credit actually contributed to the ESOP, unless bad faith on the part of the taxpayer can be demonstrated.

3. *Audit Redetermination of Additional 1% ESOP Tax Credit.*—A similar problem is created by the possibility that, on audit of the corporate return, the Internal Revenue Service will determine that property is ineligible for the tax credit which the taxpayer believed to be eligible when the return was initially filed. The amount of the related 1% ESOP tax credit would thus be subject to assessment as a deficiency liability. However, Section 301(d) of the Tax Reduction Act of 1975 fails to provide for any adjustment in the treatment of ESOP contributions in such a case. Here again, the company would be put in the position of having issued stock without receiving equity capital for it.

The law should be changed to allow subsequent adjustments to ESOP contributions to reflect amounts subject to redetermination.

4. *Costs of Administering tax Credit ESOP's.*—The Internal Revenue Service has interpreted the Tax Reduction Act of 1975 to require that the expenses of managing the additional 1% ESOP tax credit, held in trust for employees, cannot be charged to the trust. This means that such expenses must be absorbed by the company, with the ultimate effect borne by existing non-employee shareowners. Without remedial legislation, the burden of the administrative expense could discourage corporations from adopting these plans.

The law should be changed to allow a recovery from the ESOP trust of those expenses which are attributable to trust administration of this 1% tax credit.

If these four problem areas are not corrected by remedial legislation, American Telephone and Telegraph Company does not believe it is practical to elect the ESOP tax credit.

Respectfully submitted.

R. N. FLINT,
Vice President and Comptroller.

The CHAIRMAN. I hope that either in connection with this or some other legislation we pass between now and the time we adjourn, that we can take care of this. If your company were to participate, as we had intended and other companies like yours were to participate, we would need to do this before the first of the year, would we not?

Mr. FLINT. We would need to have assurances really as soon as feasible that it can be done. It is not a thing that is easy to be done. We will be filing our tax return about September 15 of next year. In the meantime if you are going to do something, there is a lot of work that needs to be done, tax payments that need to be determined. So if it were done by the end of the year, it would give us our sailing orders to understand where we stood with respect to the 1 percent investment tax credit.

The CHAIRMAN. Senator Haskell.

Senator HASKELL. I wonder if you could explain to me a little of your problem. As I understand the extra 1 percent, ESOP gives you a right to take some other additional percentage, normally investment tax credit? I forget what you——

Mr. FLINT. No, Senator. The way it would work is at the present time you are entitled to take 10 percent. If you so elect, you may take the additional 1 percent and use that money to buy stock from the employer at fair market value, set that stock up in an ESOP, which an employee stock ownership plan, put it in a trust, and then it ultimately would be distributed to employees. The 10 percent would continue as it has been.

Senator HASKELL. So really when you talk about the ESOP, you are just taking the additional 1 percent and you don't get an additional 2 and 3, and you are just putting 1 percent aside?

Mr. FLINT. That is correct.

Senator HASKELL. And your problem is basically the utility regulatory flowthrough?

Mr. FLINT. To give an example, it might help.

Senator HASKELL. Yes, sir.

Mr. FLINT. Suppose you acquired some plant for $1,000 and you were entitled to a 10-percent investment tax credit. Now that would be $100. If a plant had a life of 10 years, we would take that $100 and set it up in a reserve. Every year over the life of the plant we would release $10 so that it would benefit the customer. At the end of the 10 years, when the life of the plant is done, the customer has received the full $100. In the meantime the utility has had the use of the funds. You really get a double bang for your dollar. We have the use of the money, you see, until the customer gets it, but the customer ultimately gets it.

Now the 1 percent is subject to the same rules. And if you don't do something we will be taking the 1 percent, which in this case would be $10, that is 1 percent of $1,000, and we would be issuing stock to employees for $10 and then passing the $10 onto the customer as well.

Senator HASKELL. Basically you would have to pay out the 1 percent twice, is that what you're talking about?

Mr. FLINT. Yes, sir.

Senator HASKELL. And if I understand it—well, I can understand the problem where you have an immediate passthrough on a regulatory commission, but the same problem pertains when you have a

passthrough that—well, let me ask you this: Is it over the life of the particular property or is it over the life of the accumulated investment?

