

1 EXECUTIVE COMMITTEE MEETING ON PROPOSED TAX REFORM ACT OF
2 1986

3 TUESDAY, MARCH 25, 1986

4 U.S. Senate

5 Committee on Finance

6 Washington, D.C.

7 The committee met, pursuant to notice, at 9:35 a.m. in
8 Room SD-215, Dirksen Senate Office Building, the Honorable
9 Bob Packwood (chairman) presiding.

10 Present: Senators Packwood, Roth, Danforth, Chafee,
11 Heinz, Wallop, Durenberger, Armstrong, Symms, Grassley,
12 Long, Bentsen, Matsunaga, Moynihan, Baucus, Boren, Bradley
13 and Pryor.

14 Also Present: James Baker, Secretary of the Treasury;
15 Richard Darman, Deputy Secretary of the Treasury, Roger
16 Mentz, Deputy Assistant Secretary for Tax Policy.

17 Also Present: Mr. Bill Diefenderfer, Chief of Staff;
18 David Brockway, Chief of Staff, Joint Committee on Taxation;
19 Randy Weiss, Deputy Chief of Staff, Joint Committee on
20 Taxation; John Colvin, Chief Counsel; Bill Wilkins, Minority
21 Chief Counsel; Greg Jenner, Tax Counsel, Majority; Randy
22 Hardock, Tax Counsel, Minority; Susan Taylor, Executive
23 Assistant.

1 The Chairman. The Committee will come to order, please.
2 We will start out today on Page 12 on depreciation.
3 And I indicated I had hoped we could do both depreciation,
4 ACRS and accounting today. There is one item involving the
5 investment tax credits that I would like to postpone. The
6 House, of course, and the Administration have repealed them.
7 We do, but provided a buy-back provision.

8 And, first, I want to ask the Treasury and Mr. Brockway
9 if I am correct. In the House bill, you, in essence, allow
10 the investment tax credit to be used up over the next five
11 years. Is that correct?

12 Mr. Brockway. And if they carry it over into the
13 future.

14 The Chairman. Into the future, but at least with the
15 five years we are predicting.

16 And Treasury estimates \$44 billion in outstanding
17 investment tax credits now?

18 Mr. Brockway. I think we have essentially the same
19 number.

20 The Chairman. All right. Let me address this to
21 Treasury. And is Treasury's estimate that over the next
22 five years, if we follow the House bill, we will have
23 redeemed about \$32 billion worth? Am I correct? About
24 \$32 billion worth would be used up?

25 Mr. Mentz. That is the present value.

1 The Chairman. That is what?

2 Mr. Mentz. That is the statistical probability of
3 utilization of investment credits over the five years.

4 That is right.

5 The Chairman. Senator Bentsen was asking what page.
6 I indicated that on the proposed buy back of the investment
7 tax credits I did not want to deal with those today, but
8 I wanted to get some facts in front of us as to the cost
9 on them.

10 So Treasury indicates that \$44 billion outstanding; that
11 about \$32 billion of those would be redeemed over the next
12 five years if we were to follow the House bill.

13 And I will pause there, and Treasury can correct me if
14 I am wrong.

15 Mr. Mentz. I believe, Mr. Chairman, that was assuming
16 current law. In other words, utilization of tax credits
17 under current law.

18 The Chairman. That is correct.

19 Mr. Mentz. The utilization under the House bill may be
20 less because of the rule for the minimum tax where you only
21 use a credit if you had losses, if a corporation had losses,
22 in two out of the last three years.

23 The Chairman. So under the current law you have got
24 \$32 billion in what I call redemption over five years?

25 Mr. Mentz. That is the way the statistics come out. Yes.

1 The Chairman. And the buy-back provision that is in
2 the Chairman's draft would provide purchasing those credits
3 at \$.70 on the dollar. And is it your estimate that the
4 purchase of the credits would be about \$32 billion?

5 Mr. Mentz. That is right.

6 The Chairman. So that the difference is -- and I want
7 the members to have a chance to think about this. We will
8 not take this up today. The difference is that under the
9 current law those corporations that were sufficiently
10 profitable could conceivably use up all 100 percent of their
11 tax credits.

12 Mr. Mentz. Correct.

13 The Chairman. Corporations that were not profitable --
14 and here I mean in the genuine not-profitable sense. Not
15 the accounting not-profitable sense -- would in all
16 likelihood not be able to use all or perhaps any of their
17 credits.

18 Mr. Mentz. That is right.

19 The Chairman. I mean actual. They have nothing to
20 offset them against. They have no profits to report.

21 So that the difference between the proposal and the
22 draft that I have in the current law is that we are saying
23 to some of the very poorest, if you want to call them that,
24 or non-profit corporations that have no likelihood of
25 using up their credits; we will buy them back. The tradeoff

1 is that for some very, very profitable corporations who might
2 be able to use 100 cents on the dollar of their credits,
3 we are saying to them you are going to have to sell yours
4 back at 70 cents on the dollar also.

5 Mr. Mentz. That is correct.

6 The Chairman. The reason I ask it, I notice there was
7 a story in the paper today that this provision -- or
8 yesterday -- was a subsidy for General Electric. And
9 General Electric, in all likelihood, is one of those
10 corporations that could probably use 100 cents on the dollar
11 over the five years on their credits. And that if they are
12 forced to sell them at 70 cents, this is hardly a subsidy
13 for General Electric. We are actually taking General
14 Electric, which is very profitable, and saying in the
15 purchase, in the buy back of the credit, we are going to
16 use part of what we are taking from you to distribute to
17 some companies that are simply not making any profits at
18 all.

19 Mr. Mentz. That is right, Mr. Chairman. I just would
20 add that our analysis is only over the five years. One would
21 expect that beyond the five-year period some of the investment
22 credit carryover would continue to be used. And to the
23 extent that you repurchase all of it or \$31 or \$32 billion,
24 you are, in effect, raising revenue in the outyears.

25 The Chairman. I would assume we would have to be

1 because the 31 or 32 is for the purchase of all of the
2 credits that are outstanding no matter when they might
3 be redeemed, five, 10 or 15 years from now under current
4 law.

5 Mr. Mentz. Exactly.

6 Senator Pryor. Mr. Chairman, I have a question, and
7 that question is this: Will this take a separate or a
8 special appropriation bill in order to effectuate the
9 \$31 or \$32 billion in buy out of the ITCs?

10 The Chairman. We are working on that now. It would
11 depend how the bill was drawn. If you were to make it as
12 an offset against past taxes on a carryback, you could do
13 it straight through the Finance Committee.

14 Senator Pryor. I see. My second question is: Does
15 the Treasury support the buy-back provision of the ITCs as
16 in the Packwood proposal? Does the Treasury Department
17 support this?

18 The Chairman. I will let Treasury respond.

19 Secretary Baker. Yes, sir, we do, Senator Pryor.

20 Senator Pryor. Thank you, Mr. Secretary.

21 The Chairman. David, the reason I am going to let this
22 percolate is I think a good many -- I can tell from the
23 comments a good many people are unfamiliar with what it is.
24 We can get onto ACRS and the accounting and everything and
25 we are all familiar with it. Here is a relatively new

1 provision, and I would like to have various elements of
2 the business and non-business community have a chance to
3 consider it before we vote on it so they fully understand
4 what it is. But it clearly -- of all the things it is not,
5 it is not a subsidy to the very profitable corporations
6 because they would get 100 percent on the dollar on their
7 investment tax credits because they would have enough
8 profits to eventually offset all of those.

9 Let us start now with the changes that we have made in
10 the accelerated cost recovery system. Let me state it just
11 very briefly, and then ask Mr. Brockway and Mr. Colvin and
12 Mr. Mentz if they would comment.

13 In 1981 we enacted the accelerated cost recovery system.
14 And, roughly, it was three years for autos, light trucks,
15 certain research equipment; five years for most other
16 personal property.

17 Senator Moynihan. Mr. Chairman, would you tell me what
18 page you are on now?

19 The Chairman. Page 16.

20 Ten years for certain public utility property, and
21 15 years for real estate. And the accelerated cost
22 recovery system was designed to simplify the rules. And
23 by and large, I think the business has learned to live with
24 it and like the rule. I am not talking about the length of
25 time or the classification, but I think they have come to

1 like the system itself.

2 In 1984, we lengthened the depreciation to 18 years
3 on real estate and to 19 years last year during the
4 imputed interest legislation.

5 Under the draft bill that is before us, I have suggested
6 depreciation for all real estate be lengthened to 30 years
7 straight line; that depreciation for certain long-lived
8 assets, that your shift would be lengthened from five to
9 10 years; that cars would be moved from three to five years
10 because of the evidence we had that the useful life of cars
11 and trucks was indeed even longer than five, let along
12 longer than three; and shorten the lives on computers from
13 five years to three years; and then index the ACRS if the
14 inflation were two percent or more, but not beyond eight
15 percent, although no one is predicting inflation beyond
16 eight percent for the five years that we are dealing with.
17 The eight percent figure becomes illusory. If you could
18 have it or not have it, it should not make any difference
19 in terms of revenue. And the indexing did not apply to
20 real estate.

21 Mr. Brockway, do I roughly state it correctly?

22 Mr. Brockway. That is correct, Mr. Chairman.

23 The Chairman. Now could we open it up for comments on
24 that part of it before we move on? I know there are some
25 questions and I think some possible amendments.

1 Senator Bentsen. Mr. Chairman?

2 The Chairman. Senator Bentsen.

3 Senator Bentsen. This comment, this particular type
4 of comment, I guess, is coming from a rather unusual source.
5 I think I led the fight to keep real estate from going to
6 15 years. I thought that was much too generous. I fought
7 it again when we tried to stop at 18 years.

8 Each time I thought it should be 20. And I thought we
9 were getting so generous that you were going to have a lot
10 of buildings that were going to be built for tax reasons
11 rather than economic reasons.

12 And what I prophesized came to pass. And we have seen
13 it in a lot of cities. We have seen it in Denver, and we
14 have seen it in Houston, and complicated by economic reasons
15 in addition.

16 Now we are talking about going to 30 years. That is
17 quite a change. It is far beyond what I was suggesting.

18 But what really concerns me is now you are saying that
19 if a piece of real estate was sold, a commercial building
20 was sold, you would recapture even the 30 years on the
21 straight line depreciation. And that you would go to an
22 ordinary income tax in that.

23 I thought I was being pretty tough, but I think that is
24 overkill, frankly. And then you provide for the inflation
25 factor two to eight percent is something else.

1 Now to do it on machinery is one thing, but to deny it
2 to something that goes out 30 years is quite something
3 else. Now when you do that, the vagaries in inflation are
4 not nearly as predictable, and you could have a tax on what
5 is an illusory gain that was brought about by a major part
6 by inflation.

7 So what I am saying, Mr. Chairman, is I do not quarrel
8 with you about extending it on out to 30 years, when I was
9 one who was trying to get it extended before to 20. But to
10 then say on the sale that you have to go to total, ordinary
11 income, I think that is too much. And, frankly, your big
12 gain in revenue, as I see it, is going from 19 years to 30
13 years. That is a very material gain to Treasury. And that
14 helps pay for some of the changes in this bill.

15 But to turn around again and tax it as ordinary income
16 is not that big an item. And, in turn, I think it results
17 in an inequity, and I would oppose that. And I would suggest
18 that we go back to current law insofar as recapture. And
19 that if you use straight line out over 30 years, that we
20 stay to current law.

21 Now current law says that if you took accelerated
22 depreciation then you would be subject to recapture on the
23 entire amount. But you are doing away with that anyway so
24 that is beside the point.

25 But I think we should stay with current law insofar as

1 recapture. And I would support the going out to 30 years,
2 the extension of time of the building.

3 And another thing is happening in buildings. You are
4 having on commercial buildings a much higher percentage of
5 content is going to machinery and equipment that ages much
6 faster than old types of buildings. With the high
7 sophistication that is developing in the way of elevators
8 and air conditioning and heating and all of that, that
9 technologically ages much faster than what we used to see
10 percentagewise in the buildings.

11 Nevertheless, I still support going out to the 30 years.
12 But I just do not think that you ought to be taxed once you
13 sell that on an ordinary income basis. I think that is going
14 too far.

15 And I would like to have the numbers, if Mr. Brockway
16 has them. Your big gain to Treasury, as I understand it,
17 is going from 19 to 30 years.

18 Mr. Brockway. With regard to real estate.

19 Senator Bentsen. That is right.

20 Mr. Brockway. That is correct.

21 Senator Bentsen. Yes.

22 And do you have any idea what that is, Mr. Brockway?

23 Mr. Brockway. It is probably around \$2 and \$3 billion
24 within the five-year window. Obviously, as you go out in
25 the long-run, it becomes a much more significant item because

1 real estate is a --

2 Senator Bentsen. All right.

3 Senator Baucus. I am sorry. What was the amount?

4 Mr. Brockway. About \$2 or \$3 billion. I do not have
5 a percentage.

6 Senator Bentsen. On the five years. All right.

7 Now, then, if we stay to current law insofar as how you
8 tax it, how much does that cost Treasury?

9 Mr. Brockway. With regard to the recapture?

10 Senator Bentsen. As far as the recapture. That is
11 right.

12 Mr. Brockway. That would be point three revenue loss.

13 Senator Bentsen. Point three.

14 Mr. Brockway. Within the window.

15 Senator Bentsen. About \$300 million.

16 Mr. Brockway. The way the Chairman's package works is
17 these changes only apply to property put in service after
18 the effective date so the big revenue effect is in the
19 outyears when it could turn over.

