

1 EXECUTIVE COMMITTEE MEETING ON PROPOSED TAX REFORM ACT OF 1986  
2 TUESDAY, MAY 6, 1986  
3 Committee on Finance  
4 Washington, D.C.

5 The committee met, pursuant to recess, at 10:19 a.m. in  
6 Room SD-215, Dirksen Senate Office Building, the Honorable  
7 Bob Packwood (chairman) presiding.

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

12 Also present: Richard Darman, Deputy Secretary of the  
13 Treasury; Roger Mentz, Assistant Secretary for Tax Policy,  
14 Department of the Treasury; Dennis Ross, Tax Legislative  
15 Counsel, Department of the Treasury.

16 Also present: Bill Diefenderfer, Chief of Staff; John  
17 Colvin, Majority Chief Counsel; Bill Wilkins, Minority Chief  
18 Counsel; David Brockway, Chief of Staff, Joint Committee on  
19 Taxation; Randy Weiss, Deputy Chief of Staff, Joint Committee  
20 on Taxation; Greg Jenner, Lindy Paull, Tom Preston, Paul  
21 Strella, Tax Counsel, Majority; Barbara Groves, Trial Counsel,  
22 Minority; Susan Taylor, Executive Assistant.

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24  
25

1 The Chairman. The Committee will come to order,  
2 please.

3 Yesterday, I thought, was a very good day. It was an  
4 amicable day. We dispensed with many of the smaller amend-  
5 ments, and I am hoping today that we can possibly, and I say  
6 possibly, finish the bill. I want the press to understand  
7 "possibly" finish the bill.

8 We were very good yesterday in terms of every member  
9 proposing revenue-neutral amendments, and I thought that was  
10 a very responsible way to go. And I hope we would continue  
11 in that fashion today.

12 Senator Chafee. Mr. Chairman?

13 The Chairman. Senator Chafee.

14 Senator Chafee. Mr. Chairman, it seems to me that that  
15 is a very important aspect of proceeding here. And as we  
16 recall, we went through a process here not long ago, the past  
17 two and prior weeks to that, where there was no revenue  
18 neutrality required. And everything broke down. And I think  
19 that was the experience they had in the House, too.

20 And we found yesterday, Mr. Chairman, that everybody did  
21 exercise restraint as far as amendments go in requiring  
22 revenue neutrality.

23 So, Mr. Chairman, I think there is merit in making that  
24 a requirement. And, therefore, I throw that out. I don't  
25 want to move right now because there may be discussions.

1 The Chairman. Discussion?

2 Senator Moynihan. Mr. Chairman?

3 The Chairman. Senator Moynihan.

4 Senator Moynihan. Mr. Chairman, if Senator Chafee would  
5 make such a move, I would certainly associate myself with it.  
6 I mean we worked well yesterday. It is precisely as he says.  
7 When absent that discipline, these proceedings all but broke  
8 down.

9 Given that discipline as we have had in our private  
10 discussions and in our public meeting yesterday, we clearly  
11 progressed, we clearly moved toward a major piece of  
12 legislation. I hope we would do that, and I would hope the  
13 Chair would move it or Senator Chafee.

14 The Chairman. Senator Bradley and then Senator Bentsen.

15 Senator Bradley. Mr. Chairman, I think this is an  
16 excellent idea. It does give some discipline to the process.  
17 It gives some discipline to the process, and I think that is  
18 essential to getting a bill. And I certainly would support  
19 it.

20 The Chairman. Senator Bentsen.

21 Senator Bentsen. Well, I, frankly, would hope for more  
22 freedom in the offering of amendments, but with that kind of  
23 a limitation, I will probably give you a multiple choice on  
24 the second part.

25 Senator Long. Could I make this suggestion and see how

1 it appeals to the Committee?

2 I would like to suggest that a Senator can offer an  
3 amendment subject to finding a way subsequently to pay for it.  
4 That is, if the Committee liked the amendment, they could say,  
5 well, we will go with it to this extent, but you have got to  
6 find a way to pay for it.

7 And if at some point between then and the time we report  
8 the bill, either he or we find a way to pay for it, that it  
9 goes in the bill. If we can't, it doesn't go in the bill.

10 The Chairman. Well, I would hope we would not start  
11 down that ladder route because that is roughly where we were  
12 on the old bill. If you want to vote to get rid of something  
13 that costs \$10 billion, go ahead; \$20 billion, go ahead; and  
14 at the end of it, if we can find the money, fine. I just  
15 think the process would absolutely break down if we start  
16 down that road.

17 Senator Chafee, do you want to put that motion?

18 Senator Chafee. Mr. Chairman, I agree. It seems to me  
19 that to defer it, it gets all the temptation to go ahead with  
20 the program and not have, as has been mentioned here, the  
21 discipline of really doing it.

22 So, Mr. Chairman, I would move that all amendments must  
23 be revenue neutral. In other words, if you want to spend  
24 some money -- and we have got estimates on everything here --  
25 you have got to find a way to pay for it.

1 Senator Moynihan. Mr. Chairman?

2 The Chairman. Senator Moynihan.

3 Senator Moynihan. If I may, I would like to join Senator  
4 Chafee.

5 The Chairman. Further discussion?

6 Senator Durenberger. Mr. Chairman?

7 The Chairman. Senator Durenberger.

8 Senator Durenberger. Mr. Chairman, I think this is a  
9 very agonizing vote for everybody around here. And I made up  
10 my mind late yesterday to support this amendment. And I did  
11 it because you didn't do it to us earlier in the process, and  
12 you could have. And I think in some way you could have  
13 found a way to force this kind of a process on us very early  
14 on. But because you didn't and because each of us did have  
15 an opportunity to go through this process without the dollars  
16 that directly involved until we got to crises last week and  
17 you pulled us back in, I feel an obligation to support you  
18 and to support John's amendment.

19 The Chairman. Well, I thank my good friend.

20 Further discussion?

21 (No response)

22 The Chairman. All those in favor of the amendment will  
23 say aye.

24 (Chorus of ayes)

25 The Chairman. Opposed, no.

1 (No response)

2 The Chairman. Nos have it.

3 Senator Armstrong. Mr. Chairman, did you mean to say the  
4 nos have it?

5 The Chairman. Excuse me. The ayes have it. I  
6 apologize.

7 (Laughter)

8 The Chairman. Senator Armstrong.

9 Senator Armstrong. Mr. Chairman, are you ready to begin  
10 considering amendments?

11 The Chairman. Yes.

12 Senator Moynihan. Mr. Chairman, I had an amendment to  
13 offer.

14 The Chairman. Bill, Pat did ask me if he could offer the  
15 first one, and I said that he could.

16 Go right ahead.

17 Senator Moynihan. Mr. Chairman, as you know, this  
18 legislation is singular in that it does provide for the  
19 complete elimination of the deductibility of sales taxes for  
20 income tax purposes for those who itemize, where it maintains  
21 the present deduction for state and local taxes, for property  
22 taxes -- state and local taxes, for property taxes and  
23 for personal taxes.

24 Now the difficulty with this is that the incidence of  
25 the sales tax as a source of state and local revenue varies

1 widely across the country. The numbers are quite striking.

2 In Wyoming, 64 percent of the state taxes come from  
3 sale taxes. In Louisiana, 54 percent. As I go through  
4 members of this Committee --

5 Senator Long. I wrote that down.

6 Senator Moynihan. Texas, 40 percent. Oklahoma, 40  
7 percent. And then other states. At the other end, much less.  
8 Nationally, 13.

9 And my amendment, which I think has been discussed  
10 formally with many of us, would simply do this: We don't want  
11 to raise the level of corporate tax basis much higher than  
12 we now have it at 33 percent, although it is 35 percent in  
13 the House bill; 35 percent with the President's original  
14 proposal.

15 I would suggest, Mr. Chairman, that we permit a two-  
16 third deductibility of itemized sales tax; that this be  
17 paid for by a one percent increase in the corporate tax from  
18 33 to 34. It will still make it less than it -- than the  
19 President's proposal.

20 And the result would not be applied to principle  
21 because it is already the case that Federal Government does  
22 not allow the deduction of some sales taxes. It does not  
23 allow the deduction of gasoline taxes. In contrast to  
24 property taxes and state and local income taxes, which are  
25 sacrosanct as in present law, and for which our bill, the

1 Chairman's bill, maintains present law, this would maintain  
2 present practice of permitting, in effect, a fixed proportion  
3 of the sales taxes to be deducted, if itemized. It  
4 parallels the present practice of only allowing on a  
5 proportion.

6 That is the proposal, Mr. Chairman. I could elaborate,  
7 but I think others would like to speak.

8 Senator Heinz. Is there a writeup of this amendment?  
9 Is there a description of the amendment?

10 The Chairman. Senator Heinz.

11 Senator Heinz. Is there a description of the amendment?

12 Senator Moynihan. No. I just made a -- you just heard  
13 it. I could write it up for you.

14 (Laughter)

15 Senator Heinz. Well, I gather this is a very significant  
16 amendment to a lot of people, and it is going to reduce or  
17 restore two-thirds of the deductibility of the sales tax.  
18 Now this is just the state sales tax or is this all state  
19 and --

20 Senator Moynihan. All sales tax.

21 Senator Heinz. -- local sales tax?

22 Senator Moynihan. Right. We estimate that to bring  
23 the Federal Government -- that deductibility is worth \$18  
24 billion. Once it has been increased in the corporate tax of  
25 \$12 billion; that is two-thirds.



1           Senator Heinz. Now in addition to sales taxes, what  
2 about the excise taxes that states impose on gasoline? Do  
3 you seek to change any of the existing laws?

4           Senator Moynihan. Present law. I am only referring to  
5 what are now itemized and itemizable. And I make the point  
6 that this is a mixed practice in the case of the Federal  
7 Government now. It would continue to be. Whereas, income  
8 taxes, state income taxes and local property taxes, there is  
9 now complete deductibility.

10          Senator Heinz. Well, Mr. Chairman, do we have -- can  
11 we just also make sure that we are all correct on the revenue  
12 estimates here? What is two-thirds -- restoring two-thirds  
13 of the deductibility of sales taxes cost? And what does one  
14 percent, 33 to 34, bring in?

15          Mr. Brockway. They should both be approximately \$12  
16 billion.

17          Senator Heinz. Twelve billion dollars each. All right.

18          Now, Mr. Chairman, I would like to speak, I guess, on  
19 the merits of the amendment. The first is as an issue of tax  
20 policy. Speaking for myself, I have always had some real  
21 difficulty saying that you can take 80 percent of this  
22 deduction or 20 percent of that deduction or 50 percent of  
23 another deduction.

24          It seems to me that either something should be deducted  
25 or it shouldn't be deducted. And I don't understand from the

1 standpoint of the tax policy -- I understand from the  
2 standpoint of revenue neutrality, but from the standpoint of  
3 tax policy, I have serious concerns about voting for two-  
4 thirds or one-third or any fraction of deductibility for any  
5 deduction, no matter how legitimate.

6 My view is that if we don't want to allow something,  
7 fine; we shouldn't. If we are going to allow it, fine; we  
8 should.

9 The second issue, it seems to me, on Senator Moynihan's  
10 proposal is that if we adopt his amendment, it will be a  
11 rather different kind of revenue neutrality. Because what  
12 we will be doing is shifting revenue, shifting costs, from  
13 the corporate side to the individual side, and we will be  
14 doing so for the benefit of relatively well-to-do taxpayers.  
15 These are itemizers. These are not the people who we hoped  
16 through the very substantially increased personal exemption,  
17 the very much increased standard deduction, which should  
18 reduce, frankly, the number of itemizers quite substantially.

19 We are potentially talking about a provision that is  
20 really only going to benefit the -- oh, I don't know -- the  
21 20 or 30 percent wealthiest taxpayers in the United States.

22 And I think it is going to do two things. One, it is  
23 going to throw our distribution curve off. It is going to  
24 give a much larger effective tax cut to the rich.

25 Now on the sheets that Senator Packwood, our Chairman,

1 handed out, I would suggest we have already -- we are pretty  
2 close to the problem line. We are already giving people  
3 earning \$200,000.00 and above a 4.7 percent tax cut. People  
4 of \$30,000.00 to \$40,000.00 are only getting a five percent  
5 tax cut, just a fraction more than 4.7 percent.

6 And I would be willing to wager that this \$12 billion  
7 item is going to give the wealthy a much larger tax cut than  
8 those middle income people and a lot of other people below  
9 \$200,000.00 that I just referred to.

10 Secondly, it makes a major change in what Senator  
11 Packwood decided to do. Senator Packwood said he wanted to  
12 have a transfer of about \$90 billion, \$90 to \$100 billion, of  
13 tax burden from individuals to corporations. This will  
14 increase the transfer of that tax burden by well over 10  
15 percent, by \$12 billion.

16 And we will, if the numbers I have are correct, we will  
17 be very close to the Administration's proposal of transferring  
18 about \$120 billion in tax burdens.

19 And, Mr. Chairman, I fear that this extra increase in the  
20 corporate tax burden could be the straw that turns the  
21 business community against this tax reform bill. I would hate  
22 to see that happen.

23 Finally, I worry that if we get into the business of  
24 simply adding taxes on business to give more money to rich  
25 people that we are going to bring down the entire tax reform

1 bill.

2 Right now, this tax reform bill gives a tax cut of  
3 close to \$10,000.00, just a little under \$10,000.00, to people  
4 earning \$200,000.00 in income. It gives a tax cut of about  
5 \$1,500.00 to people earning around \$30,000.00. And that is  
6 called a tax cut that is six times, six and a half times,  
7 bigger for the wealthy than for the middle income taxpayer.

8 Senator Moynihan's amendment is going to give an even  
9 bigger tax cut to the rich. And if he could find a way to do  
10 it where we wouldn't jeopardize the distribution here, I  
11 might have a much more open mind on the amendment.

12 And I understand that there are people from states with  
13 substantial sales taxes. And I don't want to be accused of  
14 trying to gore the oxes in those states. And I am sympathetic  
15 to that problem.

16 But this particular approach to dealing with the sales  
17 tax issue is going to make our distribution table top-heavy,  
18 and I suggest that it will make the entire effort vulnerable  
19 to being attacked a rich man's tax bill. It is very close to  
20 that already. With the Moynihan amendment, it would become  
21 a rich man's tax cut bill.

22 Senator Durenberger. Mr. Chairman?

23 The Chairman. Senator Durenberger, and then Secretary  
24 Mentz, and then Bill Bradley.

25 Senator Durenberger. Mr. Chairman, let me begin where my

1 colleague from Pennsylvania left off with the understanding  
2 that he can see where Senators from certain states would raise  
3 this issue.

4 I happen to be from a state that is one of 12 whose  
5 taxpayers lose less than 25 percent of the value of their  
6 tax savings. So I think I qualify here as somebody who has  
7 more to gain from not messing around with this amendment than  
8 who does, at least as far as the constituency of Minnesota  
9 that I represent.