Mr. FLINT. As a general rule, the way we work this, Senator, is that if the investment credit were with respect to 8-year life, that particular credit would be flowed back through over 8 years. If it were 15 years, a 15-year property, it would be flowed through over 15 years. We are talking about the 1 percent and that would be used immediately to buy stock to give to the employees, but you would still have the liability over the 8 years or the 15 years, or whatever, to pass it back over, and then you don't have the dollar.

Senator HASKELL. Thank you. I think I understand.

The CHAIRMAN. Thank you very much. That concludes these hearings. The committee will meet in executive session in this room at 10 o'clock tomorrow.

[By direction of the chairman, the following communication was made a part of the printed record:]

MACHINERY AND ALLIED PRODUCTS INSTITUTE,
Washington, D.C., December 10, 1975.

Hon. RUSSELL B. LONG,
Chairman, Committee on Finance, U.S. Senate, Dirksen Senate Office Building, Washington, D.C.

DEAR CHAIRMAN LONG:

PROPOSED CONTINUATION AND/OR MODIFICATION OF FEDERAL TAX REDUCTIONS FOR INDIVIDUALS AND BUSINESSES

The Machinery and Allied Products Institute is pleased to have this opportunity to submit its views to the Senate Finance Committee concerning proposed legislation to continue and/or modify the temporary federal tax reductions enacted earlier this year. As the Committee knows, MAPI is the national representative and spokesman for the capital goods and allied product industries. For the reference of the Committee, the Institute's position on the Tax Reduction Act of 1975 was presented to the House Commitee on Ways and Means on January 29, 1975, and to the Senate Committee on Finance on March 10, 1975.

At the outset of our remarks, we commend the Committee for its decision to consider tax reductions, which may be of immediate consequence to the state of the economy, apart from the ongoing investigation of issues in tax reform. Time is of the essence, and the divisive and complex issues of tax reform should neither interfere with the Committee's evaluation of measures to stimulate the economy nor themselves be acted upon in haste. In that regard, the Institute's position on various tax reform subjects recently before the House of Representatives was presented to the House Committee on Ways and Means on July 9, 1975, and we intend to offer our views on the Senate side when the Finance Committee considers H.R. 10612 and other tax changes in the next session.

In brief summary, we support: (1) continuation of temporary tax reductions for individuals and businesses beyond 1975; (2) the House-passed extension for four years of authority for an investment tax credit at 10 percent; for the longer run and, as revenue permits, we believe the investment tax credit should be increased to 12 percent and made permanent; (3) extension of the restructured corporate income tax rate and surcharge exemption as currently in effect; (4) broader and improved applicability of tax relief provisions with respect to investments in mainly nonproductive equipment required by law to protect the general and workplace environment; and (5) when revenues permit, serious consideration of President Ford's recommendation to reduce the corporate tax rate from 48 to 46 percent.

In general, we share the consensus view that recovery from the severe recent recession is as yet a fragile thing, the somewhat uncertain path of which might well be altered by what would in effect be a substantial tax increase. Therefore,

we recommend approval of *House action* to continue tax reductions enacted in the Tax Reduction Act of 1975 as well as consideration of certain other tax law changes herein suggested. As for tying tax reductions—at the current or some greater level—to a spending reduction at this time, the Institute takes no position. This is a matter which we think must be left to Congress and the Executive Branch. On the other hand, we do feel strongly that federal expenditures must be placed under severe control.

Now let us turn to a brief discusison of our specific recommendations.

The Investment Tax Credit

On specifics, we support the House approval of an extension of the investment tax credit at the level of 10 percent through 1980. We view this as an important step in the direction of the well-documented MAPI recommendation that the Congress approve a permanent increase in the investment tax credit to 12 percent. It is important that this vital matter be dealt with now rather than in the next session of Congress. While the present 10 percent investment tax credit provision does not expire until the end of 1976, the business community needs the maximum period of time possible for forward planning of its capital expenditures.