20 Senator Bentsen. Right.

21 The Chairman. You mean the big revenue losses would be
22 in outyears if we keep the present recapture provision?

23 Mr. Brockway. Correct.

24 Senator Bentsen. That is right.

25 The Chairman. And what my draft attempted to do,

1 realizing that real property normally, I say normally, does
2 not depreciation. On occasion, we have seen some farm
3 property depreciate and we hope it appreciates again. But
4 as a rule of thumb, it is true that it really does not
5 depreciate. Isn't that true?

6 Senator Bentsen. Let me point out that it depreciates
7 insofar as inflation is concerned. When you get to true
8 values, it does normally depreciates. What the Chairman is
9 talking about is an appreciation on inflation. Now if you
10 want to turn around and put the two to eight percent on
11 real estate, that is another approach to take care of that.

12 The Chairman. Well, the reason we did not put it in
13 for real estate is that real estate normally appreciates
14 with inflation and normally will appreciate slightly better
15 than inflation as a rule of thumb. It is not all real
16 estate. Whereas, machines do not. They wear out. They do
17 not appreciate. You cannot sell, normally, a five-year old
18 machine even with inflation for what you paid for a new
19 machine.

20 Senator Bentsen. Mr. Chairman, I think that helps make
21 my point. You sell it as salvage machinery normally. And
22 that is why I can understand that being taxed as ordinary
23 income. You really don't have anything there. But when you
24 start pushing something out 30 years -- and I support you in
25 that. I will go along with that. And I say once again I am

1 the fellow on this Committee as much as anybody on it who
2 said 15 years was just too fat, too rich, and we should not
3 be cutting it back to that. And notice I said 20. You have
4 done me one better. You are going to 30.

5 But once you have that, then I think it is a mistake
6 on the sale of that to tax it as ordinary income insofar as
7 that sale.

8 And so what I am talking about is giving you the
9 benefit to Treasury of the very major part of moving it
10 from 20 to 30. That on the sale, you use the current law.

11 The Chairman. Further comments?

12 Senator Chafee. Mr. Chairman?

13 The Chairman. Senator Chafee.

14 Senator Chafee. I notice that this is the same as the
15 President's proposal, and I would be interested in
16 Treasury's rationale for the support of the President's
17 proposal, and, thus, the support for this proposal.

18 Mr. Mentz. Well, Senator Chafee, the President's
19 proposal would have indexed the basis of depreciable assets,
20 including real estate. So our rationale was that because
21 the basis of the property would reflect inflation, it was
22 appropriate in that case, when it was sold, the only real
23 gains would be realized; not inflationary gains. And,
24 accordingly, we felt that ordinary income treatment would be
25 appropriate.

1 It is really not exactly the same as this proposal.

2 Senator Bentsen. I would say to Senator Chafee I made
3 that point. I said if you want to go to the two to eight
4 percent, then that is a different approach, and I don't
5 quarrel with that as much.

6 Mr. Brockway. Senator Chafee, if I could clarify one
7 thing. The Administration proposal differed in two
8 respects. The Administration did not index -- did index
9 the basis whereas this proposal does not, but the
10 Administration also treated all gain on the disposition of
11 property as ordinary income.

12 The Chairman's proposal really merely treats real estate
13 the same way as equipment is treated under present law.
14 That is that to the extent you have claimed depreciation
15 against ordinary income for the value of the property,
16 arguably going down, and you sell the property and so you
17 really did not have a loss on that property for which you
18 had previously claimed depreciation, that is brought back
19 into income as ordinary income. So that portion is a
20 wash. You cannot convert ordinary income. I think
21 that is -- into capital gain. That is the theory of this
22 proposal.

23 It does not go as far as the Administration's proposal
24 would have gone in treating all the gain on the disposition
25 as ordinary income.

1 The Chairman. But my proposal does treat real estate
2 and non-real estate the same in terms of the recapture.

3 Mr. Brockway. That is correct.

4 The Chairman. Whereas the present law does not.

5 Mr. Brockway. That is correct.

6 Senator Chafee. Yes. But the trouble is we are then
7 going to move up to consideration of Number 3 at the top of
8 the page, the indexing provision.

9 Mr. Brockway. I think on the indexing one of the things
10 that was taken into account is that under present law
11 equipment received the investment credit as an incentive
12 for investment in equipment. If you would merely repeal the
13 investment credit and then index both real estate and
14 equipment, that the relative benefits would be increased
15 for real estate as compared to present law vis-a-vis equip-
16 ment. I think one of the considerations that was taken into
17 account is that for -- and one of the reasons for the
18 indexing of equipment is that equipment will be losing the
19 investment credit, and there was a desire to keep that a
20 relatively more attractive investment than a real estate
21 venture, for example.

22 Senator Bentsen. When you structure it to 30 years,
23 you have made a very major change that you have not seen to
24 that extent on equipment.

25 And, again, I am not quarreling with that. But you either

1 have got to give them credit, as the Administration did,
2 for an inflation index to get rid of taxing some illusory
3 property, or you ought to stay to current law insofar as
4 giving credit for straight-line depreciation.

5 I am concerned, Mr. Chairman, about an overkill.

6 The Chairman. I would come back again -- going through
7 my conversations with the members -- that if there is any-
8 thing that was mentioned frequently it was that we have got
9 to do something about our competitive problem with Japan
10 and our competitive problem overseas. And the Japanese are
11 not competing with us with buildings. They are with
12 machines.

13 And the members certainly expressed to me a feeling that
14 we have been very, very generous with real estate and that
15 if we went to 30 years, and the real estate is going to rise
16 with inflation and the personalty is not going to rise with
17 inflation with except for very unusual commodities perhaps,
18 it will not rise with inflation.

19 Senator Bentsen. Mr. Chairman, I could not agree with
20 you more. I have been on that side of the argument. It is
21 just doing too much. You can do an overkill. And that is
22 one of the problems we run into in the Congress when see
23 something that is wrong so often we overcorrect.

24 And you keep going back to inflation. Well, then,
25 all right, give them the inflation index like the

1 Administration did, if you want to. Now when you do that,
2 you run into a problem on installment sales and how that
3 works. And it will be some competition in doing it in
4 that regard.

5 I think the cleaner way would be to just have the
6 straight-line depreciation allocation out over the 30 years.

7 The Chairman. Further comments?

8 Senator Baucus. Mr. Chairman?

9 The Chairman. Senator Baucus.

10 Senator Baucus. Mr. Chairman, I am just wondering how
11 the repeal of the ITC comes in here. That is, in
12 determining the relative value of equipment versus real
13 estate.

14 The point I am trying to make is that since the ITC
15 applied only to equipment, not to real estate, it seems to
16 me that if we repeal the ITC it relatively helps real estate
17 compared with equipment. And I am wondering how --

18 The Chairman. I am assuming we have not gotten to it
19 yet. I indicated that earlier, Max. I am assuming we are
20 going to repeal the investment tax credit. The President
21 did, the House did, we will.

22 Senator Baucus. That is the assumption I make.

23 The Chairman. The question is whether we go ahead with
24 the suggestion I have made about a 70 percent buy back or
25 whether we simply let it play out. It is about the same cost

1 over five years.

2 Senator Baucus. That is correct. The point I am trying
3 to make is how does real estate fare compared with other
4 investments. It seems to me that if we do repeal the ITC
5 that on a comparative basis, anyway, that tends to favor
6 real estate as opposed to equipment.

7 Senator Bentsen. I don't think so because when you move
8 it up from 19 years to 30 years, you are talking about a
9 very substantial change. But then to turn around in
10 addition to that and then say on the sale of the building
11 you tax it all as ordinary income, I am quite willing to --

12 Senator Baucus. I agree with those two points you have
13 made, but it seems to me on the other side there is a
14 relative value --

15 The Chairman. If I could ask Mr. Brockway a question.
16 Prior to 1981, wasn't the average depreciation life on real
17 estate -- and I realize you literally had to average the
18 average -- around 27 or 28 years?

19 Mr. Brockway. Yes, Mr. Chairman. You would have to
20 look at very different types of buildings in different ways
21 that they depreciated those buildings. It would be that
22 order of magnitude. Around 30 years.

23 The Chairman. And was it indexed?

24 Mr. Brockway. It was not.

25 The Chairman. And did somehow office buildings get

1 built? You don't need to answer that. Of course, they got
2 built. They got built all over this country at 28 years
3 and no indexing.

4 Senator Bentsen. And how were they taxed when they were
5 sold?

6 Mr. Brockway. They would have had a capital gain
7 recapture on the sale on most buildings except where they
8 claimed accelerated depreciation.

9 Senator Bentsen. That is right.

10 The Chairman. Then they could not take the capital gain
11 on the acceleration.

12 Senator Bentsen. Well, that is right. Of course not.
13 And no one is asking for that.

14 The Chairman. Further comments?

15 Senator Chafee. Mr. Chairman?

16 The Chairman. Senator Chafee.

17 Senator Chafee. I think everybody has got to understand
18 what we are talking about here. The ordinary income tax
19 only apprised to the extent you have taken the depreciation.
20 And the gain you get is treated as capital gain. So you
21 have taken your depreciation as an expense as you go along
22 and now as you recapture it, to treat that as capital gains,
23 seems to me, to be very odd.

24 The Chairman. I think that gives you a double benefit.

25 Senator Chafee. Yes. I cannot understand the --

1 The Chairman. Let me use the example, if I can, on
2 personal property but because we would be treating personal
3 and real the same -- and you correct me again, if I am
4 wrong.

5 Let us say you buy a piece of equipment for \$10,000.00.
6 You claimed \$1,000.00 in depreciation. You sell it for
7 \$11,000.00. Under the law, as I understand it, you would
8 only get \$1,000.00 -- I mean as I am suggesting it.
9 One thousand dollars on capital gain and \$1,000.00 would be
10 regular income but you have already depreciated the thing
11 to \$1,000.00.

12 Mr. Brockway. That is correct.

13 The Chairman. All I am suggesting is that real estate
14 be treated the same way.

15 Senator Chafee. That is what we are suggesting here.
16 What the Chairman is suggesting would be treated exactly
17 the same as personal property. Where you have depreciated
18 it, when you recapture that amount of the depreciation,
19 only that amount is ordinary income, then your gain, you
20 are taxed as capital gains.

21 Senator Bentsen. Well, let me say to that that that is
22 not a true analogy because what you are talking about on
23 equipment is over a very short period of time traditionally.
24 And what you are selling is salvage equipment. But what you
25 are seeing over a long period of time is inflation taking

1 effect in that and you will get yourself an illusory gain,
2 and the taxes made on it, and you will make an ordinary
3 income tax.

4 Now I am quite willing to do what the Administration has
5 recommended and go ahead and do the inflation factor to
6 that. But you do have some problems on installment sales
7 making that work. Or to go just to the straight line and
8 have current law in regard to that, but move it out to
9 30 years.

10 What you are getting into, I think, really is an overkill
11 on this deal to correct something that I have been trying to
12 correct for a long time.

13 Senator Chafee. Well, it seems to me we are talking
14 two different things. If we are talking the recapture,
15 that is one thing. If we are talking the gain, which
16 involves the indexing and the appreciation, that is something
17 quite different.

18 But as I understood what you were directing your
19 volley at here was at the recapture of the depreciation.

20 Senator Bentsen. But, you see, much of what you do have,
21 the depreciation, that takes place. Those are the facts of
22 life. Buildings get outmoded on their equipment. But it
23 has been compensated for often by inflation which is an
24 illusory replacement. That is not the real money.

25 And then you turn around and tax that on ordinary income

1 basis. So the Administration tried to meet that with an
2 inflation index.

3 I am willing to go that way or to just go to current
4 law and move it up from 19 years to 30 years.

5 The Chairman. At the moment what the draft is trying
6 to do is to encourage people to buy machines and to buy them
7 rather rapidly and to turn them over rather rapidly. At the
8 moment, we don't even allow indexing on straight out capital
9 gains. And that argument has been made over and over. You
10 buy stock now; you have got a 20 percent inflation; the
11 stock goes up 20 percent and you sell it, it ought to be
12 the same. But we do not index capital gains.

13 Most real estate will rise with inflation. Again,
14 before some of the members came in, I said there have been
15 some exceptions on farm land. It has gone down rather than
16 going up.

17 But most real estate will go up with inflation, and most
18 of it will go up a little bit more than inflation. And at
19 the same time, it is being depreciated. And I just agree
20 with Senator Baucus and Senator Chafee. I think that if
21 we want to emphasize the kinds of investments we are going
22 to try to emphasize, then I think we ought to stick with the
23 draft the way it is.

24 Senator Wallop. Mr. Chairman?

25 The Chairman. Senator Wallop.

1 Senator Wallop. Even if that is true, and for the sake
2 of argument I will grant that it is true that most real
3 estate goes up, it still does not take care of that which
4 does not. And there is a substantial portion of it that is
5 not farm real estate in which those take place.

6 And while you say that what the bill tries to do is to
7 accelerate the purchase of machinery and equipment, in
8 point of fact it fails thereto. The studies that I have
9 show that the present value of the stream of tax credits and
10 deductions on investments in most of the productive
11 machinery and equipment that are covered in this bill
12 declines from 99 percent to 84 percent.

13 The Chairman. Say that again.

14 Senator Wallop. That the present value of the stream of
15 tax credits and deductions and the capital cost recovered
16 on investments in most of the machinery and equipment that
17 is covered by this bill declines from 99 percent to 84
18 percent. And in the process, the U.S. capital cost
19 recovery system, in terms of present values, declines from
20 fifth in the stream of nations with whom we do trading to
21 15th.

22 And I do not think that is what our -- you know, what
23 we hope to achieve out of this is to reduce the competitive
24 circumstance of capital cost recovery in this nation versus
25 those nations with whom we have the most competitive trading

1 circumstances.