10 But I am not here to represent a Minnesota constituency.  
11 I don't think any of us are. We are here to represent a  
12 national constituency as we reform the way in which part of  
13 their tax dollars are going to be collected.

14 And I think the argument that this is a tax break for  
15 the wealthy -- if it is benefitting the top 10 to 30  
16 percent of "the wealthiest taxpayers in the United States" --  
17 and we heard yesterday that 80 percent of the taxpayers are  
18 going to be in the category of under \$28,000.00 in taxable  
19 income per year -- I don't think this is an amendment that  
20 particularly favors the wealthiest taxpayers. It favors  
21 anyone who has the opportunity to pay a sales tax and to take  
22 a deduction for it.

23 But, Mr. Chairman, this amendment is getting us to the  
24 heart of what may potentially be the problem with what we  
25 are doing with this bill. Russell Long in one of our sessions

1 here in the last couple of days made a very prescient  
2 request of Joint Tax and the Treasury. And they said at some  
3 point in time, ladies and gentlemen, let us have an analysis  
4 of the distributional effect of this bill on all taxpayers  
5 in this country based on all of the taxes that they pay.

6 And that means that when you take this little table we  
7 have here at Page 3 of our handout, and you work down the  
8 so-called distributional effect of this two bracket, 15-27  
9 percent bracket, all by itself, you can squeeze out a favorable  
10 looking distributional effect.

11 But when you figure that each of these taxpayers is also  
12 paying a payroll tax, for example, you will find out that  
13 most Americans will reach J. Rockefeller or Jack Danforth  
14 or John Heinz's tax bracket at \$28,000.00 of taxable income.  
15 But they will also pay a payroll tax to the maximum of their  
16 income, whereas the rest of these gentlemen ain't going to  
17 pay any payroll tax on the last 95 percent of their income.

18 On top of that, everybody pays a sales tax, but everybody  
19 pays a sales tax differently depending upon where they are  
20 located and what their purchasing capacity is.

21 And now I am not here to make any gallantarian argument  
22 that somehow or other we are going to end up having every  
23 taxpayer in America pay the same proportion of income. But I  
24 would like to make the argument, Mr. Chairman, that it  
25 shouldn't make any difference where in American you happen to

1 be living that skews the federal policy towards that state and  
2 local taxes that you pay.

3 If you happen to be living in New Mexico today, 72.8  
4 percent of the public services delivered in the state of New  
5 Mexico are paid for from the sales tax. I don't know whether  
6 that is because it is federally deductible or not. But I  
7 can tell you the politicians' behavior is that when you  
8 eliminate the deductibility of the sales tax in New Mexico,  
9 they are either going to have to go someplace else to raise  
10 their revenue or they are going to have to drastically  
11 reduce --

12 Mr. Chairman, could we have order?

13 I am sure there are more important issues to a lot of  
14 the people who are sitting in this room than this particular  
15 issue. But it would be very helpful if on something that  
16 doesn't have a selfish economic interest, the Senator is  
17 only pointing us in the direction of equity for taxpayers  
18 generally for America, that we could at least listen to both  
19 sides of this argument.

20 So if you happen to be in New Mexico or you happen to  
21 be in Louisiana at 68.9 or Nevada or Tennessee or Washington  
22 or Mississippi, if you happen to be in a state where public  
23 education is more than 50 percent financed out of the sales  
24 tax -- North Carolina, Florida, South Carolina, Indiana,  
25 Washington, Idaho, Iowa -- more than 50 percent of public

1 education, elementary and secondary education, is financed  
2 out of the sales tax.

3 So I don't want to take other members' time. But I  
4 think there is a more important issue here, Mr. Chairman,  
5 than just whether or not somebody is going to get a benefit  
6 that is denied somebody else. We are playing with the tax  
7 policies of the states in this country. And we are doing it  
8 at a time when we are devolving on them greater responsi-  
9 bility to use local-base taxes like property or sales taxes.

10 I just think it is unfair. Now I don't think this is  
11 probably the right solution. If this fails, Mr. Chairman, I  
12 am going to offer an amendment that we increase the rate on  
13 individual income taxes to 27.5 or whatever it takes to do  
14 this.

15 I didn't set the 27 percent. Somebody else did the 27  
16 percent because they couldn't close enough other loopholes,  
17 and they had to take the sales tax out. So I will come back  
18 if this one fails, and I will offer you a chance on a  
19 different way to raise the revenue.

20 The Chairman. Secretary Mentz and then Senator Bradley.

21 Mr. Mentz. Thank you, Mr. Chairman.

22 The Treasury Department opposes Senator Moynihan's  
23 amendment. Let me give you some statistics. Thirty-three  
24 percent of the individual income tax returns in the lowest  
25 brackets derive two percent of the benefits from the



1 deductibility of sales tax.

2 The Chairman. Say that again.

3 Mr. Mentz. Thirty-three percent of the individual income  
4 tax returns in the lowest brackets derive only two percent of  
5 the benefits from the sales tax deduction; whereas, the upper  
6 five percent of taxable returns derive 28 percent. Five  
7 percent at the top end, Senator Heinz, obtain 28 percent of  
8 the benefit.

9 This is simply the numerical demonstration of the point  
10 that you articulated earlier -- that the benefits are  
11 significantly skewed in favor of the high-income taxpayer.

12 Senator Durenberger. What percentage of the tax does  
13 those top five percent pay? The total income tax.

14 Mr. Mentz. I don't have that.

15 Senator Durenberger. Maybe you could get that figure.

16 Mr. Mentz. I am sure I can.

17 Let me give you another statistic.

18 Senator Long. How about the people in the middle? How  
19 much do they derive? You haven't given us all the figures.  
20 You say five percent get 28 percent; 33 percent get 2 percent.  
21 What does the middle part get? Where do they come out?

22 Mr. Mentz. Well, people between \$30,000.00 and  
23 \$50,000.00 of adjusted gross income get 45 percent of the  
24 benefits.

25 Senator Long. Forty-five percent?

1 Mr. Mentz. Yes.

2 Senator Long. All right.

3 Mr. Mentz. People between 15 and 20 who have 11 percent  
4 of the taxable returns get four percent of the benefits.  
5 That, obviously, the higher up you get, the more benefits  
6 from the sales tax deduction as you might well expect.

7 Another area that is of intense concern to the IRS is  
8 compliance rate. Forty-one point -- there is an error rate --

9 Senator Long. What percent of people in that 30 to 50  
10 percent bracket, by the way? What percent of people in that  
11 bracket?

12 Mr. Mentz. I don't have that percentage, Senator, but  
13 I can find it for you.

14 Senator Mitchell. Mr. Chairman, if I could follow up  
15 on what you said.

16 Mr. Mentz, you conveniently had two categories. You  
17 said 33 percent at the bottom get two percent.

18 Mr. Mentz. Yes.

19 Senator Mitchell. The five percent at the top get  
20 28 percent. You may not have the middle figures, but by  
21 the process of deduction, we can conclude that the 62 percent  
22 in the middle get 70 percent of the benefit.

23 (Laughter)

24 Senator Mitchell. You don't happen to have those figures,  
25 but isn't that correct?

1 Mr. Mentz. I can give you a table of the figures,  
2 Senator.

3 Senator Mitchell. We don't need your table.  
4 (Laughter)

5 Senator Mitchell. I mean 62 percent in the middle get  
6 70 percent of the benefits.

7 The Chairman. Let me ask the question a slightly  
8 different way. On any kind of itemized deductions that are  
9 left that we are going to debate, I would assume that almost  
10 all itemized deductions have to tilt slightly toward the  
11 upper income levels because they are the ones who itemize.

12 Mr. Mentz. Yes. I think that is the point.

13 The Chairman. Now we have got a distribution table  
14 now for those who are worried about the defense of this.  
15 Those over \$200,000.00 get a 4.7 percent break. Then going  
16 down, 100 to 200, 3.6; 75 to 100, 3.2. You have to go clear  
17 down to the 40 to 50 group before you get to a group that  
18 gets a larger break than the richest people in the country.  
19 And the elimination of the sales tax deduction cannot do  
20 anything but further skew that chart. Isn't that correct?

21 Mr. Mentz. Exactly.

22 On the compliance problem, there is an error rate on  
23 sales and personal property. We did not have it broken out  
24 because the original proposal was to disallow both. The  
25 error rate is 41.5 percent based on the 1982 taxpayer maximum

1 compliance audit. And had the errors not been there, the  
2 extrapolated number would be an increase in federal revenues  
3 of \$107 million. In other words, if the compliance were 100  
4 percent on those two taxes, you would have had \$107 million  
5 more revenue than was actually produced.

6 The personal property tax has got to be a very small  
7 portion of that. And the sales tax is the large portion of  
8 it, of course.

9 And, finally, I would just like to support the  
10 Chairman's 33 percent maximum corporate tax rate. That was  
11 the President's rate. And I agree with the statement of  
12 Senator Heinz that I think it is very important. Treasury  
13 thinks it is very important that we retain that rate.

14 The Chairman. Senator Bradley.

15 Senator Bradley. Mr. Chairman, let me say that I would  
16 like to keep the sales tax deduction. I would also like to  
17 get tax reform. And I think that it is interesting that the  
18 first amendment that is offered poses a question most  
19 directly for me, and that is: What are you willing to give  
20 up in order to get tax reform?

21 And I think there are a number of facts that you have to  
22 look at when you consider the sales tax deduction. First,  
23 only about 20 to 25 percent of the total sales tax is  
24 deducted. Seventy-five to 80 percent is not deducted. And  
25 it is understandable why. Did you ever try to fill out

1 the form?

2 And the second point is that there are about 30 states  
3 in this country whose state income tax systems are tied to  
4 the federal income tax system. Any change in the federal  
5 income tax system automatically is a change at the state  
6 level, which means that if we broadened the tax base at the  
7 federal level, the state tax base is automatically broadened,  
8 which means, given the income tax rate in certain states,  
9 they will have additional revenue.

10 And with that additional revenue, they then have a choice.  
11 They can spend it or they can cut the sales tax. And it would  
12 be my hope that if tax reform passed that with that additional  
13 revenue they would cut the sales tax, which would benefit  
14 100 percent of the people who buy goods that have sales taxes  
15 on them.

16 So, Mr. Chairman, I think that the important thing here  
17 is to get this bill. And I am willing to vote against this  
18 amendment in order to move this process forward and give  
19 these states a chance to cut the sales tax for all consumers.

20 The Chairman. Might I add a few comments?

21 The argument that is made by my good friend from  
22 Minnesota about it falls disproportionately on some states --  
23 this is a federal structure. I don't know how many times I  
24 have heard Senator Bentsen talk about the unfair distribution  
25 of the gasoline tax revenues. I can't remember how much Texas

1 pays in in comparison to how little they get back. But I  
2 have heard you make the argument over and over.

3 Big states in the West, people drive a lot. Smaller  
4 states in the East, they don't drive as much. So you have  
5 an income transfer from big driving states on the gasoline  
6 tax to smaller mass transit states. And I don't find that  
7 many people complain about it. That is part of the federal  
8 structure.

9 Secondly, 33 percent is a magic figure like 27 percent.  
10 We have got going for us a bill that the public, including  
11 the business and non-business public who are in legitimate  
12 businesses producing jobs and good for America, are going to  
13 like. And for us to start going up on that 33 percent rate  
14 or the 27 percent rate is going to serve us ill.

15 Lastly, I want you to remember the one promise that was  
16 made in the House when the bill passed. And that the promise  
17 had to be made to get the bill passed: There will be no  
18 limitation on the elimination of deduction of local taxes of  
19 any kind. And without that promise, the bill could not have  
20 passed in the House.

21 And, frankly, if we can go to conference with the  
22 House with the elimination of the sales tax deduction in our  
23 bill, it is a tremendous persuader in our hands to help the  
24 Committee hold any number of things that are in this bill.

25 Senator Moynihan. Mr. Chairman?

1 The Chairman. Senator Moynihan.

2 Senator Moynihan. May I make a very brief response  
3 to say that I am going to be for a tax reform bill regardless  
4 of how a number of amendments come out. You know that. But  
5 I am not sure how the whole the Committee is going to be  
6 and how the country is going to be. And what Senator  
7 Durenberger said very forcefully, I would like to reinforce.

8 What we are doing here is we are raising local taxes in  
9 order to cut federal taxes. That is not a very good  
10 precedent in a federal system. And most especially we are  
11 raising school taxes. School taxes go up in order that we  
12 can cut back the pot.

13 I don't think that is a good precedent. I want to say  
14 that it is important that we have kept the deductibility of  
15 state and local income tax, property tax.

16 The present situation is mixed with respect to sales  
17 tax. And this would acknowledge that mix. I hope the  
18 Committee can do this. I hope the Treasury would recognize  
19 that the Administration was willing to see a 35 percent on  
20 corporate tax on the first go around, and this would make it  
21 a 34. We would be exactly in the middle.

22 The Chairman. Senator Dole, Senator Wallop, Senator  
23 Heinz.

24 Senator Dole. I would just say very briefly, Mr.  
25 Chairman, I think I understand the price tag is about \$12

1 billion. I supported Senator Moynihan in his original  
2 efforts on state and local taxes. We were then talking about  
3 a 35 percent rate. And I think about that time we saw the  
4 bill sort of disintegrating, our efforts disintegrating.

5 Having been the Chairman of this Committee, I know that  
6 a tax bill is the result of compromise. And it would seem to  
7 me now that we are talking about a 27 percent top rate --  
8 hopefully, we can hold the corporate rate to 33 percent -- we  
9 really don't have much choice as much as we would like to be  
10 supportive.

11 And I think in the final analysis we have to look down  
12 the road to the Senate floor action and to conference action,  
13 so I intend to reluctantly vote against the amendment.

14 The Chairman. Senator Wallop.

15 Senator Wallop. Mr. Chairman, you have heard me before,  
16 the Committee has -- one of the legs on the stool of tax  
17 reform is simplicity. And Senator Bradley was quite correct  
18 in pointing out why most people don't itemize sales tax is  
19 because of the complexity of the form.

20 Now you take the amendment, which is two-thirds of all  
21 itemized state and local general sales tax would be deducted,  
22 you get another computation. And I would say to my friend  
23 from New York; Those most benefitting by this are those who  
24 are in a position to hire legions of accountants.

25 Senator Moynihan. I would say to my dear friend from



1 Wyoming: Consider how much of a spur this would be to  
2 back to basics in education.

3 (Laughter)

4 Senator Moynihan. Two-thirds times --

5 (Laughter)

6 The Chairman. Senator Heinz.

7 Senator Heinz. Mr. Chairman, I think it is important  
8 to make the distinction here about the difference between the  
9 merits of the issue and whether we want to eliminate the  
10 deductibility of sales taxes and what Senator Moynihan's  
11 methodology for paying for that does.