Restructured Corporate Rate and Surcharge Exemption; Rapid Amortization

As to other business tax items, we urge that there be a continuation of the restructured corporate income tax rate and surcharge exemption, as in effect during the current year.

Also, we urge the Committee to act *now* on the matter of relief for taxpayers faced with basically nonproductive capital expenditures which are required by law. Here our special concern is with the spending which is needed to upgrade and protect the general and working environments under the Clean Air Act, the Federal Water Pollution Control Act, the Occupational Safety and Health Act, and similar statutes.

As the Committee probably is aware, the rapid amortization provisions for certified air or water pollution control facilities have not been very useful to taxpayers faced with these expenditures and they are scheduled to expire this year. We feel that it would be desirable to extend and improve this mechanism and to make it available for qualified spending under OSHA and other "environmental" statutes as well. Alternatively, these expenditures could be made eligible for a 15 percent investment tax credit.

Two supplementary points should be made with respect to this recommendation. First, the fact that the present provisions in the law providing special amortization for qualified "environmental equipment" expenditures have not been used to any significant extent should not mislead the Congress to conclude that such tax relief is unnecessary. The current law and regulations have not been used simply because of severe restrictions which they contain so that the intended support and tax relief is not available in any real sense. A further point should be underlined. Capital expenditures not only provide an important strength in an economic sense, but they are absolutely critical to modernization, expansion, productivity improvement, and the ability of the United States to compete in international markets. Financial resources for such capital expenditures are limited and have been very adversely affected by inflation. Substantial funds are required to carry out legally mandated installation of environmental and safety equipment and—without implying any criticism of these socioeconomic programs—funds spent for these purposes represent a diversion of capital resources which would otherwise be available for investment in economically productive programs. This diversion has reached substantial proportions because available data indicate that approximately 10 percent of total capital expenditures flow to investment in environmental and safety equipment. Finally, it is our view that the Congress has not been sufficiently aware of this situation and the urgent need for remedial action.

Corporate Rate Reductions

In the context of business tax reductions, we would be remiss if we did not comment on President Ford's recommendation to reduce the corporate income tax from 48 percent to 46 percent. Much has been written on the capital shortage which is developing in the United States and which, in the opinion of many students of the subject, may reach crisis proportions in the not too distant future. The effect of inflation has seriously aggravated the problem. One step in the direction of buttressing capital resources would be a reduction in the corporate income tax rate.

Any such reduction, however, must be assigned a priority among other needed tax changes in our total federal tax system. We do not urge that the Congress take this action at the present time in the light of a number of factors including our strong view that a substantially liberalized investment tax credit is of overriding importance. In addition, revenue considerations place a restraint on how far the Congress can go. There is another aspect of the situation which deserves consideration, namely, assignment of a priority between a reduction in the corporate income tax rate and significant tax reduction in the individual income tax rates for middle income tax brackets. We turn to that subject next.

Reductions for Individuals

We endorse a continuation of the tax reductions for individuals enacted in 1975. This is especially important at this time since continuation of the economic recovery in the short run will, in large part, depend on consumption expenditures. We wish to point out that when priorities assigned tax actions and revenue considerations permit, substantial tax relief is required in the middle income tax brackets. As we use the term, it applies to tax brackets which extend up to approximately $30,000 in taxable income. Many taxpayers who have reached the $20,000 to $30,000 taxable income brackets have done so by pulling themselves up by their bootstraps from lower income levels.

Moreover, they are being punished by excessive tax rates and by inflation. Further, in examining the tax positions of these individuals, it is necessary to look at all levels of taxation including federal, state, and local, not alone personal income taxes. Real estate taxes, excise taxes, so-called county surcharges, are creating what is close to capital seizure.

These comments are offered in terms of goals, equity, and what we believe to be an insufficient recognition on the part of government, including legislators, that the middle class—properly defined—in the United States is suffering an intolerable tax burden.

We appreciate this opportunity to provide the Senate Finance Committee with our views on federal tax reductions for individuals and businesses.

Respectfully,

CHARLES STEWART,
President.

[Whereupon, at 2:15 p.m. the committee adjourned subject to the call of the Chair.]