2 The Chairman. Let me ask Mr. Brockway, before I call
3 on Senator Roth, if you have those figures that you gave me
4 at the start of the markup on the relative cost of capital
5 formation, current law, House bill, President's proposal
6 and this draft?

7 As I recall, this draft was better for capital formation
8 by a slight margin than even current law. It was
9 significantly better than the House bill. It was slightly
10 less than the President's bill.

11 Senator Wallop. That is if you just stop at capital.
12 You have got the rest of the tax structure in there that has
13 changed. That is why the bill relates as a whole. The
14 figures that I am quoting are Arthur Anderson figures.

15 The Chairman. I think he was talking about the whole
16 bill.

17 Mr. Brockway. Well, I think the difference in the
18 numbers, Senator Wallop -- you are talking about the present
19 value of the depreciation, the ITC. And the numbers that
20 I heard you read out, I think I have slightly different ones.
21 I think that just depends upon the discount rate.

22 But that is just looking at the present value of the
23 cost recovery; not giving any benefit for the rate of the
24 change in -- you are talking about, I think, the present
25 value of --

1 Senator Wallop. No, I'm not talking present value in
2 the present code. I am talking in terms of present value
3 in dollar recovery.

4 Mr. Brockway. Correct.

5 Senator Wallop. It declines from 99 percent to 84
6 percent. Presently, it might not.

7 Mr. Brockway. Of the present ACRS and ITC, and it
8 reduces by your numbers down to 84 percent under this bill.
9 But that only looks at the cost recovery provisions. It
10 does not look at the benefit from the rate reductions that
11 you get on the property.

12 The cost of capital numbers which Treasury has used to
13 analyze this and the numbers that we provided to the
14 Chairman try and look at in the aggregate what the impact
15 is on, one, the change in the cost recovery provisions, and
16 also offsetting that with the benefit you get from the
17 lower rates on the property.

18 Senator Wallop. But, you see, the rate reduction is of
19 no benefit except to those with -- of no real benefit, given
20 the -- the thing that I hate so bad I can't remember the
21 name of it.

22 (Laughter)

23 The Chairman. The minimum tax?

24 Senator Wallop. The minimum tax.

25 (Laughter)

1 Senator Wallop. I just have a hard time getting that
2 out on my tongue.

3 (Laughter)

4 Senator Wallop. But in point of fact, the only
5 beneficiaries of those are old companies whose investment
6 stream is essentially static or declining. All the new
7 businesses, all the growing businesses, all the ones that
8 are going to be doing lots of investing are going to be
9 declining in their relative positions. And that just does
10 not seem to me the idea that a Republican administration
11 wants to encourage -- is fossilized business structures.

12 Mr. Brockway. First, if I could just respond on the
13 cost of capital numbers, the Chairman's request. Right
14 now, using this methodology, the cost of capital would be
15 eight point two. And under the Chairman's draft, would
16 drop down to eight point zero as compared to the House bill,
17 which would have -- it would have increased from present
18 law.

19 But in terms of who benefits, I think, that, in fact,
20 if you are a growing business and a high profit business,
21 which is why I think, for example, computer companies tend
22 to like it, they do have -- if you have substantial tax
23 liability, the rate reduction benefits from it.

24 What tends to happen, I think, is that some declining
25 businesses do not have substantial tax liability because

1 they are not generating a lot of profits. And, obviously,
2 for that business, a rate reduction would be less
3 significant.

4 But a highly profitable business will have a
5 significant benefit from a rate cut, and so will the extent
6 it pays out, for example, dividends to its shareholders,
7 there will be a benefit there in terms of aggregate cost
8 of raising money to run the business.

9 Senator Wallop. I can tell that you and I have a long
10 way to go before we see eye to eye on the effects of this.
11 I have not seen any study that justifies that conclusion.
12 I have heard yours, but I have not seen it.

13 Mr. Brockway. In terms of who tends to benefit from
14 rate cuts. All I am saying is I think it turns on whether
15 or not you have substantial current tax liability.

16 Senator Wallop. But the rate cut is only a portion of
17 the tax conclusions that this bill seeks to achieve. Isn't
18 that the truth? I mean you recapture most of what you
19 reduce in terms of the excise taxes, which is another --
20 depending on where you are in the capital stream, that is an
21 increase in the cost of capital. And in your fairness
22 provisions. I won't say it.

23 Mr. Brockway. I think actually on the minimum tax both
24 these numbers are somewhat different because there you
25 don't even get the same depreciation system. Obviously, it

1 would be a different analysis if you looked at someone who
2 is on that.

3 But, again, I think that they tend to be more so from
4 the studies that I have that -- for example, minimum tax,
5 that might be a lower profit company that wasn't -- the
6 higher profits you have, the higher your taxable income is
7 and the more you are likely to be on the regular tax system
8 in the structure.

9 Senator Wallop. The regular tax system. But that is
10 where you stop because then you don't pay the minimum tax
11 if you don't have all these preferences. So that if you
12 are not investing in new equipment, new machinery and
13 generating preferences that are allowed and encouraged under
14 the code -- in other words, if you are basically a fossil
15 industry whose investment stream is accomplished, you don't
16 come under the minimum tax. And, therefore, there is no
17 increase in the cost of capital because you are not spending
18 any or you are not investing particularly.

19 You may be profitable under there and then you are just
20 paying straight corporate income tax. But if you are
21 investing and achieving the very preferences which we are
22 now trying to decide, they are the ones that are taken away
23 as you come around the other corner on the minimum tax.

24 The Chairman. Senator Roth and then Senator Armstrong
25 and then Senator Bentsen.

1 Senator Roth. Mr. Chairman, I want to underscore what
2 Senator Wallop has just said. I feel -- I listened to the
3 discussions yesterday on the natural resources, and I must
4 say that I sympathize with much that was said. I think it
5 is critically important that in developing tax policy we
6 do what is necessary to be competitive. And for that reason,
7 I have a lot of sympathy for what you are trying to do in
8 both the area of timber and other natural resources, including
9 mining and oil.

10 It seems to me that if this country is going to survive
11 as the leading industrial nation that that must be our
12 primary goal.

13 What I am concerned about in these discussions here is
14 that so much of our attention is being directed to revenue
15 numbers -- how much it is going to cost or isn't going to
16 cost -- when I feel that the principal goal and objective,
17 in addition to fairness -- and I think we have all given
18 up on simplicity. As Senator Long has said, we have never
19 seen a simple bill yet.

20 But in any event, I think it is important that we
21 develop the kind of policies that are going to enable this
22 country to be competitive in international markets. We
23 certainly aren't that in the case of mining. We are falling
24 behind in oil and gas. Agriculture has bad problems.

25 But I am not satisfied as to what is happening in our

1 basic industries. I think that if we are going to have a
2 chance to compete in world markets tomorrow we had better
3 take a very, very careful look as to whether our tax policy
4 is not only going to help our industry modernize, become
5 number one, but to continue to modernize with the constant
6 changes that are taking place in this technological
7 revolution.

8 I think we are overlooking that. And I am very worried
9 that what we are doing in tax reform is going to be anti-
10 growth and anti-job.

11 Now this brings me to the point that Senator Wallop and
12 others of us are concerned about, and that is the cost of
13 capital.

14 Now as I understand it, under the House bill, the cost
15 of capital for equipment increases by about 50 percent over
16 current law. And I am not talking about the current -- or
17 the income tax. I am talking about the cost of capital
18 solely for equipment. It increases 50 percent.

19 Now your proposal is far better, as I understand it.
20 The equipment cost of capital would be only 25 percent
21 higher than current law.

22 But I think there are a number of us that feel that this
23 does not go far enough. And we do intend to offer proposals
24 at the appropriate time to modify this in the interest of
25 long-term growth. As you probably know in my so-called Roth

1 Reforms, I proposed an expense cost recovery system which
2 would allow 50 percent of cost assets to be expensed. Now
3 that produces a cost of capital about 15 percent higher
4 than current law.

5 There are other ways, of course, of skinning the cat.
6 We could keep the ACRS; have a 200 percent declining balance
7 method of depreciation, which would be roughly the same as
8 I have proposed.

9 But in any event, I would like to have, if we could,
10 revenue estimates on these two options -- the ECRS as well
11 as the 200 declining balance. Because as I have said, I
12 think there is a number of us that do intend to offer an
13 amendment at the appropriate time in this area.

14 The Chairman. Senator Armstrong.

15 Senator Armstrong. Mr. Chairman, I just wanted to
16 direct a question to Senator Bentsen.

17 I share some of the concerns that you have expressed,
18 but I am not quite sure what I am going to do about that.
19 Are you going to move an amendment or would you think about
20 this for a while?

21 Senator Bentsen. I am going to work with the Chairman
22 on this. And what I am saying is I would like to see us
23 move to either the President's proposal or to take the
24 Chairman's proposal on the inflation indicator that he has
25 put on other types of equipment. That is where I would like

1 to see us move. But what I am talking about is significant.

2 Senator Armstrong. But we are going to have a few days
3 to think about this, a day or two?

4 Senator Bentsen. And I am quite willing to defer it as we
5 take a look at it, Mr. Chairman. We let you accomplish the
6 vast majority of the income that you are talking about, as
7 I understand it, \$2 to \$3 billion, over the five years, and
8 that what we are talking about is approximately \$300 million.

9 But to me it is a basic issue of fairness in trying to
10 stop the overkill. And I am quite willing to defer it and
11 let us take a further look at it, if you would like to do
12 that, Mr. Chairman, with the understanding that we have not
13 foreclosed this item at all and it will be further
14 addressed.

15 Senator Heinz. Mr. Chairman?

16 The Chairman. Senator Heinz.

17 Senator Heinz. Mr. Chairman, I would hope that the
18 Chair would work with Senator Bentsen, Senator Roth and
19 myself and others on some problems we have with this section.
20 I share Lloyd Bentsen's concern that while there are some
21 definite changes that can and should be made in the real
22 estate area -- the current lives are very short indeed
23 compared to the lives of real property -- that we may be
24 moving far too far too quickly in that area.

25 By the same token, the Chairman's draft makes very

1 far-reaching changes with respect to the depreciation
2 allowances for productive equipment. And Bill Roth has
3 cited some numbers -- 50 percent, 25 percent. Frankly, I
4 find what we have gotten from the staff so far pretty hard
5 to evaluate as of 9:30 last night. The revenue estimates
6 that were handed to me this morning at about 9:35 were not
7 available in spite of the fact that we were assured they
8 were going to be available at 6:00 last night.

9 And I intend, unless we can work an appropriate
10 compromise out, to join with Senator Roth and others in
11 offering an alternative to the changes in ACRS that you have
12 made here on equipment that is used for manufacturing.

13 I think it would be better to try and work something out
14 with you rather than just engage in a series of votes. But
15 if that is the only alternative we have got, I guess we
16 will have to do it, even though I do not think it is the
17 best way to proceed.

18 The Chairman. As I indicated in the letter you should
19 have got this morning, it will be most helpful to me, and
20 I think to the Committee and especially when we will be
21 able to announce six, seven, eight days ahead of time
22 which order we are taking things up, if you have got
23 amendments or questions, if we can have them ahead of time,
24 they can often be worked out. They are difficult to work
25 out if they come up for the first time that we bring up the

1 subject and no one else knows anything about them other
2 than you -- or maybe you and one other person that has
3 worked on them.

4 Senator Heinz. Mr. Chairman, that is exactly the way
5 I feel about your draft. It is very difficult to work up
6 amendments to a draft the revenue estimates of which are
7 only known to a few staff members the night before we take
8 up the items.

9 I think all of us want to be as responsible as possible,
10 and it is rather difficult to work up an amendment without
11 knowing what the revenue impact of either the amendments
12 are or on the provision of the Chairman's proposal that you
13 are amending.

14 So it may be, Mr. Chairman, we just do not have the
15 information we need for the next day or two to go through
16 and make any decisions because we find it very difficult to
17 analyze what we have got.

18 The Chairman. Further comments?

19 Senator Baucus. Mr. Chairman?

20 The Chairman. Senator Baucus and then Senator Bradley.

21 Senator Baucus. Mr. Chairman, I am just curious what
22 the Treasury view is of your package on the capital cost
23 recovery. I recall those in the House -- the President sent
24 a letter to the House Republicans saying that in the Senate
25 he would work to restore some capital cost provisions. The

1 bill is in the Senate. I know that your package, I think,
2 at least as I recall, loses about \$2 billion whereas the
3 House bill is 27. It actually gains \$27 billion over the
4 period of the bill.

5 I am just wondering, Mr. Secretary, if you could tell
6 us the degree to which the Chairman's package fulfills the
7 wish of the President in restoring some of the capital cost
8 provisions that were taken away from industry in the House
9 bill.

10 Secretary Baker. Senator Baucus, we think that the
11 Chairman's package meets the commitment in the President's
12 letter to House Republicans with respect to capital cost
13 recovery with respect to depreciation.

14 We would like to see some improvement in the Chairman's
15 draft, as we have discussed with the Chairman, with respect
16 to the cost of capital. And we would like to see the
17 overall cost of capital be closer to Treasury 2 than the
18 Chairman's draft is.

19 Senator Baucus. As I understand, Mr. Secretary, you are
20 basically saying that you would like some improvement in
21 the present package, but that as the package now stands on
22 those provisions that the package does meet the President's
23 objective as stated in that letter?

24 Secretary Baker. Well, it meets the requirements of
25 the President's letter to House Republicans, Senator Baucus.

1 I must reiterate that we would like to see the cost of
2 capital closer to the cost of capital as computed in
3 Treasury 2.

4 Senator Baucus. Thank you.

5 The Chairman. Senator Bradley.

6 Senator Bradley. Mr. Chairman, I would just like to,
7 if I could, not make a comment about a specific aspect of
8 the depreciation package but a more general comment, and
9 then a request for some information.