12 Now I have always been reasonably sympathetic to  
13 retaining the deductibility of all state and local taxes.  
14 My biggest single problem, as I said earlier, is that this  
15 becomes a very handsome, nice tax cut for the wealthiest  
16 people, as has been attested to.

17 There is one other factor that I think we need to focus  
18 on. Right now, about 62 percent of the tax returns claim the  
19 standard deduction and do not, therefore, itemize. And that  
20 is under today's very complex tax system.

21 If we pass the bill that is anything like the bill before  
22 us now, with all the limitations on tax shelters, with the  
23 limitations on deductions and most importantly with the  
24 substantial increases in the personal exemption of \$2,000.00  
25 per person, the increase in the zero bracket amount, the

1 standard deduction for a family of four for \$5,000.00, we  
2 are going to have substantially less itemizers.

3 And in discussing this with Mr. Brockway and Mr. Weiss,  
4 I am advised that if today some 38 percent of returns are  
5 itemized, we could expect to have as few as 28 or even 25  
6 percent of returns being itemized under this legislation.

7 Mr. Weiss or Mr. Brockway, is that not roughly correct?

8 Mr. Weiss. It would be somewhere between 25 and 30  
9 percent, we think.

10 Senator Heinz. And as a result, since we all know there  
11 is a correlation of itemization with income, Senator  
12 Moynihan's amendment, no matter how well intentioned, it  
13 necessarily skews toward upper income taxpayers.

14 Pat, I would hope you could find a different way of  
15 paying for something in this area so that we don't run into  
16 the distributional argument.

17 Senator Moynihan. I think Senator Durenberger has that  
18 point.

19 The Chairman. Senator Bentsen.

20 Senator Bentsen. Thank you very much, Mr. Chairman.

21 I note on that chart that Texas is one of those states  
22 that is generally favored by this amendment. But I think  
23 what we are doing here is a very exciting and productive thing  
24 in trying to work out true tax reform. And I am very hopeful  
25 we can do it.

1 I don't see any particular burden by what the Chairman  
2 has done insofar as an inequity. And that is the type of  
3 thing I am trying to deal with because I have a couple of  
4 them where we have true economic losses that really disturb  
5 me.

6 And, hopefully, we can do some things to try to work  
7 that out.

8 But certainly I have gone along with Senator Moynihan  
9 on his ad valorem taxes. But on this one where it is a  
10 question of itemizing and further simplification that we are  
11 trying to achieve and the very highest tax brackets are the  
12 ones who are benefitting by it, frankly, I am going to oppose  
13 the amendment and go along with the Chairman on it.

14 The Chairman. Senator Moynihan, and then I think we  
15 are probably ready for a vote.

16 Did you have a closing comment?

17 Senator Moynihan. No, Mr. Chairman.

18 The Chairman. The Clerk will call the roll on the  
19 Moynihan amendment.

20 The Clerk. Mr. Dole?

21 Senator Dole. No.

22 The Clerk. Mr. Roth?

23 Senator Roth. No.

24 The Clerk. Mr. Danforth?

25 Senator Danforth. No.

1 The Clerk. Mr. Chafee?  
2 Senator Chafee. No.  
3 The Clerk. Mr. Heinz?  
4 Senator Heinz. No.  
5 The Clerk. Mr. Wallop?  
6 Senator Wallop. No.  
7 The Clerk. Mr. Durenberger?  
8 Senator Durenberger. Aye.  
9 The Clerk. Mr. Armstrong?  
10 Senator Armstrong. Aye.  
11 The Clerk. Mr. Symms?  
12 Senator Symms. No.  
13 The Clerk. Mr. Grassley?  
14 Senator Grassley. Aye.  
15 The Clerk. Mr. Long?  
16 Senator Long. Aye.  
17 The Clerk. Mr. Bentsen?  
18 Senator Bentsen. No.  
19 The Clerk. Mr. Matsunaga?  
20 Senator Moynihan. No, by proxy.  
21 The Clerk. Mr. Moynihan?  
22 Senator Moynihan. No.  
23 The Clerk. Mr. Baucus?  
24 Senator Moynihan. Oh, wait, forgive me. Yes. Aye,  
25 by proxy for Senator Matsunaga. Aye for Moynihan. I was

1 hearing so many nos.

2 (Laughter)

3 The Clerk. Mr. Baucus?

4 Senator Baucus. No.

5 The Clerk. Mr. Boren?

6 Senator Boren. No.

7 The Clerk. Mr. Bradley?

8 Senator Bradley. No.

9 The Clerk. Mr. Mitchell?

10 Senator Mitchell. Aye.

11 The Clerk. Mr. Pryor?

12 Senator Pryor. No.

13 The Clerk. Mr. Chairman?

14 The Chairman. No.

15 The Clerk. Seven yeas, 13 nays.

16 The Chairman. The amendment is defeated.

17 Dave, I forgot that I promised Bill Armstrong next.

18 He had his hand up. Unless you want to defer to Senator

19 Durenberger.

20 Senator Durenberger. I will just explain what I intend

21 to do. I intend to offer an amendment to restore the

22 deductibility of sales tax in full; to finance it with a

23 27, changing the top rate on individuals to 27.

24 The Chairman. Changing the top rate?

25 Senator Durenberger. I won't make a lot of arguments.

1 Oh, pardon me. That would be twenty-seven and  
2 a half, 27.5.

3 The Chairman. You want to offer it?

4 Senator Armstrong. It seems to me to be related to the  
5 issue we have just been discussing, so why don't we go ahead  
6 and take that next and finish that up.

7 The Chairman. It would eliminate the -- it would  
8 allow the deduction of the sales tax by raising the personal  
9 tax rate to 27-1/2 percent, right?

10 Senator Durenberger. Yes, Mr. Chairman. I am not going  
11 to make any other arguments for it. I think most of the  
12 arguments have been made here. There is a clear difference  
13 of opinion as to how we are going to impact on taxpayers and  
14 on policymakers in this country.

15 I would just, on the subject of Treasury's support for  
16 this, I would just cite them to one quotation. It goes as  
17 follows. It is in favor of retaining the deductibility:  
18 "Some argue that itemized deductions should be eliminated for  
19 some taxes but retained for others. Elimination of any one  
20 tax deduction would have an uneven effect on taxpayers among  
21 the states. In addition, since state and local governments  
22 would be likely to increase reliance on the remaining  
23 deductible taxes, disallowing deductions for particular taxes  
24 is likely to lead to sizable distortions and state and local  
25 revenue mix. For example, disallowing only the sales tax

1 deduction might force a state like Washington that relies  
2 heavily on the sales tax but does not have an individual  
3 income tax to adopt one."

4 That is a statement by Ronald Reagan, President of the  
5 United States, in his tax reform proposal in 1985. I think  
6 it is good judgment on the part of a former governor, now the  
7 President. And I would recommend that my colleagues support  
8 this amendment.

9 Senator Chafee. And you would have the no capital  
10 gains? You would not insert any differential so the capital  
11 gains would follow?

12 Senator Durenberger. That is correct.

13 The Chairman. I think the subject is well understood.  
14 Do you want a roll call?

15 Senator Durenberger. Yes.

16 The Chairman. The Clerk will call the roll on the  
17 Durenberger amendment.

18 The Clerk. Mr. Dole?

19 Senator Dole. No.

20 The Clerk. Mr. Roth?

21 Senator Roth. No.

22 The Clerk. Mr. Danforth?

23 Senator Danforth. No.

24 The Clerk. Mr. Chafee?

25 Senator Chafee. No.

1 The Clerk. Mr. Heinz?  
2 Senator Heinz. No.  
3 The Clerk. Mr. Wallop?  
4 (No response)  
5 The Clerk. Mr. Durenberger?  
6 Senator Durenberger. Aye.  
7 The Clerk. Mr. Armstrong?  
8 Senator Armstrong. No.  
9 The Clerk. Mr. Symms?  
10 Senator Symms. Aye.  
11 The Clerk. Mr. Grassley?  
12 Senator Grassley. No.  
13 The Clerk. Mr. Long?  
14 Senator Long. Aye.  
15 The Clerk. Mr. Bentsen?  
16 Senator Bentsen. No.  
17 The Clerk. Mr. Matsunaga?  
18 Senator Moynihan. Aye, by proxy.  
19 The Clerk. Mr. Moynihan?  
20 Senator Moynihan. Aye.  
21 The Clerk. Mr. Baucus?  
22 Senator Baucus. No.  
23 The Clerk. Mr. Boren?  
24 Senator Boren. No.  
25 The Clerk. Mr. Bradley?



1 Senator Bradley. No.

2 The Clerk. Mr. Mitchell?

3 Senator Mitchell. Aye.

4 The Clerk. Mr. Pryor?

5 Senator Pryor. Aye.

6 The Clerk. Mr. Chairman?

7 The Chairman. No. Wallop, no by proxy.

8 The Clerk. Seven yeas, 13 nays.

9 The Chairman. The amendment is defeated.

10 Senator Armstrong?

11 Senator Armstrong. Mr. Chairman, on behalf of Senator  
12 Moynihan and myself, I offer an amendment to retain the full  
13 deduction for business meal and entertainment expense, and  
14 to pay for it by a corresponding increase in the corporate  
15 income tax rate, which would be a one percentage increase in  
16 the corporate rate.

17 Mr. Chairman, I judge that this is a day to really get  
18 to the nub of it and be pretty brief. And so I just want to  
19 tick off four reasons why I hope the Committee will adopt this  
20 amendment and not argue it at length.

21 The first is that it is equitable. In my judgment, it  
22 is simply unjust to single out one classification of  
23 business expense and say we are going to allow full  
24 deductibility for everything except this one classification.  
25 We don't say we are only going to permit 80 percent deduction

1 for salaries or cost of goods sold or for any other  
2 classification of business expense. We say if it is a  
3 business expense, it is business expense; you deduct it 100  
4 percent. That has always been the rule. That is what is  
5 fair.

6 And so I can't see the justification for an 80 percent  
7 rule for business meals and entertainment expenses. So the  
8 first argument I would ask my colleagues to consider is  
9 simply tax principle equity.

10 Second, I want to point out that if we actually should  
11 adopt and enact into law the 80 percent deduction rule, it is  
12 going to have enormous economic consequences.

13 I have cause to be put before you, Senator Moynihan and  
14 I have, a writeup of our amendment. And, in addition, an  
15 additional writeup showing the economic impact on each of  
16 the states of members of the Committee.

17 But I will just tell you even in small states like the  
18 smallest here, according to econometric projections, we are  
19 talking about a loss of sales of as little as \$50 million in  
20 small states and over a billion dollars in the biggest states  
21 which are represented around the room. And each of you has  
22 that information before you and can judge for yourself.

23 But according to Chase Econometrics, we are talking about  
24 a loss of sales of \$2 billion over the next two years based  
25 on their projections. Now that is not just hypothetical. I

1 might point out to my colleagues that Australia tried this  
2 notion last year, and in three months, there was a 30 percent  
3 drop in restaurant sales volume. Ten thousand people lost  
4 jobs, a number of restaurants closed up and all of the  
5 auxilliary and secondary and tertiary industries showed  
6 corresponding effect.

7 So what we are really talking about is a huge economic  
8 effect as well and on a segment of employment which is the  
9 least able to sustain that kind of a loss. We are talking  
10 about waitresses and busboys and cooks and that kind of thing.  
11 Many of them in central cities because a lot of this, of  
12 course, is that kind of revenue.

13 Senator Bradley. Australia had a bad winter.

14 Senator Armstrong. Maybe we will have a bad winter, too.

15 Finally, Mr. Chairman, my fourth argument, and then I  
16 will be happy to yield the floor, is that this amendment is  
17 revenue neutral in keeping with the decision we have made.  
18 And it is not only revenue neutral in the sense that it pays  
19 for itself, but that it pays for itself out of the same  
20 segment which is advantaged by the amendment. In other words,  
21 this is an advantage to business, but it is paid for by a  
22 higher corporate rate, which seems to me also to be consistent  
23 with just principles of taxation.

24 Senator Moynihan. Mr. Chairman?

25 The Chairman. Senator Moynihan and then Senator Symms.

1           Senator Moynihan. May I join Senator Armstrong in this  
2 matter and make emphatically the point that this is a matter  
3 that is -- the gains are small to the Treasury and the loss  
4 is so very large to the communities. They go across a great  
5 range of enterprises. The theater no less than the  
6 restaurant world and the hotel world.

7           The small, medium sized businesses are those which are  
8 particularly dependent on this type of business solicitation.  
9 It is an economic activity which ought to be an economic cost.  
10 We feel very strongly about that, and we plead the experience  
11 of Australia which was very dramatic, sharp and disagreeable.

12           The Chairman. Senator Symms wanted to speak on this,  
13 and then Senator Chafee.

14           Senator Symms. Mr. Chairman, I want to go on record as  
15 supporting this amendment. And I think Senator Armstrong and  
16 Senator Moynihan have made most of the points, but there is  
17 one point that hasn't been made. And that is if you disallow  
18 part of the deductions, who is it going to hurt?

19           It is going to hurt the small businessman that has to  
20 use travel, entertainment to make contact, business contacts,  
21 and sales. You take the big company like American Express or  
22 the Holiday Inns or somebody, they are just going to go on  
23 television with 100 percent deduction and deduct it all off,  
24 and pour a little more money into their television and radio  
25 advertising, newspaper advertising, and offset their loss in

1 business.

2 Yet the small company, the small businessman, may be  
3 in a position where they can't advertise because they have to  
4 do a rifle-shot contact of their customers. And I have seen  
5 this in a lot of my own experience.

6 I just think this is really, truly a very bad precedent  
7 to set with respect to business, not to mention the fact that  
8 in my state it is estimated it cost \$50 million in lost sales  
9 annually and 2,300 jobs of the people in the food and service-  
10 related industries.

11 So I think it is important from the standpoint of the  
12 impact on the eating, drinking, hotels, motels, commercial  
13 sports and entertainment in the state of Idaho. But also it  
14 is important for those small business people in Idaho that  
15 export products out of the state that have to entertain or to  
16 try to make contacts with their customers in the markets  
17 around the United States and are not big enough to actually  
18 go in and advertise.

19 And I just think that this amendment is important, and  
20 it should be accepted. And I hope the Committee will accept  
21 it. And I would not see it as upsetting the goal of what  
22 the Chairman has with his overall tax reform package.

23 The Chairman. Further discussion?

24 Senator Chafee. Mr. Chairman?

25 The Chairman. Wait a minute. I want to go back and

1 forth again. Senator Baucus, then Senator Chafee and then  
2 Senator Mitchell. And then Senator Heinz.

3 Senator Baucus?

4 Senator Baucus. I have a question I would like to direct  
5 to Senator Armstrong. And that is the degree to which the  
6 reduction in the corporate rate is calculated in trying to  
7 determine the economic result of the 80 percent --

8 Senator Armstrong. Max, I am having difficulty hearing  
9 you.

10 Senator Baucus. The point is this: I see lots of  
11 studies, and I think you passed out a sheet which tried to  
12 project the economic dislocations that would result as a  
13 consequence of the 80 percent limitation.

14 On the other hand, in this bill we are lowering the  
15 corporate rate to 33 percent. And I am wondering if there are  
16 any studies that show the economic benefit as a result of  
17 lowering the corporate rate to 33 percent in some of these  
18 establishes, you know, these restaurants and the entertainment  
19 facilities.

20 Have there been any studies run or has anybody tried to  
21 determine what the economic benefit would be by lowering the  
22 top rate to 33 percent?

23 Senator Armstrong. Mr. Chairman, I would have to say in  
24 response that there may be. I am not aware of them, if there  
25 are. And I am inherently cautious about the use of

1 econometric projections, although in this particular case it  
2 is such an obvious intuitively correct conclusion that while  
3 I would vouch for the magnitude of it -- in other words,  
4 Chase Econometrics says that the loss nationwide will be  
5 \$32 billion in sales. I don't know whether that is the right  
6 number. It could be off by half. It could be off by 100  
7 percent.

8 Senator Moynihan. But it is not your number.

9 Senator Armstrong. Oh, no, it is not my number. But,  
10 intuitively, I am sure that the principle it expresses is  
11 correct. Whether the correct number is actually \$20 billion  
12 or \$40 billion, I can't vouch for. And I am not aware of  
13 a study to support the question you have asked, although I  
14 think your point is correct that lowering the rate is going  
15 to be good for business. That is part of what we are  
16 attempting to do. And that may partially or perhaps  
17 conceivably totally offset the loss in this particular  
18 segment.

19 It doesn't sound to me like that would be the case  
20 because the way those two intersect at least intuitively it  
21 sounds to me like the loss would be much greater when you  
22 single out a particular expense and seek to treat it different  
23 than every other expense for exactly the reason that Senator  
24 Symms and others have pointed out. That it skews the business  
25 planning against this particular kind of expenditure and in

1 favor of all of the alternatives -- billboard, television,  
2 newspaper advertising and so on.

3 Senator Chafee. Mr. Chairman?

4 The Chairman. Senator Chafee, and then Senator Mitchell.  
5 Did you want to speak, too, John, or not?

6 Senator Heinz. Yes.

7 The Chairman. All right. I have got Senator Chafee,  
8 then Senator Mitchell, then Senator Heinz and then Senator  
9 Dole.

10 Senator Chafee. A quick question to Senator Armstrong.  
11 You mentioned the Australian experience. Two questions. Was  
12 that a 20 percent cut or was that an elimination? And,  
13 secondly, was it --

14 Senator Armstrong. It was elimination, Senator Chafee.

15 Senator Chafee. Well, I think to cite that as an example  
16 when you eliminated it as opposed to reducing it by 20  
17 percent isn't exactly a fair comparison.

18 Secondly, I just suspect that it was not accompanied by  
19 a cut in the corporate rate at the same time. Is that  
20 accurate?

21 Senator Armstrong. Fair enough. However, you can draw  
22 your own conclusion about that, but I don't think that is an  
23 unlikely or an unbecoming comparison. In fact, if anything,  
24 it is within the realm of possibility that the result of a  
25 20 percent disallowance would be identical to or conceivably



1 even more severe than eliminating it altogether simply because  
2 it has a discriminatory effect. But that is a judgment, and  
3 your point is well taken that it is not an identical fact  
4 situation.

5 I only cite Australian experience to buttress  
6 projections that have been made of what might happen here by  
7 Chase Econometrics.

8 Senator Chafee. Well, I just think that the projections,  
9 first of all -- and I don't agree with you that it is a  
10 logical comparison -- 20 percent versus the total elimination  
11 without being accompanied by a drop in the corporate rate, as  
12 we are doing here.

13 But there is a matter of equity discussed here. And if  
14 there is ever a group that I don't feel great sympathy for,  
15 it is the people that are going out and having the advantage  
16 of this, whether you call it a three-martini lunch or getting  
17 the best seats at the hockey game or wherever it is. This  
18 isn't a fellow from the assembly line that is getting this  
19 advantage. This is the people up in the executive suites.

20 And I don't think we have to weep over them. And I don't  
21 believe that the effect on the entertainment or the food and  
22 liquor industry is going to be anything near suggested. I  
23 personally don't have that belief whatsoever. It is 80  
24 percent. Is anybody not going to go out to lunch because  
25 they might have to pay a portion of it? I suspect not.

1           And I applaud the action that was originally taken and  
2 think that the amendment is not a good one.

3           Senator Symms. Senator, would you yield for a question  
4 on that?

5           Senator Chafee. Sure.

6           Senator Symms. What about the commission salesman? We  
7 hear about the guy that has the high-priced suite at the  
8 hockey game. But what about the commission salesman that  
9 works in Rhode Island that has to pay all of his own expenses  
10 as he is on the road working to make a living?

11           I mean you are going to disallow 20 percent of his cost  
12 of doing business. So what will he do? Go back to the  
13 parent company and try to get them to pick up more of it,  
14 and pay him less?

15           I mean it is just a complication. There will be ways  
16 to figure out how to get around it.

17           And then the other person is -- what about the waitress  
18 that works at the restaurant? Instead of worrying about the  
19 other part, what about all those people that do work? I am  
20 concerned about those people that work in the restaurants  
21 in Idaho, and I know you are concerned about them in North  
22 Dakota and Rhode Island.

23           Senator Chafee. I know I am too. And we are an  
24 entertaining state. But I would get back to the original point  
25 that long before there were income taxes, people were going

1 out to have meals. It isn't the deductibility of something  
2 that makes it attractive.

3 And when we get the rates down this low, as we are  
4 doing -- and that is the whole thrust of this -- people will  
5 make their own decisions. So I don't subscribe to the dire  
6 predictions.

7 The Chairman. Senator Mitchell.

8 Senator Mitchell. Mr. Chairman, I will vote against  
9 this amendment. I believe both the amendment and the  
10 proposal in the bill are deficient because they don't deal  
11 with what I think is the only problem in this area, and that  
12 is the abuses of entertainment and meals.

13 And, unfortunately, the 80 percent rule doesn't do  
14 anything about that. It penalizes the legitimate use as  
15 well as the improper use.

16 The President originally proposed a cap which would have  
17 permitted the responsible use of this provision and  
18 eliminated the abuses. Unfortunately, the Administration  
19 reversed itself half way through the procedure, and now  
20 supports the 80 percent rule.

21 It is my hope that the Administration will reconsider  
22 its position. Having reversed itself once, it is not beyond  
23 expectation that it might reverse itself again.

24 Because I believe that either one, either this amendment  
25 or the proposal in the bill, doesn't deal with what is the

1 singular problem in this area.

2 The Chairman! Senator Heinz, then Senator Dole and then  
3 Senator Grassley.

4 Senator Heinz. Mr. Chairman, I am not going to get into  
5 an argument with anybody on this for the reason that I will  
6 not be voting on this amendment, even though were I to vote  
7 I must confess I am somewhat biased in favor of the amendment.  
8 I am biased because, as I said earlier, I don't really like  
9 the notion of partial deductibility for anything. I just  
10 think it is a bad tax policy, and I had that discussion with  
11 my friend, Pat Moynihan, a moment ago on his amendment.

12 I would confess also there is some parochial concern  
13 in my home state of Pennsylvania that this would amount to  
14 a seven percent excise tax on a lot of businesses that don't  
15 cater to wealthy executives.

16 I would be the first to say that I think there are some  
17 compliance problems here. And while none of us ever get a  
18 chance to get off the Hill and see what goes on at the Le  
19 Cavenon Restaurant down here, I suspect people are getting  
20 ready to go down there and have a \$200.00 or \$300.00 lunch  
21 per person, and it kind of strikes a raw bone if it is  
22 deducted --

23 Senator Bentsen. Maybe they will just eat 80 percent of  
24 it.

25 Senator Heinz. Yes. If it is all deducted as a

1 legitimate business expense and people don't even talk  
2 business. They are too busy ordering from the long list of  
3 nouvelle cuisine items there.

4 But having said all that, under the Senate rules, this  
5 is an amendment that clearly does have an impact on food and  
6 food service organizations for obvious and apparent reasons.  
7 Were I to vote, it would pose a conflict of interest for me,  
8 and so I will withhold my vote, and will be voting present.

9 The Chairman. Senator Dole, then Senator Grassley, and  
10 then if Senator Armstrong wants to close, I think we would  
11 be ready to vote. Senator Moynihan also.

12 Senator Dole. Mr. Chairman, I appreciate that. We  
13 had some experience with this section in 1982, and it seems  
14 to me that by the time we get to the Senate floor there may  
15 be a better idea because I agree with Senator Mitchell that  
16 here we are not going after the abuses. We are just saying  
17 everybody takes 20 percent.

18 I will have an amendment later on that will permit to  
19 expense legitimate banquet or reception as part of a formal  
20 business meeting. Now we are trying to get the cost on that.  
21 I presume there would be some instances where you could find  
22 some abuses there.

23 But it would seem to me where you have a business  
24 meeting and you have a speaker, maybe even a member of the  
25 Senate --

1 (Laughter)

2 Senator Dole.-- with an honorarium, of course, we have  
3 locked that in.

4 (Laughter)

5 Senator Dole. But it might be a legitimate business  
6 expense and one that should be addressed. And we have  
7 asked the Joint Committee to give us some estimates. We think  
8 they are a little high, but we will keep working on it.

9 The Chairman. Senator Grassley, then Senator Moynihan.  
10 Senator Grassley. Mr. Chairman, I have a question to  
11 you or to staff. What is the justification for the 80  
12 percent for the individual reimbursement on the individual  
13 deductions? If that same individual were working for a  
14 corporation, it is my understanding that he could be  
15 reimbursed by the corporation 100 percent for the expenses,  
16 and the corporation would be able to deduct that as a business  
17 expense 100 percent. Is that true?

18 The Chairman. Mr. Brockway, did you hear Senator  
19 Grassley's question? He wants to know if an individual works  
20 for a business, the individual entertains somebody, and the  
21 business reimburses the individual, can the business  
22 reimburse the individual 100 percent for the cost of the meal  
23 under this, although the individual if taken the deduction  
24 themselves could not?

25 Mr. Brockway. Yes. The reimbursement is not taxable

1 to the individual but at the corporate level is where the  
2 disallowance occurs so the corporation deducts only 80  
3 percent of the reimbursement.

4 The Chairman. All right.

5 Senator Armstrong. Unless he is given a salary, Mr.  
6 Brockway.

7 The Chairman. But I think Senator Grassley's question  
8 was straight out. Could the corporation reimburse him 100  
9 percent? No, cannot. Is that correct? If the employee sends  
10 a voucher and says I took these four people out, here is a  
11 bill for \$100.00, the corporation might be able to reimburse  
12 the individual who works for the corporation 100, but they  
13 could only take \$80.00 of it as a deduction.

14 Senator Symms. Could I ask one more question on that?  
15 It is on the same subject.

16 The Chairman. All right.

17 Senator Symms. How about if a Senator or Congressman  
18 goes to their state or district and come back and turn in  
19 their expenses to the Clerk of the Senate or the House and get  
20 paid, so then they have to pay taxes on the other 20 percent?

21 Mr. Brockway. No. A reimbursed expense is simply not  
22 included in the employee's income under the proposal. The  
23 disallowance happens at the payer level. It is like any other  
24 fringe benefit, in effect.

25 The Chairman. Senator Moynihan.

1 Senator Symms. The government is treated different than  
2 the corporation, then.

3 Senator Grassley. Yes.

4 The Chairman. Senator Moynihan and then Senator Long.

5 Senator Moynihan. May I take my friend, Senator Heinz, --  
6 the point he has made about the proportional deductions.

7 Proportionality is the first principle of the income tax.

8 It is really not an alien idea at all.

9 The Chairman. Senator Long.

10 Senator Long. Mr. Chairman, if you are going to cut  
11 this, let's say you are going to cut it by 20 percent, I  
12 would think that that is the entering wedge to cut it  
13 eventually by 100 percent to say you just can't deduct this  
14 item. And that is how I would view this.

15 And if that is going to be done, I really don't think any  
16 further study of it would indicate that you can have all the  
17 different -- I am talking about legitimate restaurants often  
18 times are the best restaurant in the community -- they stay  
19 open. I think a lot of them would just have to close. And  
20 that means we will lose a lot of jobs.

21 Now I think the fair way to pay for it -- well, the  
22 corporate tax is a fair way, but it would be even more fair  
23 to say let's raise that tax up to 27-1/2 percent as Senator  
24 Durenberger suggested so that the people, the upper 20  
25 percent, pick up the tab for it, they pay the burden of it.



1           And generally speaking, those are the people who are  
2 both doing the entertaining and being entertained. So on  
3 that basis, they get the benefit of it in that group, and  
4 they pay the burden of it.

5           Now what does this mean just for the ordinary fellow  
6 down there that doesn't pay any 20 percent? It wouldn't cost  
7 him anything one way or the other if you did it that way.

8           Well, for a lot of those people what it means if they  
9 only had one -- in the ordinary sized community, they only  
10 had about one nice restaurant around town where they would  
11 take mother out on the anniversary or her birthday or  
12 something like that, only about once a year, and the rest is  
13 gone. So that restaurant can't stay open entertaining mothers  
14 on their anniversary, or their birthday. It has to have some  
15 regular business that comes in there day in and day out.

16           And the loss of business that this would bring about,  
17 they no longer have the restaurant. Now if you look at that  
18 from the point of the view of the fellow who is only going  
19 to go there once a year, he has lost something. And if you  
20 paid for it the way I would like to see it paid for, it  
21 doesn't cost him anything for him to be there.

22           So I am going to vote with Senator Armstrong on this. I  
23 definitely think that entertainment is a legitimate cost of  
24 operation. I said many times that entertainment is the  
25 selling business, the same thing that fertilizer is for the

1 farming business.

2 (Laughter)

3 Senator Long. You just see how farmers would make out  
4 operating without fertilizer. He doesn't do very well. And  
5 they certainly couldn't do very well without entertainment.

6 Senator Durenberger. Mr. Chairman?

7 The Chairman. Senator Durenberger.

8 Senator Durenberger. I will be brief.

9 I have a small conflict compared to John Heinz's. I have  
10 a son who is a busboy --

11 (Laughter)

12 Senator Durenberger. -- and I found it relatively easy  
13 to resolve my conflicts in favor of my busboy son.

14 But I just got handed a note here from a Minnesota  
15 company that was lobbying for this amendment. I mean it  
16 was lobbying for 100 percent deductibility, but it says they  
17 do not support this amendment because they prefer the one  
18 percent higher rate, which just illustrates, I think, the  
19 difficulty that -- they prefer the lower rate. The difficulty  
20 of deciding this really on its merits.