10 I mean it seems to me that what depreciation is supposed
11 to do is to give people who buy machines or invest in
12 asset X, Y or Z enough money at the end of the useful life
13 of that asset to buy a new one. I mean that is basically
14 what economic depreciation is.

15 And this Committee has made a decision that we want to
16 be more generous than economic depreciation, which I
17 understand and can understand why.

18 What I hope we would not do is compound some of the
19 errors of the 1981 Act and skew incentives among types of
20 assets so that it is a total hodgepodge. I mean my ideal
21 would be to try to get useful lives and try to provide a
22 uniform, more generous incentive for specific useful life
23 assets, and then let the market allocate the capital.

24 But I think we are heading down a road where we are
25 going to be making a lot of ad hoc judgments without being

1 able to get the information we need to determine whether
2 it will be a basically balanced approach. And I think one
3 of the bits of information that I would like to get, if we
4 could, is what the effective tax rates are under this
5 depreciation proposal by asset types.

6 I mean, for example, under the Treasury 1 and under
7 Treasury 2, what is a five-year category was split up into
8 four categories. Now we have lumped a lot of things into
9 that five-year category here.

10 And I think that we really need to get what are the
11 effective tax rates by asset type in order to see that we
12 are not skewing this investment all over in ways that none
13 of us had determined that we would like to do.

14 The Chairman. The reason for that -- and then I will
15 call on Senator Moynihan -- was to try to strike a balance
16 between confusion and simplicity. I grant you that in a
17 perfect world -- and there are some perfect worlders -- you
18 would say that the economic depreciation of every asset
19 is going to be exactly its useful life, assuming even a
20 business person knows what that is at the time they buy
21 the asset.

22 But for the sake of argument, let us assume that they
23 can figure it. And some might be four years, and some might
24 be five years, and some might be five years and five months,
25 and some might be six years, and you are going to have a

1 perpetual battle between business and their accountants
2 and the IRS as to what is the useful life of this piece of
3 equipment.

4 So we tried to strike a reasonable balance. And we
5 said computers are three years, machines are five. Now
6 somebody buys a machine and they say, well, that is a
7 computer; that is three years. All you are going to have to
8 argue is to whether it is a machine or a computer.

9 But it was an effort to strike simplicity. Is every one
10 of the classes exactly on it as to exactly what the life
11 is? No, probably not. There may be some computers that
12 don't have a useful life of two years, and there may be
13 some that have a useful life of four.

14 But it was an effort to strike some certainty, and,
15 therefore, simplicity.

16 Senator Bradley. Mr. Chairman, the Commerce Department
17 has a Bureau of Economic Analysis, and they do a regular
18 study on what is the service life of various kinds of
19 assets. And in their latest data, if you look at what is
20 in our five-year category, it ranges from assets with service
21 lives of 27 years to assets with service lives of eight
22 years. And we have jammed all of that into a five-year
23 category.

24 And I am just saying that I do not think that that is
25 a very rational way to go about it. And I think a way to be

1 helpful would be to -- can Treasury or Joint Tax give us
2 effective tax rates by assets?

3 Mr. Brockway. Well, we certainly can do that type of
4 analysis. I would very much like to emphasize the point
5 that it is very sensitive to the assumptions you make. You
6 cite the BEA statistics. They do not do a current study.

7 One of my problems with the BEA lives is that those
8 are based on essentially a Bolt and F that was concocted
9 in 1942 based on surveys done in the 1930s. One of the
10 major problems in structuring depreciation systems and to
11 try and get them exact is not having good data on what even
12 the average lives are of different types of equipment -- what
13 the average life of a computer is, for example. What the
14 average life is of an aircraft. There are very substantial
15 problems with any of that data.

16 In fact, I would be more comfortable probably using the
17 ADR mid-points as a guide. But you could do effective rate
18 studies either based off the BEA lives or off of the ADR
19 lives that would give you, once you crank in all the
20 assumptions you wanted to make, how much debt financing
21 you would to take into account, so on and so forth, you
22 could come up with that analysis. It would give you a very
23 rough guide; not a precise guide whatsoever. A very rough
24 guide as to how the relative tax burden on different types
25 of assets.

1 Senator Bradley. Well, could Treasury tell us why they
2 split the five-year category into four different categories?

3 Mr. Darman. Senator Bradley, the reason is generally
4 the one that you have in mind -- trying to be more precise
5 in classifying these assets in order that one can achieve
6 more nearly equal effective tax rates for different
7 categories of assets.

8 The price you pay for that, on the other hand, is a
9 degree of increased complexity and for some categories of
10 assets, less acceleration than I think some members of this
11 Committee would want.

12 Senator Bradley. Well, Mr. Chairman, will anyone do
13 that analysis in the Joint Tax Committee on effective tax
14 rates or not? Or are we just going to proceed? Treasury
15 must have had some analysis that allowed them to break
16 the fifth category into four different categories.

17 Mr. Darman. Senator Bradley, we would be happy to share
18 with you what analysis we have. I might just say that, as
19 Secretary Baker said, we would like to see some improvement
20 in the cost of capital in Senator Packwood's proposal. But
21 Senator Packwood's proposal is, in fact, by our calculation
22 probably the most level in effective tax rate across
23 categories of investment of any now on the table -- that
24 is ours, the House's and current law. It is probably the
25 most level in effective tax rate.

1 Senator Bradley. Well, Mr. Chairman, I don't want to --
2 The Chairman. I will try to have Joint Committee get
3 you the useful lives you want, so long as you remember that
4 my draft was not an effort to make every life exactly its
5 useful length.

6 Senator Bradley. I understand that.

7 The Chairman. And that I was trying to strike this
8 balance of simplicity where if you had a machine that had
9 an average range of four to six years, I might have put it
10 in the five-year category.

11 Senator Heinz. Would the Senator from New Jersey
12 yield for a question?

13 Senator Bradley. Sure.

14 Senator Heinz. The Senator from New Jersey mentioned
15 the term "effective tax rates" on the specific investments.

16 Senator Bradley. Yes. By assets.

17 Senator Heinz. What is an effective tax rate on an
18 investment? Does it mean we should be taxing investment?

19 Senator Bradley. It means what you pay on that asset
20 after you have depreciated it basically.

21 Senator Heinz. And so the Senator from New Jersey
22 believes that there should be a tax on investments?

23 Senator Bradley. I believe there should be a tax on
24 income. Income is determined a variety of ways. Some ways
25 it is after depreciation.

1 Senator Heinz. And what does the Senator view as the
2 appropriate measure of cost recovery? Should the cost of
3 an investment be recovered free from tax or not?

4 Senator Bradley. The issue here is not the rates. The
5 issue is trying to have some balance so that you do not
6 give some assets a much bigger incentive unintentionally
7 simply because you have lumped them into one category.
8 And that is the whole purpose of --

9 Senator Heinz. I understand the desirability of having
10 some kind of conceptual neutrality in investments. It is
11 difficult to define it, and you have a methodology that you
12 believe is useful in analyzing neutrality, which you call
13 the effective tax rate on investment.

14 It is not clear to me whether it is a valid method of
15 analysis.

16 Senator Bradley. Well, I will do my best over the next
17 couple of weeks, Senator Heinz, to convince you that it is
18 valid. But I think it would be helpful in being able to do
19 that to get the material from Joint Tax and from the
20 Treasury.

21 And, Mr. Chairman, I will say that when we get that
22 material at some appropriate time in the future I would be
23 intending to offer an amendment on this depreciation section.

24 The Chairman. Senator Moynihan.

25 Senator Moynihan. Mr. Chairman, my question has been

1 asked by Senator Bradley, but I will go through it just
2 a little bit and really ask for the judgment of the
3 Secretary and Mr. Brockway about this question of effective
4 tax rate.

5 We have a letter, for example, from the Institute for
6 Research in the Economic Taxation, a respectable board.
7 The chairman is the managing director of Arthur Andersen
8 and the President's former under secretary of Treasury who
9 we know does not approve this bill.

10 But men like Freelow Harris and others command your
11 attention. And it says that under current law most machinery
12 and equipment, ACRS 5 percent property, faces an effective
13 tax rate of two point five to six percent. And then it
14 goes on to say that under the Chairman's proposal this would
15 rise to six point zero nine percent. And that is what
16 Norman Ture was sort of saying to us, and he is on this
17 board.

18 But I guess two questions: One, is this an art that
19 attains to any percision? I mean do economists agree among
20 themselves on what the effective tax rate of this provision
21 would be or that provision would be? Is it something that
22 the profession has down to the point where, you know, it
23 is the generally accepted accounting principles?

24 The Chairman. Could I ask the Senator a question? I
25 am curious. I have a sense of deja vu. Didn't we go through

1 this with Norman Ture at the --

2 Senator Moynihan. Yes.

3 The Chairman. And there were a couple of other
4 economists with him?

5 Senator Moynihan. Yes.

6 The Chairman. And I think you posed that exact question.

7 Senator Moynihan. Yes. And I didn't get an answer
8 then.

9 The Chairman. No. That is what I thought.

10 (Laughter)

11 The Chairman. I think what you got was that the
12 answer was no; they did not agree among themselves that
13 you could estimate effective tax rate.

14 Senator Moynihan. I think that is the answer I got.

15 But Mr. Brockway is sometimes -- it helps to ask one
16 person so you get one answer.

17 Mr. Brockway. Well, I think the answer would be no,
18 the short answer. The long answer is that all these
19 analyses are very sensitive to what assumption you make,
20 what assumption is truly economic depreciation, what
21 assumption you make as to how much debt financing there is
22 or whether you assume it is all equity financing.

23 They are useful for trying to answer the question
24 Senator Bradley raised about measuring the effective rates
25 across assets to see whether you have a relatively neutral

1 system. They are useful that way.

2 They are not terribly useful -- if I did an effective
3 rate analysis, we came up with that, we published that in
4 the past, and we will do them for the Committee here, that
5 is not our saying that we think that if you change your
6 system in that regard that after 10 years corporations would
7 be paying that same rate of tax on their income. There are
8 a lot of other things that go into measuring what effective
9 rate of taxes you compare. Let us say the book profits
10 to the actual check they send into the government. These
11 are not attempting to measure that kind of issue, which I
12 think is frequently what people are thinking about.

13 Senator Moynihan. Are you saying like a fair number
14 of measurements, the measurement itself may be quite
15 inaccurate, but it might accurately reflect differences
16 between one category and another? And you know one is
17 higher and the other is lower as it were.

18 (CONTINUED ON NEXT PAGE)

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1 Mr. Brockway. That is correct, and you might do a
2 measurement that is very accurate for what it purports to be.
3 But one of the problems with this is that what it purports to
4 be is not really, I think, what many you think in terms of.
5 When I say "effective rate of tax," I think you are probably
6 thinking about, "Well, how much income did this company have
7 and what tax did they pay?" This does not purport to do that
8 at all; it is a stylized investment, the marginal investment,
9 assuming it made a 4-percent real rate of return, assuming it
10 it is financed with x-amount of debt and y-amount of equity
11 -- a variety of assumptions -- and it is purely a stylized
12 item. But it is useful for trying to design the system.

13 Senator Moynihan. Comparison. Yes, exactly. So, you
14 are going to give us your range?

15 Mr. Brockway. Yes, sir.

16 Senator Moynihan. Otherwise we are left with Mr. Turez,
17 which I think is rather ominous.

18 Thank you, Mr. Chairman.

19 The Chairman. Senator Chafee, and then Senator Armstrong.

20 Senator Chafee. Mr. Chairman, what do you wish from us
21 at this moment? Are you asking us for comments on anything
22 in the accelerated cost recovery section here, before we move
23 to accounting? Just general comments, without necessarily
24 amendments?

25 The Chairman. I would like that, because the accounting

1 section has some significantly parts of it unrelated to
2 depreciation.

3 Senator Chafee. Well, Mr. Chairman, I think, as we go
4 through this, we have got to all bear in mind that down the
5 line there are things that we presumably are going to wish
6 to take out of this bill that are going to be big-ticket items
7 and cost a lot of money. One of them undoubtedly is the
8 excise tax, and I think there is considerable sentiment that
9 we have to look at that very carefully and probably cut down.
10 And that is, I believe, Mr. Brockway, \$62 million -- is it?
11 -- plus another \$15 billion attached to it and linked to it
12 closely.

13 Mr. Brockway. That's right.

14 Senator Chafee. Then, also, I for one am deeply
15 disturbed over what I consider to be the unfair treatment of
16 the federal employees' pension system on the three-year
17 rule.

18 So, in looking at these items, I think we have got to
19 look at where we can possibly pick up some money to pay for
20 those items, if indeed we wish to change them.

21 And Mr. Chairman, you asked for our comments here. On
22 page 19, that indexing, the proposal that you have got, as
23 I understand the figures, is minus-\$4.3 billion. In other
24 words, that is what it costs us over present law. And I am
25 unenthusiastic about that provision. I like the House

1 provision better that has a zero-figure on it. Correct me if
2 I am wrong on these figures, Mr. Brockway.

3 Mr. Brockway. The revenue cost for the House is zero.
4 Senator Chafee. Zero. Although, in the out-years, it
5 will probably cost something, because there is a partial
6 indexing for inflation.

7 Mr. Brockway. Well, on that, Mr. Chafee, the reason why
8 it is zero, the assumption is that there is a 4-percent
9 inflation on an ongoing basis. We just straightlined it for
10 what inflation is. And the House bill only indexes for
11 inflation over 5 percent. So, in effect, the revenues just
12 assume that there will be no indexing under the House bill;
13 although, in fact, if inflation did exceed 5 percent in the
14 House bill, there would be a revenue loss.

15 Senator Chafee. Yes.

16 Secondly, Mr. Chairman, on the accounting conventions,
17 item number 4 on that same page, I think that that needs a
18 little examination. I don't see why we don't go to a
19 quarterly system, and I would be interested at the proper time
20 to ask staff what is the matter with that, going to a
21 quarterly system instead of a half-year convention.

22 And finally, Mr. Chairman, on the next page, the
23 expensing for the small business, I have a lot of small
24 businesses in our state, and obviously they are rallying
25 around this provision; but where it came from, I don't know.

1 Previously there was indication of satisfaction with
2 the House measure, which costs \$1.3 billion; and suddenly up
3 pops this one that costs \$22.9 billion. I don't know where
4 that came from, and it indeed is a big-ticket item. I am not
5 sure of the philosophy behind it, when people seemed very
6 satisfied with the provision that was in the House bill.

7 Finally, Mr. Chairman, it seems to me that -- and I
8 will be repeating myself, possibly -- the whole purpose of
9 this measure is to get the rates down. And if we can get the
10 rates down, we are taking care of small business, we are
11 taking care of everybody as far as being more competitive in
12 the international market, and all those things.

13 So, the more we make this non-revenue-neutral, the less
14 chance we have of keeping the rates down, because the rates
15 are where we are going to look, finally, to increase it. And
16 that is why I raise these possibilities.

17 Just going back a minute to that indexing, in indexing
18 we take care of that to some degree by having capital gain
19 treatment of appreciation. And capital gain treatment is
20 less than ordinary income. And I presume one of the reasons
21 we have kept capital gain treatment is for appreciation, which
22 is attributable to some degree to inflation.

23 The Chairman. I have in order Senator Armstrong, then
24 Senator Long.

25 Senator Chafee makes a good point, because I know what

1 the tendency of the committee can be -- we will go along, and
2 we will make an amendment that will cost a billion here and
3 two billion there, and we go through all the Titles, and we
4 get down to the end and are \$50 billion short. Then we look
5 around and say, "Now, where are we going to get \$50 billion?"
6 We can go back to the House provisions on depreciation and
7 just absolutely devastate capital formation, and even that
8 won't pick up \$50 billion; we can raise the rates, which you
9 are opposed to and I am opposed to; we can look at the
10 deductions for excise taxes. But if we are going to come out
11 with a bill that, at worst, is revenue neutral -- we are not
12 coming out with one that is less than revenue neutral -- then,
13 as we go along, we have got to weigh what it is we want to
14 loosen or tighten. But if it is going to be loosen, loosen,
15 loosen, loosen, all the way, I can see disaster coming on the
16 last day.

17 Senator Armstrong?

18 Senator Armstrong. Mr. Chairman, as I understand it,
19 your proposal on real estate puts back into ordinary income
20 amounts that have been depreciated on the sale of that real
21 estate. I didn't hear any discussion about indexing the basis
22 in the computation of capital gain.

23 Now, something that Bill Bradley said makes me want to add
24 that as a line of inquiry and ask staff to do a little work on
25 it, because if our goal here is to permit people to recover

1 their cost before paying tax on the disposition of an asset
2 -- and it seems that is, arguably, our goal -- then, one way
3 to get there would be to go along with the idea of requiring
4 people to recapture depreciation but indexing the basis.

5 Now, I am not necessarily sure that I am for that, but
6 I would like to at least consider it. So, having mentioned
7 it, I guess we are going to come back, Lloyd, to this whole
8 general area. I would kind of like to put that on your list
9 of options.

10 Senator Bentsen. Bill, that is what I was talking to
11 Treasury about on their proposal.

12 Senator Armstrong. Oh, I missed the discussion.

13 Senator Bentsen. That's what they do. And I said that,
14 as the alternative, is what we ought to look at, so we are not
15 taxing some illusory profit.

16 Senator Armstrong. As usual you are a jump ahead of me,
17 and I thank you.

18 The Chairman. Senator Long?

19 Senator Armstrong. Will we have the numbers on that, or
20 do we have the numbers on that now, of what the effect would
21 be on revenues if we were to do that?

22 The Chairman. Was that the one proposal with \$300
23 million on over five years?

24 (Pause)

25 Senator Armstrong. Well, we don't need it at this point;

1 but whenever we come back to it, at least for consideration,
2 I would like to know what is the revenue effect if we take the
3 Chairman's proposal on recapture but permit real property
4 owners to index the basis before they begin to pay tax.

5 Mr. Brockway. The recapture provision raises \$300
6 million in the package that the Chairman has. That indexing,
7 the tentative reaction, and it is going to be very rough, is
8 that is going to be about \$500 million within the window if
9 you did that to real estate. But we would really like to look
10 at it again.

11 The Chairman. That \$500 million, Mr. Brockway, is
12 within the first five years, right?

13 Mr. Brockway. That is correct, Mr. Chairman. It is very
14 important to emphasize in all of this, particularly in real
15 estate but with indexing generally, that the revenue effect
16 in the out-years, in the future, is a substantial
17 consideration.

18 Senator Armstrong. Well, I don't want to ignore revenue
19 effect; but it does seem to me that we ought to, as we
20 consider all of these provisions, have some concern for the
21 underlying principles involved rather than just sorting out
22 who gets helped and who gets hurt.

23 One principle that we are on the verge, at least, of
24 losing sight of is this question of when should a taxpayer
25 have a liability? And I don't think anybody ought to pay

1 taxes until they have had a return of their capital in a
2 sale. So, at least with that as a benchmark, I would like to
3 look at that when we come back to this issue.

4 The Chairman. Senator Long?

5 Senator Long. Mr. Chairman, before we plan to dispose of
6 accelerated depreciation -- not necessarily today, but when-
7 ever you want to bring about a decision -- I would like for
8 us to focus on this matter of going from three years to five
9 years on the economic life of automobiles and light trucks
10 when used for commercial purposes.

11 Now, my understanding is that the economic life is
12 regarded as being somewhere in the two-to-four year category
13 for commercial purposes, and the only study of a longer life
14 would be an estimate of seven-to-nine years based on 85 per-
15 cent personal rather than commercial use. "Mileage is a
16 major determinant of the automobile and light truck
17 depreciation. Average commercial vehicles are driven 23,000
18 miles per year, which is twice the amount of mileage on a
19 personal vehicle, according to the Department of Transpor-
20 tation data."

21 My understanding is that this five-year classification
22 means that there is no acceleration at all, no acceleration
23 in the depreciation for automobiles or light trucks.

24 Before the ACRS, autos and light trucks could be
25 depreciated over 30 months, with a 200-percent declining

1 balance. Under ACRS, they receive three years accelerated
2 depreciation. Adopting a five-year life means that cars and
3 trucks will be less favorably treated than before the ACRS.

4 I would like to ask Treasury, how far back do we have
5 to go before we would find treatment for cars and light
6 trucks when used for commercial purposes less favorable than
7 this proposal before us now?

8 Mr. Mentz. I think, Senator, ADR came in in 1971; so,
9 I would assume it would be before that time.

10 Senator Long. So, we would have to go back prior to
11 1971 to find where we treated cars and light trucks less
12 favorably than what this proposal here would do?

13 Now, I am not wedded, necessarily, to what we have here
14 and what we have under the ACRS. But it does seem to me that
15 we ought to move toward at least a three-year straight line,
16 let us say, more favorable to the purchase for commercial
17 purposes than otherwise.

18 Now, I believe I have some understanding of the
19 difference between commercial use and personal use. Back in
20 the days when I was going to law school, and that type of
21 thing, and starting out practicing law, I drove my automobile
22 around 12,000 miles a year, which is around the average --
23 usually a little less than 12,000 miles a year.

24 When I started running for public office, I would drive
25 that automobile in one year more than I would in five or six

1 years going to college and practicing law just in my own
2 home town. There is a great deal of difference between what
3 a person drives in a car when he is out trying to make a
4 living, and how much you drive the car when you are driving
5 it for your personal use. And of course, we are not talking
6 about the personal use; we are talking about commercial use.
7 Some of this would be rental of automobiles that we are
8 talking about here.

9 When you rent an automobile -- I have been on both ends
10 of that -- when you rent the automobile, the fellow who rents
11 the automobile oftentimes is unfamiliar with it, and as far
12 as he is concerned if that thing holds out for three days
13 until he gets it back, well, that serves his purpose, and he
14 doesn't have to learn how to drive it the way it is supposed
15 to be driven or to take care of it, as long as that thing will
16 roll on in.

17 I one time made the mistake of getting involved in
18 renting used automobiles. Our way of doing that was,
19 sometimes if we would rent one of these wrecks, we'd say to
20 the fellow, "Now, what happens if this thing stops going?" He
21 would say, "Well, we will give you another one. There are a
22 lot of old broken-down automobiles out there, just take your
23 choice. And if the one you rent doesn't make it, we'll trade
24 you. Just take the luck of the draw."

25 But we are talking here about a law that encourages

1 people for commercial purposes to have new automobiles, or
2 safe and good equipment, and I would submit that if you were
3 using it the way people use commercial automobiles, that they
4 aren't likely to last that long.

5 Now, I would not insist that we change the matter with
6 regard to these diesel trucks. My impression about these
7 diesel engines is that those things will last for a long, long
8 time -- even though they do drive them 50-90,000 miles in a
9 year.

10 But for cars and light trucks, it would seem to me that,
11 if we do it this way, this will cut back on the purchase of
12 those automobiles.

13 The Chairman. What was the study, Mr. Jenner, we had
14 last July on the useful life on cars and trucks?

15 Mr. Jenner. Mr. Chairman, the Commerce Department
16 estimated that the useful life, the average useful life, for
17 both commercial and non-commercial cars was 11 years. They
18 said it was nine for commercial use.

19 Senator Long. Well, I have here seven to nine, but
20 that is based on 85 percent of the use being personal. Isn't
21 that right?

22 Mr. Jenner. No, sir, not in this study. It was nine
23 years.

24 Senator Long. Well, that is the study I am referring to.
25 What percent of that is personal, now?

1 Mr. Jenner. Oh, excuse me, sir. The average for both
2 commercial and personal was 11; the average for commercial
3 only was nine.

4 Senator Long. Well, those are not the figures I have.

5 Senator Boren. Mr. Chairman, what assumption did they
6 use? I share Senator Long's concern that we are making an
7 excessive change here as far as automobiles are concerned.
8 I can't imagine a nine-year life for commercial use of an
9 automobile. What assumption of mileage per year did they use?

10 Mr. Jenner. I don't have that figure offhand, Senator.

11 Senator Boren. I don't know who they surveyed, but it
12 would be strange to me that you could have a nine-year life.

13 I hope, Mr. Chairman, that we will examine that and see
14 what the number of miles per year were assumed. I agree
15 with Senator Long that I think the change that is projected
16 is --

17 Senator Long. Let me ask one question.

18 The Chairman. Secretary Darman has an answer, I believe.

19 No?

20 Senator Long. I just have one further question for
21 Mr. Jenner here. The figures I have here indicate that the
22 average commercial vehicle is driven 23,000 miles per year.
23 Is that what you have?

24 Mr. Jenner. I don't have the figures in front of me,
25 Senator.

1 Senator Long. Well, my estimate is what was given me,
2 supposedly Department of Transportation data. It says
3 23,000 miles per year, twice what the personal use would be.
4 And if that is seven years, then that means that that useful
5 life is 161,000 miles. Is that your estimate?

6 Mr. Jenner. That would be the multiplication, Senator.

7 Senator Long. Well, may I say that if you can make that
8 thing go 161,000 miles, bless you.

9 (Laughter)

10 Senator Long. I mean, I wouldn't want my wife out there
11 driving that automobile and risking her life at 161,000 miles.

12 Secretary Darman. Mr. Chairman, I was just going to
13 suggest that it would merit further work, though, to look at
14 the differences within this category, as Senator Long is
15 himself suggesting. In other words, leased cars have dif-
16 ferent expected lives than other cars and have little
17 difference than light trucks and tractors, and so on.

18 The reason I think it is worth looking at it more
19 carefully is that there is an awful lot of money involved.
20 And if you just took the whole category and moved it from
21 five years to three years, our rough estimate -- I don't know
22 what Joint Tax is, I think it is quite similar -- is that it
23 would be about \$9 billion lost.

24 That breaks out as follows: Leased cars alone would be
25 about \$2 billion. Other cars would be about \$3.8 billion. So

1 there is a total for cars of about \$5.8 billion.

2 Light trucks would be about \$2.2 billion, and tractors
3 would be about \$1.1 billion.

4 The Chairman. Going just from five to three?

5 Secretary Darman. Right.

6 So, without trying to judge where one ought to come out,
7 I mean simply to suggest that it is worth disaggregating this,
8 because there is so much money involved. It is in fact quite
9 a bit of difference in the expected lives.

10 Senator Long. Suppose we said that, instead of giving
11 three years with 150-percent declining balance, you just said
12 straight line for three years. Can you tell me how much
13 that would change the estimate?

14 Secretary Darman. I can't tell you right now, but we
15 could tell you fairly quickly.

16 Senator Long. I would like to know it, when you can
17 provide it.

18 Senator Symms. Mr. Chairman?

19 The Chairman. Yes?

20 Senator Symms. I just wanted to ask another question,
21 along with the direction of Senator Long's question. Let us
22 take other equipment that is rented. I have some of the
23 people in the rental business complaining they've got some of
24 their items put into a five-year category now, like clothing
25 for example. How did that ever happen?

1 Mr. Brockway. That is the way it is under present law
2 for rental clothing. Rental clothing right now does not have
3 an ADR class, and the way each year the present law works is,
4 anything that did not have an ADR class is put into the
5 five-year recovery class, which is where they are now. I
6 think the major change for rental clothing under this
7 proposal is that it would lose the investment credit, but it
8 would also gain indexing. But other than that, it would
9 maintain the same position as in present law.