21 I've never approached either this or Bill Bradley's  
22 automobile amendment last year on the basis of subsidies  
23 for General Motors or subsidies for the restaurant industry.  
24 I am sure if we wanted to have 2.6 million restaurants in  
25 America, we would find a more efficient subsidy than the

1 business lunch to do it.

2 But particularly with the track that we are on with the  
3 lower rate, I search for principle. And I guess my principle  
4 is that in making policy here at the federal level when we  
5 have less than one-third of a stake in the decision, we  
6 shouldn't try to determine what is deductible and what is  
7 not when someone else has to make the decision to make the  
8 actual investment.

9 So until I become persuaded that we ought to eliminate  
10 this sort of deduction entirely, I will support the amendment  
11 which does away with partial deduction.

12 The Chairman. Senator Moynihan -- excuse me, Senator  
13 Bentsen, and then we will vote.

14 Senator Bentsen. Well, Mr. Chairman, I just wanted to  
15 comment that I have neither John Heinz's problem or Dave  
16 Durenberger's problem. And since I rarely pick up the  
17 check, I can be totally objective and vote for it.

18 (Laughter)

19 The Chairman. I don't think we will top that all day  
20 today.

21 (Laughter)

22 The Chairman. All those in favor of the Armstrong-  
23 Moynihan amendment will say aye?

24 (Chorus of ayes)

25 The Chairman. No, no, no. The Clerk is going to call

1 the roll.

2 Clerk, call the roll.

3 The Clerk. Mr. Dole?

4 The Chairman. No.

5 The Clerk. Mr. Roth?

6 Senator Roth. No.

7 The Clerk. Mr. Danforth?

8 Senator Danforth. No.

9 The Clerk. Mr. Chafee?

10 Senator Chafee. No.

11 The Clerk. Mr. Heinz?

12 Senator Heinz. Present.

13 The Clerk. Mr. Wallop?

14 Senator Wallop. No.

15 The Clerk. Mr. Durenberger?

16 Senator Durenberger. Aye.

17 The Clerk. Mr. Armstrong?

18 Senator Armstrong. Aye.

19 The Clerk. Mr. Symms?

20 Senator Symms. Aye.

21 The Clerk. Mr. Grassley?

22 Senator Grassley. No.

23 The Clerk. Mr. Long?

24 Senator Long. Aye.

25 The Clerk. Mr. Bentsen?

1 Senator Bentsen. Aye.  
2 The Clerk. Mr. Matsunaga?  
3 Senator Moynihan. Aye, by proxy.  
4 The Clerk. Mr. Moynihan?  
5 Senator Moynihan. Aye.  
6 The Clerk. Mr. Baucus?  
7 Senator Baucus. No.  
8 The Clerk. Mr. Boren?  
9 (No response)  
10 The Clerk. Mr. Bradley?  
11 Senator Bradley. No.  
12 The Clerk. Mr. Mitchell?  
13 Senator Mitchell. No.  
14 The Clerk. Mr. Pryor?  
15 Senator Pryor. Aye.  
16 The Clerk. Mr. Chairman?  
17 The Chairman. No.  
18 Senator Grassley. Mr. Chairman?  
19 The Chairman. Senator Grassley.  
20 Senator Grassley. I'd like to vote yea.  
21 The Clerk. Nine yeas, nine nays.  
22 The Chairman. The amendment is defeated.  
23 Are there further amendments to the bill?  
24 (No response)  
25 The Chairman. If no further amendments --

1 (Laughter)

2 The Chairman. Senator Heinz and then Senator Roth.

3 Senator Heinz. Mr. Chairman, I would like the staff to  
4 pass out my proposal on the corporate rate and minimum tax.

5 I think most members are familiar with this amendment.  
6 Let me briefly describe it and the rationale for it.

7 The problem -- Mr. Chairman, could we have order?

8 The Chairman. Let me doubly request order because this  
9 amendment is a particular -- I don't want to say any of the  
10 others were not, but this is a particularly important and  
11 philosophical amendment as among industries. And I think  
12 the Committee should play close attention to the proposal.

13 Senator Heinz. Mr. Chairman, in the legislation we have  
14 before us, we have a very stiff minimum tax. It is at 20  
15 percent. It is collected two different ways; first, on  
16 tax preference items and then on book incomes. It is, at  
17 least where corporations are concerned, an airtight minimum  
18 tax. And I think all of us believe it is very important to  
19 have a minimum tax where corporations that are earning money  
20 pay their fair share of taxes. At least, I speak, I think,  
21 for a good -- the majority of the Committee on that  
22 proposition.

23 Secondly, in an effort to try and make sure that capital  
24 intensive industries, because we are repealing the investment  
25 tax credit, are able to recover their costs in a relatively

1 short space of time, have given an accelerated depreciation,  
2 specifically 200 percent declining balance method with ACRS  
3 lives, for most investments in equipment.

4 The minimum tax that is part of the Chairman's proposal  
5 counts as tax preference income and subject therefore that  
6 tax preference to the 20 percent minimum tax. The difference  
7 between to that 200 percent declining balance method of  
8 depreciation over and above the depreciation that would be  
9 claimed under straight line ADR mid-point lives, which in  
10 most cases is very different and much longer than the ACRS  
11 lives.

12 The result of that change is that many businesses,  
13 farms, small businesses, marginally profitable businesses,  
14 capital intensive businesses, that are marginally profitable  
15 will pay a substantial minimum tax even though by any common  
16 sense definition they are not making any substantial amount  
17 of money.

18 It is my view that it is important that any corporation  
19 that is generating economic income and is profitable should  
20 pay its fair share. But it makes no sense to me to force  
21 corporations that are not making money, that do have to make  
22 capital investments to stay alive, to force them to pay an  
23 unfairly high minimum tax.

24 So my amendment makes the following changes: It would  
25 consider as a preference item that depreciation that is above

1 ACRS straight line, which would obviously catch any  
2 depreciation at 200 percent ACRS lives.

3 Secondly, it would allow the investment tax credit  
4 discounted at 70 percent to be allowed to offset up to 70  
5 percent of subsequent year minimum tax liability.

6 The amendment would be paid for by raising the regular  
7 corporate tax rate, which in this bill is 33 percent, by the  
8 amount necessary to pay for those first two changes.

9 Now according to the estimates I have received from  
10 the Joint Tax Committee, the first two parts of my amendment  
11 would cost in the neighborhood of \$6-1/2 to \$7 billion. That  
12 is less than raising the corporate tax rate a full percentage  
13 point.

14 And since the objective of my amendment is to be revenue  
15 neutral, no more, no less, my best guess is we are talking  
16 about an approximately three-quarter percent increase in the  
17 corporate tax rates.

18 Would that be correct, Dave?

19 Mr. Brockway. It should be in the neighborhood of  
20 three-quarters of one percent. It is going to be in that  
21 neighborhood if we just had the leeway to adjust it. Let's  
22 say if you had to go up to eight-tenths of a percent or down  
23 to seven-tenths of a percent, that we can obviously set it.  
24 It will be in that table.

25 Senator Heinz. I think the bottom line, Mr. Chairman, is



1 this will be somewhat less. I can't quite say substantially  
2 less, but it will be significantly less than a full percentage  
3 point increase in the corporate rate.

4 And I think the judgment the Committee has to make is  
5 whether it makes sense to tax marginally profitable enter-  
6 prises that really aren't making much in the way of money  
7 through the minimum tax.

8 Those businesses tend to be, as a matter of statistical  
9 facts, farms -- farms are not making a lot of money, with  
10 Senate Symms reminding me of this every day. They tend to be  
11 small businesses. Small businesses tend to be less  
12 profitable, and they tend to be the more capital intensive  
13 industries, which seem to be the ones that are subjected to  
14 the most foreign competition.

15 One other point I would like to make and that is that  
16 I have been assured by staff that this amendment will not  
17 relieve, the way it is drafted, it will not relieve anybody  
18 from paying something in the way of a minimum tax.

19 Mr. Brockway. That is correct, Senator Heinz. This  
20 gives a benefit to circumstances where the taxpayers are on  
21 the minimum tax because of the treatment of depreciation, and  
22 the minimum tax being straight line over ADR lives.

23 But since it doesn't affect the book preference -- that  
24 is, as long as they have book income, they would definitely  
25 remain subject to the minimum tax under the proposal.

1           Senator Heinz. So if anybody is worried, Mr. Chairmann  
2 that this is going to let people out of the minimum tax, it  
3 will not.

4           Senator Bentsen. Le me ask a question.

5           The Chairman. Senator Bentsen.

6           Senator Bentsen. My question has been answered since  
7 then. Thank you.

8           Senator Symms. Mr. Chairman?

9           Senator Heinz. Mr. Chairman, I would just make one other  
10 point and then I will yield the floor.

11          Senator Symms. I want to ask a question, Senator Heinz.

12          Senator Heinz. Oh.

13          Senator Symms. Senator, I support your amendment, first,  
14 but I want to make a point to the Committee that mining in  
15 this country is, as we all know, under a lot of stress. And  
16 I think in your amendment that I would just like to offer an  
17 amendment, if the Senator would accept it, that exploration  
18 and development costs would not be considered a preference  
19 item.

20          Now the mines in my state are under a lot of pressure  
21 from foreign imports from countries, non-market countries,  
22 that have nationalized the mines and have used almost slave  
23 labor in many cases to mine those minerals and to put them  
24 under more preference. And if these exploration and  
25 developments costs, which are the front end costs tied to a

1 new mine and for new jobs in the United States -- I don't  
2 know what that would cost, but I would venture to say it is  
3 a very minimal impact. Mr. Brockway?

4 Mr. Brockway. I believe it is less than \$100 million.  
5 Senator Symms. Somebody told me it was less than 50.

6 Mr. Brockway. It could well be.

7 Senator Symms. I have seen it less than 50, I think.  
8 But you would agree it is a low cost?

9 Mr. Brockway. Correct.

10 Senator Symms. I just wonder if the Senator would be  
11 amenable to an amendment that would say that exploration and  
12 development costs in mines be not considered a preference  
13 item.

14 Senator Heinz. Senator, let me ask the staff one other  
15 question.

16 I am sympathetic to Senator Symms' amendment under two  
17 conditions. One, that it not cost any significant amount of  
18 money. And you are saying it is \$50 million or less, you  
19 think.

20 And, secondly, that it won't result in anybody not  
21 paying their --

22 Mr. Brockway. The only area where that would happen,  
23 Senator Heinz -- since, again, I would interpret this not to  
24 affect the individual who was actively in the business.

25 If you did it just for corporations, I could give you

1 the answer without any hedging whatsoever.

2 Senator Heinz. Would the Senator be willing to  
3 constrain that just to corporations?

4 The Chairman. Further comments? Oh, I am sorry.

5 Senator Heinz. Mr. Chairman, I withdraw my question.  
6 But I just want to go back to what you are saying that there  
7 isn't going to be a corporate --

8 Mr. Brockway. Corporate level because this would not  
9 affect the book preference.

10 Senator Heinz. Mr. Chairman, I personally would be  
11 willing to accept Senator Symms' amendment.

12 Senator Symms. I am not certain there are many mines  
13 going on that aren't corporate entities. I would have to  
14 check on that.

15 Senator Heinz. That is all right. I will accept the  
16 amendment as you have stated it, Senator.

17 Senator Symms. All right, thank you.

18 Senator Heinz. Mr. Chairman, I just want to make one  
19 last point. It is important to realize that depreciation is  
20 not now a tax preference item under the minimum tax, under  
21 current law. So by making -- going to the Committee draft or  
22 adopting the House amendment, we are nonetheless making a  
23 very significant change in subjecting a portion of  
24 depreciation to the minimum tax.

25 (CONTINUED ON NEXT PAGE)

1           Senator Heinz. We have never done that before, and I  
2 must say I even have some reservations about doing that,  
3 coming from a state with a lot of capital-intensive  
4 industries. But I have tried to be reasonable and not  
5 overreach in this amendment, and I hope the committee will  
6 support it.

7           The Chairman. Bill Armstrong, and then Senator Bradley.

8           Senator Armstrong. Mr. Chairman, I just want to  
9 compliment Senator Heinz. I think he has been very sports-  
10 manlike on this.

11          The Chairman. Senator Bradley?

12          Senator Bradley. Mr. Chairman, I will have to say I  
13 oppose the amendment. I think we ought to think about what  
14 this amendment really does.

15          This is a proposal to raise the overall corporate rate  
16 by about a point. Now, if you raise the overall corporate  
17 rate by a point to pay for this kind of investment tax credit  
18 and depreciation proposal, you are raising the overall cost  
19 of capital. You are raising the overall cost of capital on  
20 the whole economy, so that you can take care of a smaller  
21 segment of that economy.

22          The other part that concerns me is that you are saying  
23 that, for this segment of the economy, their minimum tax  
24 rate would be about six percent; whereas, for all the other  
25 companies, that minimum tax rate would be 20 percent.

1           So, Mr. Chairman, I think that this is probably going to  
2 be the first of a number of amendments that will be offered,  
3 all of which will go to raising the corporate rate, thinking  
4 that that is the pool of money that everybody has to pay for  
5 whatever they want to do. It is not free. You raise the  
6 corporate rate, you increase the overall cost of capital.

7           I think, based on that reason as well as capping the  
8 minimum tax at six percent, I would oppose this amendment.

9           The Chairman. Mr. Secretary?

10          Secretary Mentz. Thank you, Mr. Chairman.

11          I think Senator Bradley has correctly characterized the  
12 choice that you must make on this amendment. I think it can  
13 be looked as, on the one hand, slightly loosening the  
14 minimum tax, and on the other hand slightly increasing the  
15 corporate rate.

16          The bothersome feature from Treasury's standpoint on the  
17 minimum tax is that, because of the investment credit  
18 feature, it would be possible for some of the well-known  
19 corporations in America that are very profitable on the  
20 book-income basis to pay perhaps some minimum tax, but much  
21 less than would be under the Chairman's proposal. And that  
22 is because you have an investment credit offset.

23          The other point I just want to emphasize is that lower  
24 rate, the 33-percent rate, is really a very significant plus  
25 to the Chairman's package. And I think, once you start

1 eroding it with this amendment or any other, you are simply  
2 not going to end up with nearly as an attractive package as  
3 you have right now.

4 Senator Heinz. Mr. Chairman?

5 The Chairman. Senator Heinz?

6 Senator Heinz. I think there may be a way to solve a  
7 problem here for Senator Bradley and others.

8 Within a relatively modest timeframe, investment tax  
9 credits will have all been used up, or will have expired --  
10 they will be gone.

11 At that point, what is now the front-end cost of this  
12 amendment will drop substantially. I would like to see, with  
13 the utilization of those investment tax credits, which we  
14 are in any event discounting to begin with at 70 percent, in  
15 order to take into account the difference in corporate rates,  
16 going from 46 to 33, and which can only be partially used in  
17 any tax year to offset a portion of the minimum tax, what I  
18 would like to write into the amendment is the proposition that  
19 the corporate tax rate drop when there are no more investment  
20 tax credits to be used up. And I would anticipate it would  
21 drop very close to 33 percent.