10 The Chairman's proposal does not change present law
11 with respect to this.

12 Senator Armstrong. But I think that ought to be looked
13 at. I happen to agree with the thrust of Senator Long's
14 questions on automobiles, but there is other rental equipment.
15 People in the rental business are renting things that
16 obviously wear out before five years can expire, and they
17 get a huge account on their books of non-existent, already
18 salvaged equipment. It seems like this is a real unfair
19 burden to put on small business in the rental business, to
20 ask them to do that. And that is what is happening to some
21 of them right now. If this is going to be changed, is there
22 any way you can come up with an answer to solve that, so
23 there would be a more applicable current life on something?
24 Is there any way there can be any flexibility on that?

25 Mr. Brockway. Well, for formal clothing itself, formal

1 wear, the House, for example, I think has assigned that to a
2 three-year class. If you would do that on this proposal --
3 we have been requested -- that would be a number of
4 approximately \$100 million.

5 You can't do it for every category of asset, because
6 the general thrust of what both ACRS is and the Chairman's
7 proposal is is not to try to split up into that many
8 different categories in assigning things, but to try to stay
9 with some broad overall groups for simplicity's sake. But
10 that one item, as I say, is about \$100 million.

11 Senator Armstrong. Well, under the Chairman's proposal,
12 let's see. Where would light construction equipment that
13 some contractors rent be categorized?

14 Mr. Brockway. Probably in the five year. I would have
15 to point out what the ADR life is. But as long as that was
16 less than 16 years it would remain in the five-year category.

17 The Chairman. Could I ask you a quick question on
18 rental clothing? I have no idea whether the people involved
19 in this are big business or small business, but to the extent
20 they are small they could expense it under this proposal,
21 unless they were buying immense quantities of clothing.

22 Mr. Brockway. That is correct, up to \$50,000 worth a
23 year of expenses.

24 The Chairman. Senator Danforth?

25 Senator Danforth. Mr. Chairman, maybe this is a dumb

1 question, wading into something without having thought it
2 out, but on the depreciation of automobiles and light trucks,
3 isn't mileage a more accurate gauge in the useful life of a
4 vehicles than the years on it? Why wouldn't we determine the
5 depreciation of an automobile on the basis of mileage rather
6 than years? Or wouldn't that be appropriate?

7 Mr. Brockway. Well, you can use mileage if you take the
8 21 1/2 cents a mile, I think is what it is now. You can just
9 charge off the mileage on your car.

10 The difficulty with that, again, is a recordkeeping
11 complexity problem.

12 Senator Danforth. Why would it have to be complex,
13 though? Why not just say that the useful life of a car,
14 instead of being three years or five years is 70,000 miles
15 or 60,000 miles, or whatever? And if somebody drives
16 30,000 miles a year, he gets to depreciate half of it; if
17 he drives it 10 miles, he gets to depreciate a sixth of it.

18 Mr. Brockway. That would be a very precise way of
19 measuring your depreciation, and you can in fact elect a
20 general notion such as units of production, where you look at
21 how much you actually use the asset. The difficulty is that
22 you would then have to keep records for how many miles you
23 use on every car. And obviously, last year you went through
24 a somewhat unpleasant experience with trying to make sure you
25 knew exactly how many miles the autos were used.

1 Senator Danforth. But that is not a matter of driving
2 around with a clipboard by your side as the case was last
3 year, when you had to determine how much was used for business
4 and pleasure. What I am saying is, if you assume something is
5 a business vehicle, why not just say that the car is going to
6 go 60,000 miles, or 70, or whatever the appropriate use is,
7 and as fast as you get there you would depreciate it?

8 Mr. Brockway. You could do that, Senator. But the
9 difficulty is really just a trade-off between the simplicity
10 of not even having to worry about how many miles, checking the
11 odometer on each auto that the company had and the mileage
12 used during the year, and attending to all of that, rather
13 than -- that is what would be required.

14 Senator Danforth. But what is so complex about that,
15 though? That takes five seconds.

16 Mr. Brockway. Well, it is simply more to do that for
17 every car than a system as under present law or under the
18 Chairman's proposal, or any of the other proposals under
19 consideration, where the accountants just take the cars that
20 you had acquired and multiply it by, for example, 25 percent
21 in the first year as in present law, 38 in the second year,
22 37 in the third year. It is solely a bookkeeping entry. You
23 have to know how many cars you bought and the cost of them;
24 but you don't need to go into checking the actual mileage used
25 during the year.

1 Senator Danforth. It doesn't seem to me to be
2 complicated. I mean, maybe it is. Maybe it is just a
3 foolish idea and nobody would support it. But it seems to
4 me it would be just as simple to keep track of mileage at the
5 beginning and end of the year as on the date on which you
6 bought it.

7 Mr. Brockway. It's simply another step in accounting
8 that the business would go into. So, saying, as a rough
9 justice, assuming all the cars are used on some sort of
10 average and a write-off. Surely you could do it. Clearly,
11 present law is less precise, but I think it is easier for
12 the businesses generally to use it that way.

13 The Chairman. Senator Bentsen?

14 Senator Bentsen. Mr. Chairman, I think Secretary Darman
15 has made a good point about breaking down the categories in
16 looking at this. But I think the problem you run into is not
17 particularly the number of years or the amount of mileage, but
18 how it is used.

19 I don't even keep a personal car back in Texas, because
20 when I go back to Texas and fly back there, it is just to
21 change planes to go someplace else in Texas. And when I get
22 there I have a rental car. So, I am tending to be something
23 of an expert on rental cars. And what I ask for is the one
24 with the very lowest of mileage. I don't care what it is; just
25 give me the lowest mileage. Because, unfortunately,

1 Americans trash rental cars. They just trash them.

2 (Laughter)

3 Senator Bentsen. I saw one fellow take a car and go
4 quail shooting, and then clean his quail in the car.

5 (Laughter)

6 Senator Bentsen. I said, "What in the world are you
7 doing?" He said, "It's a rent car."

8 (Laughter)

9 The Chairman. Well, I think we can work out a two-year
10 life on that, the quail cars.

11 (Laughter)

12 Senator Bentsen. And what you are looking at, I think,
13 is not the \$50,000 exemption with small businesses where most
14 of this is going; I think you are talking about some very
15 big companies. I think you are talking about Hertz and Avis
16 and National, and whatever the rest of them are. And I think
17 the end result is, if we keep it at five years, I am going to
18 be driving some awfully old rental cars.

19 (Laughter)

20 Senator Bentsen. And I think that is what you have to
21 consider in the process.

22 The Chairman. Further comments on anything in this
23 section?

24 Senator Baucus. Mr. Chairman?

25 The Chairman. Senator Baucus?

1 Senator Baucus. Mr. Chairman, I was out for a few
2 minutes, and I think when I was out you and the Joint Tax
3 Committee discussed ways to get data that we could tend to
4 agree on with respect to the cost of capital and capital
5 cost-recovery.

6 What I am really getting at is, I think that all of us
7 here do not want to do anything that is going to increase the
8 cost of capital. We don't want to do that. And I think your
9 bill does not, but it may marginally. Other Senators think
10 that it does, having their own set of data.

11 I am wondering, is there some way the Joint Tax
12 Committee or the Treasury, and/or both, with the various
13 asset categories, could try to work up some data that we
14 can tend to agree on, so that we are talking about apples and
15 apples, and not apples and oranges?

16 The Chairman. There is, but here is what you are up
17 against.

18 Senator Baucus. I say this, Mr. Chairman, because it is
19 a critical point. In fact, it is one of the key turning
20 points of this whole bill, is the degree to which it does or
21 does not increase the cost of capital. So, the more we can
22 tend to agree and operate, as best we can, on the same data,
23 then we can more intelligently make that decision.

24 The Chairman. Well, let me see if I can again phrase it
25 right. The study that Mr. Brockway referred to was really a

1 study of all of the bills in total. Is that right?

2 Mr. Brockway. The total bill. That's correct.

3 The Chairman. The total bill. So, you have the
4 President's bill, you have the House bill, you have my
5 proposal, current law. Of those four, the President's,
6 overall, if you meant cost of all capital, was better. If I
7 cite the study right. Mine was second-best; the House bill
8 was worst.

9 Now, that is a generic conclusion, however.

10 Mr. Brockway. That's right.

11 The Chairman. And if you say, "Well, but how does it do
12 for machines or real estate?" -- real estate doesn't do as
13 well under my bill as it does under the current law. Nor
14 does it do as well under the President's bill or under the
15 House bill as it does under current law. So, if you are in
16 the real estate business, you say, "These are all terrible,
17 because it is increasing our cost of capital."

18 As to machines themselves, it becomes a tougher hole,
19 because you are limiting the investment tax credit. So,
20 clearly, all by itself, when you eliminate the investment tax
21 credit, does that increase or decrease the cost of machines?
22 All by itself, it increases it.

23 What happens if you drop the corporate rate to 35 percent
24 and the individual rate to 35 percent? Then you start to
25 fracture the businesses. For those businesses that do not

1 have heavy investment tax credits, they say, "Boy, our cost
2 of capital is now less." And for those who are heavy
3 capital-intensive industries, they are inclined to say, "Oh,
4 well, our cost of capital is more."

5 And if we are going to go through this bill and say,
6 industry by industry, and segment by segment within industry,
7 "We are not going to adversely affect anybody, so that
8 anybody's cost of capital is any less than it is now," then
9 you are going to have a bill that is an immense revenue
10 loser.

11 Senator Baucus. Mr. Chairman, I understand that. I
12 understand all of that, and I think there is no one who
13 disagrees with that. But I still think we need to draw the
14 line somewhere between aggregates only on the one hand, and
15 just minute, specific individual firm data on the other hand.
16 It seems to me there is some mid-range or there is some place
17 we can draw the line so that we get a little more informa-
18 tion, as best we can get it, and then make an intelligent
19 decision as to which categories we want to increase or
20 decrease, and to what degree, compared to some others.

21 I just think we need a little bit more data here. Some-
22 one once said, "Abstraction is cruelty," you know, and
23 aggregates tend to be cruel because they deal with averages,
24 and averages obscure.

25 So, it seems to me that we have to, to some degree, do

1 the best we can, and with some reasonable number of categories
2 try to determine are we increasing this categories's cost of
3 capital or are we not, and to what degree? I just think it
4 is critical that we do that; otherwise, we are just shooting
5 in the dark around here, because aggregates don't help very
6 much here. They really don't help very much, particularly,
7 if I might add, Mr. Chairman, if we are trying to increase
8 our international competitive position. We have to be a
9 little bit targeted here, a little bit selective here. We
10 have to make some choices, some judgments. The economic pie
11 is only so large, and we have to slice it in some way.

12 The Chairman. And that is one of the reasons that the
13 committee members over and over, when I met with them, said
14 they didn't mind substantially increasing the cost of capital
15 to real estate. The Japanese have not yet figured out a way
16 to move the buildings here, altogether, and tow them across
17 and set them up.

18 Senator Baucus. They will. They are coming.

19 The Chairman. And well they may. They may. And when
20 we get to that place, we will have to consider that. I
21 suppose you could put a forty-story building on a barge and
22 bring it across the ocean.

23 Senator Baucus. They are, in fact, doing it. They are
24 building buildings here that they have shipped over.

25 The Chairman. Oh, not 40-story skyscrapers.

1 Senator Baucus. Not that high. The Japanese are
2 smaller.

3 (Laughter)

4 The Chairman. So, the committee said, by and large,
5 assuming we have to trade off segments, "Let's make real
6 estate a bit more expensive and machines a bit cheaper." I
7 mean, that was an aggregate balance. But even within
8 machines, you have differences.

9 Senator Baucus. That is what I am trying to get at.
10 Even within machines, isn't there some way that the
11 committee can work up some data to give us a little better
12 idea?

13 And the second point I might raise, too, is on revenue.
14 If we can get revenue estimates for these various divisions
15 in the book, as we did yesterday, and get that data in
16 advance, it would make a big difference, I know.

17 The Chairman. Well, let me ask, because I thought we
18 were going to have the data in advance.

19 Mr. Brockway, what is the status now on the issues in
20 the order in which we will take them up as to how soon you
21 can have revenues, where the members can simply write into
22 their books, "Plus-three, minus-two, zero," and what not?

23 Mr. Brockway. Well, last night we distributed to the
24 members -- as Mr. Heinz pointed out, later than 6:00; about
25 9:00 -- the numbers on ACRS and on accounting. And hopefully

1 later today we will go back and do natural resources, that
2 you covered earlier, to get those down precisely. I think
3 your schedule so far for the remainder of the week -- they
4 sent to you. Other areas that we may move to, we will do
5 those as well.

6 The Chairman. I was doubtful if we would get past
7 depreciation, ACRS and accounting today. I will announce at
8 the end of the day the order of the next five or six. And
9 my hope is that, especially while we are gone during the
10 recess, you can cost not only those five or six but have the
11 rest of it costed out, so that the members can at least know
12 item-by-item where they are.

13 Mr. Brockway. The intention, Mr. Chairman, is, when
14 they come back from recess, to have the entire packages done.

15 The Chairman. Good.

16 Senator Long, then Senator Boren.

17 Senator Long. I would like just one short answer from
18 Treasury.

19 Do you have studies on the useful life of automobiles
20 and light trucks? And if so, what does your study say?

21 Mr. Darman. Senator Long, we don't have a study
22 that Treasury itself has done; we have used only the
23 available outside studies.

24 Senator Long. You have no estimate on the useful life
25 of automobiles?

1 Mr. Darman. We do, but you asked do we, Treasury, have
2 a study of our own, or that is what I understood you to ask.

3 Senator Long. Well, what is your estimate, then?

4 Mr. Darman. It is not a study of our own; it is an
5 outside study.

6 Senator Long. You have an estimate based on outside
7 information. What is the estimate?

8 Mr. Darman. When we put together Treasury-II, we used
9 something that comes very close to three years.

10 Senator Long. That was your estimate, then?

11 Mr. Darman. That is the one we used. It is an outside
12 estimate. That is the one we used.

13 Senator Long. Well, let me ask you now, did you use
14 that because you thought it was realistic?

15 Mr. Darman. Yes.

16 Senator Long. Thank you.

17 The Chairman. Senator Boren?

18 Senator Boren. Mr. Chairman, I apologize if this
19 question has been asked. I was curious about the cost
20 recovery class for refineries. Am I correct in reading the
21 staff draft that it would change? That refineries are
22 presently in a five-year class, and if we changed the mid-
23 point lives, the 16 years, does that then drop them into the
24 10-year class instead of the present five years? Is that
25 correct?

1 Mr. Brockway. That is correct.

2 Senator Boren. I am concerned about that. When we look
3 at what has happened to the domestic refining industry, we
4 have dropped from 315 operating refineries four years ago
5 down to 199. We have lost about four million barrels a day
6 of capacity, and it is a trend that is going to have to be
7 reversed one of these days if we are going to have the
8 sufficient ability in a national emergency to refine our
9 everyday needs plus even some out of the strategic petroleum
10 reserve.

11 What is the revenue involved? That is something I hope
12 we would think about before we make a final decision on it.
13 What is the revenue involved for just changing refineries, not
14 the other elements of that?

15 Mr. Brockway. We will have to look at that, Senator
16 Boren.

17 Senator Boren. All right.

18 Mr. Chairman, I just raise the question; I would like to
19 look at what the revenue is just for that particular area
20 before we make a final decision about what should be done on
21 where we would place refineries.

22 The Chairman. Senator Heinz and then Senator Bradley.

23 Senator Heinz. Mr. Chairman, thank you.

24 I would like to get some information from Mr. Brockway
25 and the Treasury Department on some of the revenue estimates

1 in our handout. One of them that I am not quite sure I
2 understand is why there is such a large difference under the
3 Chairman's proposal in terms of the effective date regarding
4 the ITC. It is a \$28.6 billion revenue loss.

5 Mr. Brockway. I think, largely, that is explained by
6 the fact that the House bill has a five-year spread of the
7 investment credit. So, instead of allowing the investment
8 credit in the year that you claim it under the House bill, and
9 as under present law, you only get two percent a year. And so
10 a substantial part of that revenue loss is outside the window
11 in the House bill.

12 You also have differences due to the fact that you have
13 a different revenue-estimating window we are looking at here,
14 because we had to do the House bill and the President's
15 proposal very roughly to come up with these numbers. They
16 are not estimated on the same basis as the Chairman's
17 proposal. These are basically taken from the estimates that
18 were done on the House side. Since then, there have been
19 updated economic assumptions. And also, you are looking at
20 1991 as well in measuring the Chairman's proposal.

21 But my suspicion, without knowing right now, is that the
22 largest reason is that five-year spread in the investment
23 credit in the House bill, that had the House bill allowed the
24 investment credit in full as in the present law, in the year
25 the property is placed in service, that transitional loss in

1 the five-year window would have been a larger number.

2 Senator Heinz. Now, as one compares the Chairman's
3 proposal to the President's proposal, it is about, oh, one-
4 third to a quarter less generous on depreciation; it is
5 slightly less generous on indexing but more generous on
6 indexing than in the House; it provides for a considerable
7 amount of expensing, which is largely targeted at relatively
8 small companies -- take the current \$5000 or \$10,000 expensing
9 provision, raises it to \$50,000, and for the phase cut-off at
10 \$200,000. And all proposals repeal the ITC. I will skip
11 over the effective-date issues. And there are other
12 relatively less-significant changes.

13 Now, let me ask at this point the Treasury Department
14 this: If you disregard -- and maybe we shouldn't -- if you
15 disregard the Treasury Department's windfall recapture of
16 access accelerated depreciation, which phases out over a
17 period of time, at a certain point you no longer capture that
18 depreciation, and you disregard -- again, maybe we shouldn't
19 -- the Chairman's proposal to increase expensing to \$50,000,
20 how would you compare the changes in the cost of capital
21 among both proposals? Would the President's proposal
22 increase the cost of capital more than the Chairman's
23 proposal, or vice versa? And if so, by what kind of margin?
24 And I am trying to look five or six or seven or eight years
25 out.

1 The reason I do this, by the way, is that I am concerned
2 that in the short run we can fudge numbers and make things
3 balance out and deceive ourselves; but we should be writing
4 a tax bill that is going to last more than another two years.
5 If history bears us out, it won't, and probably for good
6 reasons.

7 Mr. Darman. Senator Heinz, let me give you our
8 calculations on that. Roughly, the conclusion would be that
9 the Senate Finance would be better than the House bill,
10 substantially better than the House bill. It would be
11 marginally better than current law for the overall corporate
12 cost of capital.

13 If you took the total cost of capital, Senate Finance
14 would be better -- it is the same pattern -- substantially
15 better than the House bill and marginally better than current
16 law. However, the President's proposal would be better than
17 all of the above -- marginally better than all of the above.

18 Senator Heinz. Is that true if you disregard the
19 expensing provision?

20 Mr. Brockway. Basically, we are giving you virtually the
21 same set of numbers on the cost of capital. These numbers
22 are constructed without taking into account the expensing, and
23 they are constructed without taking into account the windfall
24 recapture item. It is solely looking for new investments,
25 hypothetical new investment, and the long-run effect of that

1 investment.

2 Senator Heinz. Is that analysis available?

3 Mr. Darman. We can make it available.

4 Senator Heinz. It would be very helpful.

5 The Chairman. Further discussion?

6 Senator Bradley. Mr. Chairman?

7 The Chairman. Senator Bradley, and then Senator Baucus.

8 Senator Bradley. Mr. Chairman, I wanted to not comment
9 specifically on depreciation but in terms of asking the staff
10 to develop something. Would this be the appropriate time to
11 do it?

12 The Chairman. Yes.

13 Senator Bradley. Mr. Chairman, I think that all of us
14 have constituents who ask us, "Why are our tax rates so high?"
15 And one of the answers as to why they are so high is because
16 we choose to spend on national defense and education and
17 environmental programs. And we look at those direct spending
18 programs, and we know who benefits, how many people benefit,
19 and we try to assess whether it is achieving its purpose.

20 Another reason tax rates are so high is because we have
21 accepted \$400 billion in tax expenditures.

22 Now, in doing tax reform, we are saying that we are
23 going to cut tax rates, and a part of that deal is to
24 eliminate tax expenditures. It seems to me there are a couple
25 of questions that are important for us to do that in a kind of

1 systematic way: One is to know how much they cost. And I
2 appreciate the Chairman and the committee making their best
3 efforts now to get us those revenue numbers in advance.

4 It seems to me the question is also who benefits, how
5 many taxpayers benefit, and what their income levels are.
6 And then, finally, whether the tax expenditure is achieving
7 its purpose or not.

8 And I think the question of who benefits is a very
9 important and relevant question; it matters. And it matters
10 in terms of numbers and in terms of income class.

11 For example, just take the capital gains on timber.
12 Now, I think it would make a difference to the committee if it
13 was going to benefit just a couple of companies versus
14 thousands of individual timber growers. And I think that
15 that is a fact that we ought to have. I mean, I can't
16 imagine the Secretary of Agriculture, for example, spending
17 \$4 billion on some timber program, and then having the
18 Inspector General do a report and say, "But we can't tell you
19 who receives this, or how many people receive it."

20 You know, I picked timber almost intentionally, because
21 I know that is really not going to be one that we are going
22 to touch. But I think it is important that we know how many
23 taxpayers benefit from a particular expenditure, and what
24 their income level is. Because, basically, we are making our
25 best efforts here to get the tax rates down on middle income

1 people, and we need the most information that we can get to
2 do that.

3 So, I would hope that we could also generate not just
4 the revenue but who benefits from and how many taxpayers
5 benefit from the individual provisions.

6 The Chairman. Well, Bill, I cannot accede to the request
7 for everything you want. You want two companies that benefit,
8 and they each have 30,000 employees; does that count more
9 than 10,000 companies with two employees apiece? There is a
10 limit to how much the Joint Committee can do. There is a
11 limit as to how much computer time they have access to and
12 money. They cannot give you everything you want, and if you
13 want to keep asking for all and all and all of these
14 statistics, we might as well shut up shop, because they won't
15 get these statistics done by the end of the year. And then,
16 they will be relevant only until we change one or two factors
17 in the bill, and then they will all have to be recomputed
18 again, unless I am wrong.

19 Mr. Brockway. Certainly, as you change the bill, the
20 numbers have to be ultimately updated to reflect the entire
21 package. But it is very true that the more information we
22 have to do, there are certain limits on what information we can
23 come up with. Some items we have the distribution on, and
24 we can provide that, typically, in the individual sectors;
25 a lot of the items you are discussing now we simply don't have

1 a breakdown for. We would know the number of firms, perhaps,
2 but I am not sure what that tells you.

3 The Chairman. Here would be a good example: Three years
4 versus five years on cars. You can say, "All right, how many
5 companies are affected if we have three years on cars but
6 you have 50,000 expensing?" Well, that might be one thing.
7 What happens if you go to \$25,000 in expensing and five years
8 on cars? All of your other statistics are out the window.

9 Senator Bradley. Mr. Chairman, if I could, let me just
10 say that I fully accept and know that you can't get this data
11 on every provision of the bill, and I understand that. And
12 I also think that it is not as relevant on the corporate as
13 it is on the individual side. And I don't want to run the
14 Joint Tax Committee through loops and have them try to
15 develop things they don't have.

16 But the fact of the matter is, some of the material is
17 available, in, for example, the document on Treasury I that
18 the Administration did. They came up with certain things
19 that I think are relevant to this question. They came up,
20 for example, just on one issue, the intangible drilling cost,
21 that 50 percent of the benefit goes to 31,000 taxpayers, and
22 the average subsidy is about \$28,000.

23 Now, you know, that is a fact that is available, is in
24 the literature, and I think it would help us as we go through
25 this, making choices about which expenditures we eliminate in

1 order to get rates down.

2 I don't want to complicate matters; I don't want to run
3 the Joint Tax Committee through a hoop. But it is available
4 anyway. The question is, do we have to use our own resources
5 and pull it together, or can the Joint Tax Committee do it?

6 The Chairman. The Joint Tax Committee can do as much as
7 it can do. It does not have the time to do everything you
8 want it to do.

9 Senator Baucus. Mr. Chairman?

10 The Chairman. Senator Baucus?

11 Senator Baucus. Mr. Chairman, I appreciate the part in
12 your package which transfers computers from five years to
13 three years. So, at the appropriate time I am going to offer
14 an amendment which would also transfer the semi-conductor
15 processing equipment to the three-year category. The data I
16 have indicates that the actual useful life of semi-conductor
17 processing equipment is much closer to the three-year rather
18 than the five-year period. I want to put you on notice.

19 Second, Mr. Chairman, I wonder if I could ask a house-
20 keeping, administrative question here? Yesterday there were
21 no amendments offered on the agriculture and natural resource
22 provisions. It is my understanding that at some future date
23 amendments will be in order to that section. I don't expect
24 to see any amendments today, either, on the accelerated cost
25 recovery and depreciation provisions of this bill. I expect

1 that at some future date they will be in order.

2 My question really is, based upon that action, is it
3 your choice that we have already approved the agriculture and
4 natural resource provisions that we discussed yesterday,
5 pending some Senators' action at a later date to offer an
6 amendment to go back and reopen that? Or have we just
7 discussed that area and not approved that area as a committee
8 action? I am just curious. And the same question would apply
9 to the depreciation provisions today.

10 The Chairman. What I am trying to do as a rule of
11 thumb, as we go through these, I have asked the Senators
12 ahead of time, where they have amendments, to have them
13 prepared. I don't mean prepared technically, because we are
14 going through this from a standpoint of concepts, and we will
15 get it drafted afterwards if the concept is drafted. But if
16 we go through the sections, and as the Senators have five-
17 six-seven-eight-nine days notice, I would hope that whatever
18 issues they want to raise, they raise, and we have a chance
19 then to look at the amendments -- many of which can be
20 harmonized, many of which can be adopted or at least
21 compromised, and we can get down to the half a dozen that are
22 very controversial and that we will have to vote on one way
23 or the other.

24 What I don't want to do is go back to the agriculture
25 or natural resources section and now have Senators say, "Well,

1 now, I have 15 new amendments I have just thought up; didn't
2 bother to bring them to your attention then or now," because
3 on that process we can go on ad infinitum.

4 Senator Heinz. But, Mr. Chairman, on that point --

5 The Chairman. Let Senator Baucus finish.

6 Senator Baucus. Well, as I understand you, then, as far
7 as you are concerned, we have already concluded that portion
8 of the package.

9 The Chairman. Any number of Senators mentioned
10 amendments yesterday, and I think they are getting them ready
11 now, and I have asked them to get them to me. And we will go
12 back and consider them.

13 Because yesterday was the first day on the first section,
14 if you have a special amendment you want to bring up, just get
15 it to us. But as we go through these other sections, we just
16 can't go through talking through 18 or 20 sections for 30 or
17 40 days, then go back and see, now, what amendments we have,
18 and then start back again on which amendments we are going to
19 consider. At some stage we are going to have to have them as
20 we are getting to the sections.