22 Mr. Brockway. Well, unfortunately, when you are looking  
23 at trying to make sure that this is revenue-neutral on a  
24 long-run basis, in fact I don't think that is the major piece  
25 of it. The way the minimum tax works, one reason why the

1 book preference is such an important element of the tax  
2 component here, the revenue component, is that essentially  
3 that is picking up revenue for book profits of the next five  
4 years. That is book profits that are derived from existing  
5 investments. So, there would be a lot of situations where  
6 you are going to pick up revenue in the window. From the  
7 depreciation preference, it is something that only applies  
8 under the Chairman's marked new investment.

9 So, on the long-run basis, the amendment as such will  
10 end up losing money. In the window it will be revenue neutral.  
11 So, you can take that one piece --

12 Senator Heinz. Well now, I am talking about, though, the  
13 investment tax credit, which clearly, five years from now,  
14 there shouldn't be any unused investment tax credits left.

15 Mr. Brockway. Well, it will be more than five years.

16 Senator Heinz. How long do we think it will be?

17 Mr. Brockway. For some taxpayers it will be up to 15  
18 years. There are a number of taxpayers who find themselves  
19 in a situation where they do not expect really to be on the  
20 regular tax for a substantial period into the future. In  
21 fact, that is one reason why there has been interest in the  
22 ITC cash-out proposals, because they wouldn't see themselves  
23 using the ITC certainly in the next five years, and even out  
24 into the future.

25 Senator Heinz. Then, let me withdraw my proposal, or



1 the last part of it -- not the entire amendment.

2 I had suggested that there might be a way to drop the  
3 corporate rate after several years, because the investment  
4 tax credits should be used up. It turns out, my assumption  
5 about the rapidity of use of the investment tax credits was  
6 flawed. Therefore, I just revert to the amendment which is  
7 before you, including the Symms modification.

8 Senator Pryor. Mr. Chairman, a question, if I might.

9 The Chairman. Senator Pryor.

10 Senator Pryor. Mr. Brockway, how many companies might  
11 be affected? Let's say if we took 30 companies now that we  
12 see on our list all the time that pay no income taxes. How  
13 many companies on that list would be affected favorably by  
14 Senator Heinz's amendment, if they can apply this against the  
15 proposed corporate minimum tax?

16 Mr. Brockway. I think it is a working assumption,  
17 Senator, that you will have a great number of the corporations  
18 that have significant reported profits, book profits, and no  
19 taxable profits, will find themselves coming on the tax  
20 rolls first through the minimum tax. And if they are coming  
21 through on the minimum tax, and the reason they re there is  
22 because essentially of the book preference, that effectively  
23 is a tax rate of 10 percent on their book profits.

24 Then, they would be allowed a minimum tax to offset  
25 seven out of that 10; so, they have an effective rate of

1 three percent on this income, if I am doing my calculations  
2 correctly.

3 And I would assume that the corporations you are talking  
4 about would be -- that would be the characterization. They  
5 would start coming on the tax rolls on the minimum tax  
6 rather than on the regular tax. So, many of those corpor-  
7 ations -- I don't have a breakup, but I think a great number  
8 of those corporations would be benefitted by this proposal.

9 Senator Pryor. But if we allow the Heinz amendment to  
10 go into effect, if we would support it, for example, would we  
11 not see a perpetuation of many of the major corporations of  
12 America who are making massive profits, like some of our  
13 major defense contractors for example -- General Dynamics, to  
14 name one -- using their unused investment tax credit against  
15 the minimum corporate tax; therefore, once again paying no  
16 taxes?

17 I think we are unraveling the equity of a system we  
18 are trying to build in here. Maybe I am wrong.

19 Mr. Brockway. Without trying to split hairs, they would  
20 not, under this amendment, go down to a zero tax. I think if  
21 the reason they are there is because of the book profits, they  
22 essentially would be paying a three-percent tax, which would  
23 be a 10 percent tax because of the book profits, and then  
24 they would be allowed an investment credit to offset seven.  
25 So, they would not be paying tax, but it would only be at

1 a three-percent rate.

2 Senator Pryor. Now, you stated a moment ago, I believe,  
3 that there are approximately 15 years left in some of the  
4 unused investment tax accounts for some of the major  
5 corporations. Is that, about 15 years, a pretty good figure,  
6 do you think?

7 Mr. Brockway. That is the maximum it would be. On some  
8 of them, it might be shorter. It will be shorter for others.  
9 That is a limitation on carryover. So, in other words, if  
10 your credits were generated this year or last year, you would  
11 have 15 more years. But it could be up to 15.

12 Senator Heinz. David, would you yield for a question?

13 Senator Pryor. I would be glad to yield. I am just  
14 trying to find out what this does.

15 Senator Heinz. I understand you are.

16 Senator Pryor. I think you know what I am concerned  
17 about.

18 Senator Heinz. I do. And here is the problem that I  
19 think we have:

20 The way the minimum tax is written in this bill, you are  
21 virtually in it forever; you can't get out of it. As a  
22 result, what happens is, if you made some investments in 1979  
23 or 1980 or 1981, or right up on til this year, and you did it  
24 in part so you could get an investment tax credit, but your  
25 profitability was such that you couldn't take any advantage

1 of that investment tax credit, the practical effect of  
2 leaving out the second part of my amendment is that those tax-  
3 payers will never be able to claim any portion of their  
4 investment tax credits.

5 In effect, it is retroactive taxation on people who made  
6 investments as far back as 1979, if they haven't already been  
7 able to use their investment tax credits. That is the issue.

8 It seems to me the committee can make the choice, "Look,  
9 if you made an investment in 1981 and you haven't used your  
10 investment tax credit since then, fine, too bad. You know,  
11 we won't let you use 70 percent of it, even if under the  
12 Heinz amendment it is going to take you several years to use  
13 it all up. We just don't want you to use any of it up."  
14 I think that is a decision the committee is entitled to make.

15 I don't think that is good policy, and that is the other  
16 side of the coin that you were flipping.

17 Senator Pryor. I would just like to respond by saying I  
18 think that Senator Packwood and the committee made real  
19 progress in trying to achieve equity and some real, real  
20 fairness in this whole tax situation. And I just think we  
21 are retreating on this one. I may be entirely wrong, but I  
22 feel like this is a retreat from that equity that we are  
23 trying to find. That is my only comment.

24 The Chairman. Senator Boren, then Senator Bradley, then  
25 Senator Baucus.

1 Senator Boren. Mr. Chairman, I want to support what  
2 Senator Heinz is trying to do in this situation. I think that  
3 he is right in terms of us not changing tax policy here to the  
4 point where people are going to lose incentives that they  
5 acted upon.

6 I think particularly, and I think I am correct -- I would  
7 ask the Senator from Pennsylvania -- would this not have  
8 potentially a rather large impact on farmers, who are in such  
9 a desperate economic shape, and will now be able under this  
10 provision to at least salvage a portion of the investment  
11 tax credit that they hoped to receive? They would be covered,  
12 would they not?

13 Senator Heinz. The answer to the Senator is Yes.  
14 Anybody who had been marginally profitable or unprofitable  
15 will benefit in future years from this amendment. And without  
16 it, they won't.

17 Senator Boren. Well, we have struggled in the Agricul-  
18 ture Committee I would say unsuccessfully to come up with  
19 programs to try to keep our family farmers in business. I  
20 compliment the Senator from Pennsylvania; I think this is  
21 something that might be of real benefit.

22 I have talked to several of the family farm organizations  
23 in our state, and they tell me that it would do as much as  
24 anything they could think of right now to keep more farmers  
25 from being forced into foreclosures.

1 I also think the Senator is right -- we have struggled,  
2 we have talked around this committee table so many times  
3 about the cost of capital, and about the need to keep the  
4 cost of capital down so that we can compete in the world  
5 marketplace.

6 We have done a lot. The Chairman has moved to improve  
7 the depreciation schedule, and I commend him for that. The  
8 only problem is that we have made those improvements by the  
9 way that the minimum tax is now written. The more we have  
10 improved depreciation, the more we have made it a preference  
11 item, by definition under the minimum tax, and have the effect  
12 of taking away with one hand the additions that we are making  
13 to the depreciation with the other.

14 I think that by the kind of proposal that the Senator  
15 from Pennsylvania is making, we are going to more effectively  
16 carry out the intent of the committee, in terms of encouraging  
17 capital formation, the same intent we had when we changed  
18 the depreciation schedule; while we will still, with the  
19 book value provision, make sure that there are not companies  
20 that get off. Many of us feel strongly about it -- I do --  
21 that we should not have companies making immense profits and  
22 paying no taxes at all.

23 But I don't think that will result under the amendment  
24 of the Senator from Pennsylvania; I think that protection is  
25 still built-in. But there are a number of those that deserve

1 to have an opportunity to take advantage of it that will be.

2 I think we will still be able to catch those that are  
3 getting by with paying no tax at all.

4 The Chairman. Senator Bradley, then Senator Baucus,  
5 then Senator Chafee.

6 Senator Bradley. Thank you very much, Mr. Chairman.

7 After I heard Mr. Brockway's response to Senator Pryor's  
8 question, what really troubles me is that it appears that for  
9 some of the nation's major profitable companies, like  
10 General Dynamics, that the effect of this amendment will be  
11 to reduce the minimum tax from about 20 percent to about  
12 three percent. I thought it was six percent. But it might  
13 even be below that.

14 I don't think this committee wants to do that, or it  
15 shouldn't want to do that. And the way we are going to pay  
16 for this benefit that we are going to give to these companies  
17 is to raise the overall corporate tax rate, which has the  
18 effect not of decreasing the cost of capital but increasing  
19 the cost of capital.

20 So, Mr. Chairman, again, I think that the important  
21 point here, in addition to the cost-of-capital question, is  
22 that the minimum tax rate for some of our major corporations  
23 who pay no tax would be reduced from 20 percent to three  
24 percent. I mean, that is what this vote is, I think.

25 The Chairman. Senator Baucus?

1 Senator Baucus. Mr. Chairman, I wonder if I could  
2 direct a question to Secretary Mentz?

3 As I understand it, the Treasury is generally opposed to  
4 the Heinz amendment. I would like to ask the Secretary the  
5 degree to which Treasury is opposed to the depreciation  
6 preference provision -- that is, part one.

7 The Chairman. Excuse me -- I can't quite hear you, Max.

8 Senator Baucus. Secretary Mentz, the question is the  
9 degree to which Treasury opposes Section One of the Heinz  
10 amendment, as opposed to Section Two of the Heinz amendment.  
11 Is the Treasury equally opposed to both, or more opposed to  
12 one compared to the other?

13 Secretary Mentz. Well, as I tried to frame my answer  
14 following Senator Bradley, both portions are slight  
15 looseners of the minimum tax. The trade-off is the higher  
16 rate.

17 Treasury is opposed to both. If you are asking for a  
18 weighting, I suppose I would weight it a little heavier on  
19 the investment credit, because that does provide the ability  
20 to get down to three percent, which seems to me to be wrong.

21 But to speak to the other part of the proposal, which  
22 hasn't been discussed very much, under current law we do have  
23 a slightly extended period to measure the acceleration versus  
24 some sort of economic depreciation. That is the basis on  
25 which tax preferences are determined under the current



1 alternative minimum tax, and that is the basis of the  
2 Chairman's proposal.

3 I think Treasury's view is that some measure of economic  
4 life rather than ACRS life is the appropriate life to use.

5 Senator Baucus. If I can follow up on that, I understand  
6 that Treasury is working up some study to reevaluate, to  
7 redetermine, the actual economic lives for various assets.

8 The question is, is that correct? Is my statement  
9 correct? And, second, if so, how quickly will we have that  
10 study? And, third, to what effect will that determine what  
11 the preference will be, assuming the Heinz amendment does not  
12 pass?

13 Secretary Mentz. The answer to number one is correct.  
14 Let me find out what the answer to number two is.

15 Mr. Brockway. During the break, Senator Heinz, just a  
16 point of clarification. In your exchange with Senator Boren,  
17 I think the indication was that this investment credit,  
18 allowance of that against the alternative minimum tax, would  
19 also be against the individual minimum tax? Because I am not  
20 sure that is incorporated in these numbers, because under  
21 present law you don't get the investment credit against the  
22 individual alternative minimum tax. But still, I think the  
23 corporate rate changes in the same order of magnitude.

24 The Chairman. Well now, can I understand something? And  
25 maybe, Mr. Secretary, you can help me on this.

1 This is basically a trade-off. I was ambivalent about  
2 this, until I began to grasp that this is a trade-off. We  
3 are going to raise the rent one percent, so that some  
4 corporations will pay 34 percent so that others will pay  
5 three or four or five percent. Is that a rough trade-off?  
6 I mean, some will.

7 Secretary Mentz. Some will, that's right.

8 The Chairman. Somebody just handed me this example, and  
9 I am curious: "General Electric has \$379 million in investment  
10 tax credits, not counting 1986. Although they could not  
11 totally escape tax with just the ITC, their tax rate would  
12 be very, very low." Is that correct?

13 Secretary Mentz. Yes. As Mr. Brockway says, if they  
14 fall into the minimum tax by reason of the book income  
15 provision, their tax rate under the minimum tax would be  
16 three percent.

17 The Chairman. Well, in that case, in terms of trying to  
18 do rough-cut equity and equality of taxation between these,  
19 do you mean it can be some of the very profitable corporations  
20 that can reduce their tax significantly?

21 Secretary Mentz. That is correct.

22 Senator Baucus. Mr. Chairman, I have two questions yet.  
23 I haven't got an answer to my question yet.

24 Secretary Mentz. We will not be able to get the results  
25 of that study, Senator Baucus, in time to blend it into the

1 legislative process that you are now engaged in.

2 Senator Baucus. What is your best guess as to the  
3 degree to which that will lower the tax preference item here,  
4 assuming again that the Heinz amendment does not pass?

5 As I understand it, that study will shorten the economic  
6 lives of a lot of different categories -- that is, the present  
7 ADR system is dated.

8 Secretary Mentz. Well, it would depend upon what  
9 statutory provisions you enacted.

10 Senator Baucus. I am assuming the provision that is  
11 before us right now. Absent the Heinz amendment, I am asking  
12 the degree to which that preference will be -- what I am  
13 really getting at is, I think the main thrust of the Heinz  
14 amendment is the gap or disparity between ADR midpoint and  
15 ACRS lives.

16 I was trying to point out that if the ADR lives is  
17 updated, that gap will be much less than is anticipated in  
18 the Heinz amendment.