21 Senator Baucus. May I ask what your disposition will be
22 with respect to this depreciation and accelerated cost
23 recovery package of the bill?

24 The Chairman. The disposition will be the same as
25 yesterday: I am asking the Senators to have their amendments

1 ready. Yesterday and today you had two days notice.

2 Senator Baucus. So, when do you expect to have amend-
3 ments brought up on this section of the bill?

4 The Chairman. I would hope that after we have gone
5 through three or four or five sections, and it is clear we can
6 compromise 30 amendments, and we have 10 left to vote on in
7 these sections, we would go back and say, "All right, here
8 are the three amendments outstanding." But at that stage I
9 would be very reluctant to be considering new amendments that
10 have never come up to those sections.

11 Senator Baucus. Do you expect amendments before or after
12 this coming recess?

13 The Chairman. Oh, I was hoping we would simply get
14 through accounting, depreciation, and natural resources, in
15 terms of our discussion, Monday, Tuesday and Wednesday. I
16 said whether we meet Thursday or not depends on what we are
17 going to do on the floor.

18 Senator Baucus. So, if there are amendments, they would
19 be on Thursday?

20 The Chairman. Yes. Well, we may or may not meet on
21 Thursday; it depends. My hunch is if we vote today or
22 tomorrow on Contra aid and there are no votes on Thursday,
23 that I might have trouble getting a fair number of people
24 around here.

25 Senator Baucus. I cannot give my endorsement to this

1 section at this time.

2 The Chairman. I am not asking that, if you don't say
3 anything now, you are foreclosed from raising an amendment,
4 Max. What I will object to is when we come back to it, and
5 you haven't had an amendment then, and I say, "All right,
6 that closes the section," and then three or four days later
7 when we are on capital gains you want to come back with
8 another amendment on natural resources or some other section
9 we have finished.

10 Senator Baucus. Even at the very end of the process?

11 The Chairman. Even at the very end of the process I am
12 going to try to be as even-handed as I can. Because I think
13 what is going to happen at the end of the process is that
14 we are going to have to make some adjustments all the way
15 along. That is just my intuitive hunch, because we are going
16 to have to go back and say, "All right, we were higher than
17 the House here, lower than the President there; we are short
18 of revenue on this issue, and we are \$20-30 billion short
19 altogether," if that is what we are up against, "Where do you
20 want to make the adjustments?" At that stage, if I say, "Well,
21 the only place you can make the adjustment is in the last
22 section which we haven't closed, which happens to be
23 "Miscellaneous," or something like that, we are not going to
24 succeed at it.

25 Senator Heinz. Mr. Chairman, on that point, if I may:

1 If you are saying that the committee is going to go along and
2 make decisions, and that the decisions we make subsequently
3 either to the present section we are on in the bill or other
4 sections, that those decisions must be made independently of
5 any portion of the bill that the committee has gone over,
6 that is a proposition, if that is what you were saying, that
7 I can't accept.

8 The reason I can't accept it is, I can very easily
9 imagine a situation where we are going through this legis-
10 lation -- the day after tomorrow, or two weeks from now --
11 and someone adopts an amendment. Maybe it costs \$20 billion,
12 maybe it loses \$20 billion. Let us assume it loses
13 \$20 billion. I don't want to be foreclosed, if I think it is
14 a meritorious amendment and I have supported it, from going
15 back and getting the necessary revenue that is needed from
16 any other portion of the bill.

17 Equally, if we should actually surprise people -- and I
18 admit this is a long shot -- and actually find some additional
19 revenue, if I want to go back to accelerated depreciation and
20 put it into that, I don't want to be precluded from doing
21 that.

22 It seems to me that to go through the bill and consider
23 each portion of it as we have discussed it closed, if that
24 is what you are saying, really locks up portions of the bill
25 that shouldn't be locked up, and that the decision in which

1 order one wants to do that therefore becomes very critical.
2 You have the right to choose the order in which we go through
3 the bill, but I don't know that it makes good policy in
4 choosing the order to have the order determine the extent to
5 which choices can or can't be made as we look at the bill in
6 its totality.

7 My only other comment is that we all want to write a
8 balanced bill. You want to, you tried very hard to. And at
9 the end, we all know we are going to make a lot of decisions
10 between now and the conclusion. We are going to have to do
11 some balancing and weighing of many portions of this bill. We
12 can't just make decisions on the last two or three sections of
13 the bill and say the other 20 are off limits. That doesn't
14 make any sense to me.

15 Now, I don't know if that is what you were saying; I hope
16 it is not. Because if it is what you were saying, I think it
17 is an impossible way to proceed.

18 The Chairman. John, I didn't mean to mislead you. It
19 is not what I am saying. As we work through this bill there
20 are going to be sections which are going to be, for all
21 practical purposes, somewhat non-controversial, and I think
22 by and large de jury closed. Can they be reopened? Sure.
23 Are members going to come back at the end of this with
24 hundreds of amendments? I doubt it.

25 You and I have worked through this before -- I have gone

1 through the Commerce Committee as the Chairman for four
2 years -- and somehow we have gotten from A to Z in complicated
3 bills and finished it, and the members got to bring up what
4 they wanted. But at some stage we have to finish -- except
5 for those who do not want to finish. And I understand that.
6 There are some that are perfectly happy to have no bill. And
7 to that extent, the Senate lends itself, both in committee and
8 on the floor, to legitimate procedural delays for those who
9 don't want to move things.

10 I hope to get a bill out of this committee, and at some
11 stage -- I will try not to be abrupt, but I may be a little
12 forceful in saying, "We are going to go ahead. You've got
13 your amendment? Bring it up. We'll vote on it."

14 Steve?

15 Senator Symms. Well, Mr. Chairman, this has been a
16 very interesting discussion all morning, and I guess I am now
17 coming back to where we started when Senator Bentsen started
18 his first line of questions to some of the people at the head
19 table down here about the cost of these different proposals.

20 But the thought occurs to me, after hearing all of this
21 discussion this morning, that one thing this committee should
22 strive to do is, whatever we do in terms of a bill, make it
23 as simple as possible in terms of how it treats different
24 groups of taxpayers. I mean, if there has to be some
25 adjustments made, so be it; but, the closer we can stay to

1 current law for interpretation, that would probably be the
2 simplest thing, because the whole idea of simplification has
3 been given up in this process months and months ago.

4 I would like to know how much it would cost, or actually
5 in this case it would be a savings to the Treasury, to treat
6 all of this section as current law except for real estate
7 and move it to 25 years instead of clear to the complete 30.
8 What would the cost be? You had some of those numbers
9 earlier when you were answering Senator Bentsen, John.

10 Mr. Colvin. Do you mean present law compared to the
11 Chairman's proposal?

12 Senator Symms. If you use present law instead of the
13 Chairman's proposal, except for one item in the current law,
14 and that is where real estate property is now -- what? -- at
15 18 years? Move it to 25. How much money would that be, and
16 how much, then, could you save?

17 Mr. Colvin. The Chairman's proposal in the
18 depreciation area loses \$4.3 billion compared to present law.
19 And so, if you started with present law, that would
20 immediately pick up \$4.3 billion over the Chairman's proposal.
21 The adjustment for real estate would cost some fraction of the
22 \$2-3 billion that was referred to earlier.

23 Senator Symms. So if you just raised real estate to 25
24 years and left everything as it is -- now, then, we will have
25 a few amendments that have been mentioned here this morning on

1 some equipment that probably obviously, out of fairness,
2 should be reduced in time. And the reason for the Chairman's
3 cost is the \$50,000 for expensing?

4 Mr. Colvin. That is correct. And the reason that that
5 figure is so large is that that benefits approximately 85 to
6 90 percent -- that is a preliminary estimate -- of businesses.
7 That is about the percentage of businesses that have
8 investment up to \$200,000 a year, and so it benefits all
9 businesses except the largest 10 or 15 percent. That is why
10 you get that large figure on expensing.

11 But if you combine all the depreciation provisions in the
12 package, it loses \$4.3 billion relative to present law.

13 Senator Symms. If you include the expensing part of it?

14 Mr. Colvin. Yes, sir.

15 Senator Symms. All right.

16 So, then, I guess the question I am basically asking is
17 the difference between a 30-year schedule on real estate and
18 25 years. How much difference would that make?

19 Mr. Colvin. That would have to be several hundred
20 million; I would imagine less than a billion. But that is
21 just a top-of-the-head figure.

22 Senator Symms. Per year?

23 Mr. Colvin. Over the period.

24 Mr. Brockway. Let us get back to you, Senator Symms.

25 If we are correct that it is \$2-3 billion for going to 30

1 years from present 19 going to 25, it would have to be
2 roughly half of that. But it was really just an off-the-
3 cuff remark that we thought it was about \$2-3 billion of
4 real estate, of going to the full 30 years. We will be able
5 to get you a more precise answer.

6 Senator Symms. Thank you.

7 The Chairman. Senator Durenberger?

8 Senator Durenberger. Thank you, Mr. Chairman.

9 Keeping track of people's special interests, you might
10 note my interest in Senator Long's issue, the automobiles and
11 light trucks.

12 I would add to the discussion we heard here this morning
13 on how to differentiate the argument that, particularly on
14 short-term leases as opposed to the fleet leases, there is
15 another factor involved, and that is the competitive pressures
16 that aren't necessarily mileage-related or year-related,
17 because they may fluctuate from time to time; but largely it
18 is reflected by Senator Bentsen's comment that "I want the
19 car with the lowest mileage." There is always going to be
20 somebody who provides me a good deal on a low-mileage car.
21 And I think that is another element.

22 The other issue, on which I will have an amendment to
23 your proposal, deals with accounting conventions, the issue
24 of the half-year or mid-month conventions, number 4 on page
25 19 in our book. I think I am going to recommend we consider

1 a mid-quarter convention. I suspect I will be able to
2 demonstrate to you that it is not only fairer but more
3 realistic than both current law and your 40-percent proposal,
4 both of which seem to be somewhat biased in favor of getting
5 in in the last quarter and sort of neglecting what happened
6 in the first quarter. So, if you are open to that suggestion,
7 I will have a specific amendment.

8 The Chairman. Well, you know the problem. And let me
9 thank you, because your staff advised us of your interest in
10 both that, on the rental cars and on the quarter versus the
11 mid-point. The problem, of course, that we are trying to get
12 away from on the mid-point is somebody buying in December
13 and taking, in essence, a five-month correction when they
14 bought in December.

15 The problem with going to a quarterly is, it makes it a
16 bit more complicated for businesses; they have more possible
17 report periods now. And again, it is that attempting to
18 balance all the time the relative simplicity on the one
19 hand -- relative; anybody who says anything other than
20 "relative" is fooling themselves. If we want to go to ultimate
21 simplicity we would say, "All right, all machines can be
22 depreciated over five years; it doesn't matter if it is a
23 battleship or a tuxedo, it is going to be five years." And
24 that is very simple, just straight-line them over five years.
25 But, clearly, we are not going to do that.

1 Senator Pryor. Mr. Chairman, I think these meetings
2 like we have had the last couple of days are very helpful;
3 to a degree, they are kind of like an all-day dinner on the
4 ground, where we just sort of talk and hear our various
5 concerns.

6 I am very concerned that if we have any votes before
7 Easter in this committee, that we are going to be sorry. I
8 think we will add to the confusion, and I also feel we ought
9 to give ourselves the opportunity, after we talk about these
10 issues some here in Washington, to go back home for that week
11 or 10 days and listen to our own people talk about their own
12 situations.

13 I am just very hopeful. I am not going to make this in
14 the form of a motion, but I am very hopeful that we will not.
15 And even though you might state that we might not have any
16 votes on these issues before we return from Easter, I think it
17 would be wise, and I think we would be glad in the long run if
18 we did not put ourselves in these positions and then have to
19 go back home and say, "Here is what it is going to be,
20 because we have voted, and we passed that." I just don't think
21 we are ready for that. That is just my opinion.

22 The Chairman. Let me announce, if I can, the order, so
23 that members can be prepared, that we will take up issues, at
24 least for the next five titles:

25 Accounting, which we will start on tomorrow and discuss;

1 and then, in order, trusts and estates, pensions, foreign
2 taxation, and bonds, municipal bonds, including effective
3 dates, arbitrage, and everything in that municipal bond
4 section.

5 Now, at some stage, David, if we have gone far enough
6 through accounting and depreciation, I may say, "Wait a
7 minute; we are going to take a day and a half and go back to
8 the three or four issues we have considered, because the
9 members have now gotten their amendments in, and we have been
10 able to harmonize them, and we have 10 or 12 we need to get
11 rid of," and go back to those sections and vote. I do not
12 intend to do that prior to the Easter recess.

13 Senator Pryor. Thank you, sir.

14 The Chairman. Further comments? Senator Matsunaga?

15 Senator Matsunaga. Mr. Chairman, just for purposes of
16 clarification, as I understand it your package provides that,
17 under the five-year ACR class, renewable energy property will
18 continue to be eligible for inclusion as under the current
19 law.

20 The Chairman. Is that correct, John?

21 Mr. Colvin. That is correct.

22 The Chairman. Further comments?

23 (No response)

24 The Chairman. In that case, we will adjourn. We have a
25 vote at 12:00, and we will start on accounting tomorrow

1 morning.

2 (Whereupon, at 11:15 a.m., the meeting was recessed, to
3 be resumed Wednesday morning, March 25.)
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C E R T I F I C A T E

This is to certify that the foregoing proceedings of an Executive Committee meeting of the Senate Committee on Finance on March 25, 1986, was held as herein appears, and that this is the original transcript thereof.

William J. Moffitt

WILLIAM J. MOFFITT
Official Court Reporter

My Commission expires April 14, 1989.