19 Secretary Mentz. I think that is a fair point, Senator.  
20 Yes.

21 Senator Baucus. So I am trying to figure out how much  
22 less it will be, given your best guess.

23 Secretary Mentz. Well, it is very hard to say. It  
24 would depend on asset-by-asset, and it would naturally depend  
25 upon how quickly that progress is made on that study.

1           Some would go longer and some would go shorter, so it  
2 is not -- what you are saying is correct. I am just not sure  
3 what conclusion can be drawn from it.

4           Senator Baucus. All right. But generally will the  
5 preference be lower or higher? Can you tell?

6           Secretary Mentz. Again, we cannot tell.

7           Senator Baucus. Thank you.

8           The Chairman. I have the following order: Senators  
9 Chafee, Moynihan, Pryor, and Danforth.

10          Senator Chafee. Mr. Chairman, I am deeply troubled by  
11 this, particularly the investment tax credit being offset  
12 against the minimum tax.

13          It seemed to me, Mr. Chairman, when we gathered here,  
14 long before we went through all the iterations we have gone  
15 through, there is one thing that there was unanimity on, and  
16 that was that we wanted everybody paying some tax. And we  
17 set it at 20 percent.

18          The House has 25 percent, and we went 20 percent. And  
19 that was one thing that I think everyone seemed to agree on.  
20 Indeed, I think we went as far as to say in some of our  
21 speeches, at least I did, that no matter what happened around  
22 here on tax reform, that a tax bill at the minimum would come  
23 out with a minimum tax which everybody would have to pay.

24          Now as I see it, as I follow the discussion here and  
25 what Secretary Mentz said to Senator Pryor, we are really

1 creating a big hole in the minimum tax. So, as was pointed  
2 out, by using the investment tax credit as an offset against  
3 the minimum tax, a company could get its minimum rate down  
4 to three percent.

5 I don't see how we can support that. It just doesn't  
6 seem right in the context of everybody paying something.

7 The Chairman. I didn't fully understand that when I  
8 first saw the amendment. I am inclined to agree with you now  
9 that the appearance of equity can be lost.

10 Senator Chafee. Well, I think so, Mr. Chairman.

11 If there is one thing, again, that we have had absolute  
12 consternation and anger from our constituents on, it is  
13 that some of the major corporations in the country, and some  
14 people, can get away with paying no tax.

15 And after all the trouble we have gone to, to suddenly  
16 get into that predicament once again, I would think would  
17 be unfortunate.

18 Now, I think there is also something to remember here,  
19 that if a company has no profits, it is not going to have to  
20 pay a tax -- minimum or otherwise.

21 So, that is where I have my hangup with the Heinz  
22 proposal, Mr. Chairman.

23 Senator Moynihan. Mr. Chairman?

24 Senator Pryor. Mr. Chairman, could we have order,  
25 please? We can't hear. Could we have order, please,

1 Mr. Chairman?

2 The Chairman. I apologize.

3 Senator Heinz. Senator Chafee, I thank you for yielding  
4 just briefly. You made two statements, and I would  
5 appreciate it if you might clarify it with the staff down  
6 there. I think they are kind of central to the debate.

7 The first is that we sacrifice the appearance of equity  
8 if we leave the carryover of the investment tax credit in  
9 here now. I think you and I agree that those investment  
10 tax credits were earned by companies; they did make  
11 investments.

12 The question I would appreciate your posing to the staff  
13 is: Would those investment tax credits ever be redeemable  
14 within any reasonable timeframe under the bill, the way the  
15 bill is written? And if they are not, we are engaging in  
16 retroactive taxation.

17 The other question would be related to the question of  
18 whether a company that is not making any money will be forced  
19 to pay the minimum tax.

20 I think you will find, if you ask the staff, that the  
21 answer is they will.

22 Senator Chafee. If they are not making any money? Well,  
23 what is the answer, Mr. Secretary, to the first question?

24 Secretary Mentz. Well, the answer, Senator Chafee, is  
25 the investment credit carryovers are usable against regular

1 tax liability, and they carry over for 15 years.

2 Senator Chafee. So, all we have done so far, before  
3 the Heinz amendment, is that you can't use them as an offset  
4 against the minimum tax?

5 Secretary Mentz. That is right.

6 Senator Chafee. You can use them as an offset against  
7 the ordinary income?

8 Secretary Mentz. If a corporation is in a profitable  
9 position, and gets into a regular taxpaying position, they  
10 are available as under the Chairman's proposal.

11 If the corporation stays in the minimum tax position,  
12 it arranges its affairs so that it is able to, for one reason  
13 or another, stay in that posture where it never gets to the  
14 regular tax, is always in the minimum tax, then they are not  
15 available. But I think they are not available for a specific  
16 reason, and the reason tha you just articulated.

17 Senator Chafee. Now, the next question Senator Heinz  
18 had was, can a company not have profits and pay the minimum  
19 tax?

20 Secretary Mentz. If a company has profits, book profits,  
21 it will pay at least a 10-percent minimum tax. The question  
22 is -- that is before investment credits. So at that point  
23 you have a question whether you allow the investment credit  
24 or you do not. If you allow it, it is three percent; if you  
25 don't allow it, it is 10 percent.

1 I guess that is as straightforward an answer as I can  
2 give.

3 The Chairman. Senator Moynihan?

4 Senator Moynihan. Mr. Chairman, as a member of the  
5 minority, I feel I may have to vote "present" on this measure.

6 We have a very precise interest in becoming a majority  
7 in this body, and in 1984 we picked up very valuable seats  
8 in the Senate with a campaign, a very respectable campaign,  
9 which was based on a simple pamphlet, which was absolutely  
10 true, which said in the State of Illinois, "Last year you  
11 paid more taxes than General Electric."

12 I really want to ask whether we really want to do this.  
13 This may sound odd, but if the Chairman can hear me, do we  
14 really want to do this to American business?

15 During the deliberation which we held in informal  
16 meetings, we made constant reference to an annual report of  
17 an American corporation, a very well-known one, which  
18 reported that its accountants found it had made \$149 million  
19 in profit last year, which reported in effect that it paid  
20 a large amount of taxes to Colonel Qadhafi and got a refund  
21 from the United States Government.

22 Now, that sort of thing does not do American business  
23 any good. Its officers are almost bound by their trust to  
24 take advantage of arrangements that make it possible; but, in  
25 the end it erodes the reputation of our corporate system.



1           And if we end up putting through this arrangement and  
2           insisting we are going to have a minimum tax, we are going to  
3           close shelters, as the Washington Post said yesterday, "We  
4           are going to tear the roof off tax shelters," and end up with  
5           giant corporations paying three percent tax, it erodes the  
6           whole confidence not just in our tax system but in our  
7           economic system. And if you care about that economic system,  
8           don't vote for this.

9           The Chairman. Senator Pryor?

10          Senator Pryor. Mr. Chairman, all of my life I have tried  
11          to figure out some way to get rich.

12          (Laughter)

13          Senator Pryor. And I am poorer today than I think I  
14          ever have been in my entire life.

15          But I have been sitting here for three years on this  
16          committee, watching not only how the rich get rich, but how  
17          they stay rich. And I think I have found the solution. And  
18          I think it is embodied right here in this particular  
19          discussion on this particular amendment, because we don't see  
20          out here in these halls the GEs and the General Dynamics, and  
21          the major corporations of America lobbying us to support the  
22          Heinz amendment.

23          What we see are hundreds of phone calls coming into my  
24          offices, and other offices, from poor, broke farmers that the  
25          ITC coalition has called and said, "Look you bought a hay

1 baler two years ago," or a tractor a year ago, "and you are  
2 going to get \$212 back if you will get Senator Pryor to get  
3 these ITCs back." So, they are using the poor to do that work  
4 and the rich are not even touching this issue, because they  
5 know they can get the poor to do the work for them. So, it is  
6 just kind of historically and traditionally the way they do  
7 it.

8 But maybe the \$200 that farmers get back, maybe they will  
9 get that back; but they don't talk about the \$150 million and  
10 \$600 million that one corporation is going to get back.

11 I don't think this is right. Once again, I say that we  
12 are retreating from the basic policy and the purpose of this  
13 "tax reform" measure that you have engineered and brought to  
14 this point. And perhaps on the day or on the eve of passing  
15 it, we are diluting it, and we are making, once again, a  
16 retreat, and once again we are saying that we are going to  
17 favor a few major corporations in this country.

18 Mr. Chairman, it is wrong. I am hoping, in all due  
19 respect, that we will not support the Heinz amendment. And  
20 I am also hoping that if we want to do something for the  
21 poor, and the people that really need this, if Senator Boren  
22 offers an amendment to give an investment tax credit of \$212  
23 back on this tractor, I am going to vote for it. But I am  
24 not going to vote to return it to the major corporations that  
25 don't make any money.

1 By the way, these poor farmers, they are not going to get  
2 anything, anyway, under this amendment, because they don't  
3 even qualify for the minimum tax; they are all broke, anyway.  
4 I hate to tell them that, but that is the case.

5 The Chairman. Senator Danforth, then Senator Boren.

6 Senator Danforth. I want to follow up on Senator Pryor's  
7 comments and Senator Boren's earlier comments and ask a  
8 question of Secretary Mentz.

9 Senator Boren in his remarks created the impression that,  
10 but for this amendment, bankrupt farmers -- and they are; they  
11 are bankrupt or on the verge of bankruptcy -- are going to be  
12 sucked into the minimum tax. I seriously doubt that. I  
13 don't think that the farmers of, for example, Missouri, who  
14 are going under right now, are somehow going to be sucked into  
15 the minimum tax because we don't apply the investment credit  
16 against the minimum tax.

17 My guess is that those farmers who will benefit by the  
18 Heinz amendment are corporate farmers, not family farmers;  
19 that farmers who benefit by the Heinz amendment are farmers  
20 who are doing it in a big way and have been doing it in a  
21 big way, and have had the money available in the last few  
22 years to put into a lot of equipment.

23 The family farmers haven't been buying equipment for  
24 years. And my guess is -- and Secretary Mentz may be able to  
25 shed some light on this -- that we are not going to see the

1 struggling farmers of the Midwest drawn into the minimum tax  
2 by the bill that we have before us.

3 Secretary Mentz. Well, I agree with you, Senator  
4 Danforth. I think what is the typical pattern -- it is not  
5 just farmers but any business that is experiencing hard  
6 times -- is that that business is incurring net operating  
7 losses. Not only are they not paying minimum tax but, if  
8 they were to turn profitable, their net operating losses  
9 would be available. But they are fighting bankruptcy; they  
10 are not fighting being subject to the minimum tax.

11 Indeed, last year in Reconciliation, there was an  
12 amendment made that took into account the case of an insolvent  
13 farmer whose property was foreclosed upon, and that gain was  
14 taken out of the minimum tax. To my knowledge, that was the  
15 one situation that might have possibly put him in a minimum  
16 tax.

17 But exclusive of that point, you are just simply talking  
18 about folks that are not going to be subject to the minimum  
19 tax.

20 Senator Danforth. And conversely, such farmers who would  
21 benefit by this are likely to be large operators or people  
22 who have got more than one business, or corporations in  
23 agriculture that have been able to purchase equipment and so  
24 on in the past. Would that be correct?

25 Secretary Mentz. Generally, yes. I suppose there might

1 be or could be all different fact patterns, and the reason why  
2 a business, whether it is a corporation or an individual, is  
3 in the minimum tax could vary. It could be because it is  
4 engaged in a series of leasing transactions designed  
5 deliberately to lower the tax, or it could be that they have  
6 made investments in equipment where there is investment  
7 credit and depreciation. But if that is the case, that  
8 business, whether it is a corporation or an individual, will  
9 phase out of the minimum tax and be back on the regular tax,  
10 and use its credits.

11 But if the idea is that the tax planning that they are  
12 pursuing is investing in sort of a corporate shelter to reduce  
13 or minimize their tax, they will be in the minimum tax; but  
14 I don't think you will feel sorry for them.

15 Senator Boren. Mr. Chairman?

16 The Chairman. Senator Boren?

17 Senator Boren. Mr. Chairman, I think I can clear up this  
18 mystery. I finally figured it out myself.

19 There were two Heinz amendments yesterday; both of them  
20 had to do with the ITC carryover. One of them was simply  
21 dealing with the cash-out of unused ITCs, which is the one  
22 I thought we were talking about. I thought that was the  
23 second portion.

24 The other ITC dealt with changing the preference  
25 definition under the minimum tax.

1           So, I think what the Senator from Arkansas and the  
2 Senator from Missouri have said, now that I have put them both  
3 in front of me, is correct.

4           I cannot anticipate a situation in which farmers who are  
5 going broke would end up being covered by the minimum tax.  
6 So, I don't think that the provision of carrying forward the  
7 70 percent of the ITC under the definition of tax preference  
8 is going to help the farmers that much, if any.

9           Senator Bentsen. Mr. Chairman, may I comment on that?

10          I get amused by the fact that people keep saying, "You  
11 know, once they incorporate, farmers start making money." I  
12 don't know any large corporate farmers, small corporate  
13 farmers, individual farmers, making money today.

14          Senator Boren. No. That is exactly right.

15          But Mr. Chairman, what I intend to do -- and I would like  
16 to ask the Senator from Pennsylvania this question -- I am  
17 troubled, as Senator Pryor is troubled, that if we allow this  
18 ITC carry-forward in the definition of minimum tax, it could  
19 have the effect -- and Senator Moynihan has also spoken to  
20 this -- of greatly reducing the minimum tax liability of  
21 very highly profitable corporations by a large amount,  
22 throwing them back into the book-value definition and down to  
23 possibly a three-percent rate.

24          I intend to offer, having heard this groundswell of  
25 sympathy from Senator Danforth and Senator Pryor and others,

1 a separate amendment, perhaps in league with the Senator from  
2 Pennsylvania, on agriculture, defining farmers as we have  
3 defined them in the Code, and allowing them some carryforward  
4 cash-out value on their unused ITCs that really will help  
5 the people I was talking about a while ago. I intend to  
6 offer that separately.

7 I do think the Senator from Pennsylvania has a very good  
8 point on the first half of his amendment, dealing with  
9 depreciation.

10 We have worked very, very hard to try to improve the  
11 situation with the depreciation. The Chairman has talked  
12 about this, and I think rightly so. Many of us have been  
13 concerned about cost of capital. And inadvertently, since  
14 we have a 20-percent rate under the minimum tax -- which is  
15 not that far a gap now between the regular corporate rate  
16 as we have lowered it -- we are really throwing back into the  
17 preference much of the advantage that we have given here in  
18 terms of depreciation. I think that is a mistake.

19 I would urge the Senator from Pennsylvania, for what it  
20 is worth, that he might take the first part of his  
21 amendment, which I think has great merit in terms of only  
22 defining as a preference the difference between ACRS and  
23 straight line, let us have an opportunity to vote on that --  
24 and I would enthusiastically support that -- set aside the  
25 question on the ITC carryforward, and let us try to deal with

1 that. I hope to deal with it separately for agriculture only,  
2 at some future time, before we can close out debate.

3 But I wonder if the Senator from Pennsylvania would  
4 entertain that thought?

5 I think, frankly, we don't want to open the door toward  
6 major reductions in the minimum tax through this cash-out of  
7 ITCs for some of those who have been the most notorious, in  
8 terms of providing us with examples for those who are not  
9 paying their fair share back to the system.

10 Senator Heinz. If I may respond to the Senator from  
11 Oklahoma, the reason that I would permit the investment tax  
12 credit -- which, after all, is an investment incentive that  
13 we did give people, going back some six or seven years -- to  
14 be utilized in part, and at a discounted rate of 70 percent  
15 against the minimum tax, is that it is my strong feeling that  
16 what we do if we don't permit that is, in effect, to achieve  
17 retroactive taxation.

18 So, I can't in all good conscience take this out of  
19 this amendment. If someone at some other point offers an  
20 amendment, and this isn't accepted, well then, that is another  
21 ballgame.

22 The only other thing I would say to my friend from  
23 Oklahoma is this: Somebody mentioned the Houes corporate  
24 minimum tax, and that it was at a higher tax rate. Indeed,  
25 it is: 25 percent.



1 It is interesting to me that the House corporate minimum  
2 tax raises \$5.7 billion at a 25-percent rate. Our minimum tax  
3 without the Heinz amendment raises roughly \$30 billion.

4 Even if my amendment were adopted and not paid for by  
5 the incremental increase in the corporate rate of roughly  
6 three-quarters of one percent, the Senate bill, if we didn't  
7 pay for my amendment, would raise between \$22 and \$23 billion  
8 through the corporate minimum tax, or roughly four times what  
9 the House provision would raise.

10 So, anybody who suggests that we are not being tough  
11 on corporate America, with or without the Heinz amendment,  
12 and particularly when compared to the House, ought to realize  
13 that we are going to be \$22-23 billion very tough on the  
14 corporate minimum tax, with the option of the Heinz amendment.

15 The Chairman. Is the committee ready to vote?

16 (No response)

17 The Chairman. Clerk, call the roll. Those in favor Aye,  
18 those opposed, No.

19 The Clerk. Mr. Dole?

20 The Chairman. No.

21 The Clerk. Mr. Roth?

22 Senator Roth. No.

23 The Clerk. Mr. Danforth?

24 Senator Danforth. No.

25 The Clerk. Mr. Chafee?

1 Senator Chafee. No.  
2 The Clerk. Mr. Heinz?  
3 Senator Heinz. Aye.  
4 The Clerk. Mr. Wallop?  
5 Senator Heinz. Aye, by proxy.  
6 The Clerk. Mr. Durenberger?  
7 (No response)  
8 The Clerk. Mr. Armstrong?  
9 Senator Armstrong. Aye.  
10 The Clerk. Mr. Symms?  
11 Senator Symms. Aye.  
12 The Clerk. Mr. Grassley?  
13 Senator Grassley. Aye.  
14 The Clerk. Mr. Long?  
15 Senator Long. Aye.  
16 The Clerk. Mr. Bentsen?  
17 Senator Bentsen. No.  
18 The Clerk. Mr. Matsunaga?  
19 Senator Matsunaga. No.  
20 The Clerk. Mr. Moynihan?  
21 Senator Moynihan. No.  
22 The Clerk. Mr. Baucus?  
23 Senator Baucus. No.  
24 The Clerk. Mr. Boren?  
25 Senator Boren. No.

1 The Clerk. Mr. Bradley?

2 Senator Bradley. No.

3 The Clerk. Mr. Mitchell?

4 Senator Mitchell. No.

5 The Clerk. Mr. Pryor?

6 Senator Pryor. No.

7 The Clerk. Mr. Chairman?

8 The Chairman. No.

9 Senator Durenberger. Durenberger, Aye.

10 The Clerk. Seven Yeas, 13 Nays.

11 The Chairman. The amendment is defeated.

12 Are there further amendments?

13 Senator Boren. Mr. Chairman?

14 The Chairman. Senator Boren?

15 Senator Boren. I would like to now offer the first  
16 portion of the Heinz amendment on depreciation as a separate  
17 amendment, and have it offset -- I don't have the figures in  
18 front of me to know of the exact same offset on the corporate  
19 rate, but that the corporate rate would be adjusted to pay  
20 for it just as under the Heinz assumptions, that we would use.

21 I assume it is going to be almost the same. And that  
22 the second part was at least in theory something of a trade-  
23 off.

24 The Chairman. David, did you say you were going to  
25 raise the corporate rate to pay for it?

1 Senator Boren. Raise the corporate rate to pay for it,  
2 and I would have to rely upon staff to say whether it  
3 requires one percent or in the neighborhood of one percent.

4 Mr. Brockway. Well, Senator Heinz's was about three-  
5 quarters of a point; it wasn't a full point. And if you are  
6 just doing the first part on the depreciation preference,  
7 that would only be maybe half.

8 Senator Boren. Half of a point?

9 Mr. Brockway. Or maybe four-tenths of a point, something  
10 like that.

11 Senator Boren. So I would like to offer that amendment,  
12 Mr. Chairman. As I said a while ago, I think we have worked  
13 very hard to try to put some balance back in. You were  
14 absolutely right to make the changes in depreciation that  
15 you supported and that Senator Durenberger supported.

16 I think the point was made by Heinz a minute ago that  
17 we all need to think about: Given the fact that we have  
18 changed the whole method in which we are calculating  
19 preferences, we are raising a lot more money under the  
20 minimum tax than is even raised by the House at a higher rate,  
21 we have the effect of throwing many more items into the  
22 preference category. I think we should really be concerned  
23 about that; especially when you have a corporate rate with  
24 not a wide spread between that rate and the minimum tax rate,  
25 you really are in some respects taking away with one hand what

1 you are giving with the other.

2 I don't think that this will have the evil or be subject  
3 to the criticism that was made a moment ago in terms of  
4 allowing some of the defense contractors and others to carry  
5 forward these ITCs to throw them into the lower rate.

6 It will certainly have some impact, but I would suggest  
7 it is the kind of impact we want to have. We want to  
8 encourage capital formation. We have all talked about that  
9 at length. I think we all understood the discussion of the  
10 matter; it just sets aside the whole controversy over the ITC,  
11 which I, frankly, myself misunderstood earlier in the  
12 discussion, and it gets us back simply to the point on  
13 depreciation, so that we can have a separate expression on  
14 that.

15 So, I just move adoption of that part-one, standing alone,  
16 of the Heinz amendment.

17 The Chairman. Senator Bradley?

18 Senator Bradley. Mr. Chairman, as I understand  
19 Senator Boren's amendment, it is only part one of Senator  
20 Heinz's amendment?

21 Senator Boren. That is correct, and it would be paid  
22 for -- the staff has estimated they would have to do the  
23 exact calculation. It is four-tenths of one percent, as  
24 opposed -- roughly.

25 Senator Bradley. All right.

1 Senator Heinz. It would be paid for by part-three,  
2 wouldn't it?

3 Senator Boren. Paid for by part-three of the Heinz  
4 amendment, correct.

5 Senator Bradley. The question that I guess comes to  
6 mind, Mr. Chairman, is why we want to double the amount of  
7 depreciation that can be claimed without a minimum tax? That  
8 is how I read this amendment.

9 If you are going to "for corporate and individual  
10 minimum tax, the depreciation preference for both real  
11 and personal property would be changed to require straight-  
12 line treatment, not over ADR midpoint as under the Chairman's  
13 proposal, but instead over ACRS life," now that is the  
14 difference between 33 years and 18 years. I don't know why  
15 we want to double the amount of depreciation that you can  
16 take before you even get to a minimum tax, and to pay for  
17 that by raising the corporate rate, which will have the  
18 effect of increasing the cost of capital for the whole  
19 economy in order to take care of an even narrower segment of  
20 the economy than the previous amendment.

21 The Chairman. Senator Symms?

22 Senator Symms. Mr. Chairman, I support the Boren  
23 amendment, and I think the Senator from Oklahoma made a good  
24 point, that the broad base of the minimum tax, even at a  
25 lower rate, is a much higher dollar figure than may be

1 meeting the eye here.

2 But, unfortunately, the one part of the Heinz amendment  
3 that was part of it that I think the committee would look  
4 favorably on was to keep current law in mining exploration  
5 and development cost, so that they are not considered a  
6 preference.

7 It would be minimal cost, and I would like to offer it  
8 as an amendment to the Boren package, if he could accept  
9 that.

10 Senator Boren. Is that on the mining?

11 Senator Symms. It is on mining exploration and  
12 development cost, that those would be treated as current law  
13 and not put in as a preference.

14 Senator Boren. Yes. I would be happy to accept that.

15 Senator Symms. That is worth \$100 million.

16 Mr. Brockway. I should clarify one thing: in current  
17 law they are treated as a preference, both in the individual  
18 minimum tax and the corporate add-on tax. So, that has  
19 historically been a preference.

20 I am sorry, excuse me. Not the corporate add-on, just  
21 the individual alternative minimum tax. The corporate add-  
22 on, they have not been treated as a preference.

23 Senator Symms. Well, just keep current law on that.  
24 It is a small part, but the mining industry, my colleagues,  
25 is just being bombarded with foreign imports and loss of jobs,

1 and we are losing our mineral capability.

2 Senator Boren. Mr. Chairman, I am very sympathetic to  
3 that. I know about the devastation of that industry, and I  
4 would accept it.

5 Senator Symms. I would appreciate it.

6 Senator Boren. Let me say, again we are going to pick  
7 up much of what Senator Bradley has talked about in the book  
8 value portion.

9 I think we have to think long and hard. We can do great  
10 things in terms of providing capital formation incentives  
11 in the basic bill; but then, if we go ahead and make all of  
12 these full preference items at a 20-percent rate, we are  
13 going to end up -- and I am for a minimum tax. I don't want  
14 to see 50 corporations in this country make \$53 billion and  
15 pay not tax; I am strongly for that.

16 But I think, at the same time, we have to keep our eye  
17 on the ball. Part of what we are trying to do here is to  
18 encourage investments and get our productivity up, and  
19 encourage capital formation, and I think that should be as  
20 strong an aim in any tax bill we write, is lowering rates.

21 We had better start thinking about these deficits we  
22 have, including the trade deficit. I think, here we are,  
23 encouraging investment.

24 The Chairman and we were all absolutely right when we  
25 voted for the improvements in depreciation. All I can say is,



1 let's don't take away with one hand what we are purporting  
2 to give with the other.

3 The Chairman. Mr. Secretary?

4 Secretary Mentz. Thank you, Mr. Chairman. I would just  
5 like to make an observation: The reason that the Chairman's  
6 proposal on the minimum tax, on the corporate minimum tax,  
7 raises dramatically more money than the House is primarily  
8 the book-income provision; it is not the difference in  
9 treating the accelerated portion of depreciation as a  
10 preference.

11 Indeed, the House provision is the same, basically, as  
12 the Chairman's in that respect -- it takes the accelerated  
13 portion of the depreciation over what they call "nonincentive  
14 depreciation," that is, depreciation over roughly useful  
15 lives, and that is a preference in the House bill as well.

16 And, indeed, that is where current law is by and large.

17 The idea of a minimum tax, as I said before, is to  
18 measure the preference over what economic depreciation would  
19 be. That is the preference, and for minimum tax purposes we  
20 think that is the right measure of the preference.

21 Also, I had mentioned that the rate reduction is a  
22 significant improvement to cost of capital. We think that is  
23 really where you ought to be focusing. That is the real  
24 cost-of-capital advantage to this proposal.

25 The Chairman. I wonder if I might reemphasize that.

1           For years -- Bill Roth isn't here, but he deserves a  
2 great deal of credit, and Bill Bradley -- they have been  
3 talking about the efficiencies of lower rates. They have  
4 brought me around as a convert. And I hate to see us move  
5 at all off of that.

6           If we can say to the public: 27-individual, 33-corporate,  
7 and not 33.3 or 33.4, and say we have eliminated all kinds of  
8 deductions and exemptions, we are going to have a bill that  
9 the public will overwhelmingly support and we can justifiably  
10 support, and I would hope we would not weaken now when we  
11 have been so successful in holding it to this 33-percent rate  
12 so far.

13           Senator Bradley?

14           Senator Bradley. Mr. Chairman, I would just echo your  
15 words and say, in particular, if the effect of this  
16 amendment would be to take individual real estate investors  
17 effectively out of the minimum tax, which is precisely what  
18 this amendment would do, and the idea that you would catch  
19 them in book value -- you wouldn't catch individuals in book,  
20 you would catch corporations in book.

21           So, the point is that the effect of this, I don't think,  
22 is the result we want from an equity standpoint, at all.

23           Senator Heinz. Would the Senator yield, Mr. Chairman?

24           If I thought that was the case, I would agree with him.  
25 But under the committee bill, we give real estate straight

1 line, not accelerated. And therefore, I don't see how, since  
2 realtors get straight line depreciation under the committee  
3 bill, they are going to be taken out by this amendment.

4 Senator Bradley. I would refer to Mr. Wilkins on this,  
5 if we could, to answer this question. But it is my  
6 understanding that it doubles the amount of depreciation you  
7 get before you even get to a minimum tax.

8 Mr. Wilkins. Senator Bradley, the depreciation  
9 preference for individuals for real estate is the difference  
10 between 40-year straight line and 30-year straight line.

11 If the Boren amendment were accepted, there would be  
12 no difference between 30-year straight line for the regular  
13 tax and the straight-line rule for the minimum tax, so there  
14 would be no depreciation preference. There might, however,  
15 be a passive loss preference in the case of a passive  
16 investor.

17 Senator Bradley. But no depreciation preference?

18 Mr. Wilkins. That is correct.

19 Senator Heinz. And passive loss preferences have been  
20 eliminated, as I understand it, by the bill.

21 Senator Bradley. At this time, that is correct,  
22 Senator Heinz.

23 Senator Heinz. All right.

24 The Chairman. Senator Symms?

25 Senator Symms. Mr. Chairman, right along this line, I

1 want to ask a question.

2 The Chairman has made the point here that he doesn't want  
3 to raise the corporate rate, and Senator Bradley is saying  
4 this is going to raise the cost of capital. Is it possible  
5 to adjust this -- I would ask Treasury -- in a fashion so  
6 that Senator Boren could achieve his goal and I could achieve  
7 my goal of concern for some of these companies that are  
8 under such stress, and do it by stretching out the  
9 depreciation a little bit so you don't have to fool with the  
10 rate, and still have the same effect, that the impact of the  
11 minimum tax would be less damaging? Is that possible?

12 Secretary Mentz. I suppose it is possible. What you are  
13 suggesting, Senator Symms, is a slightly different  
14 depreciation system, if I understand it correctly for a  
15 regular taxpayer.

16 Senator Symms. I don't know if this is going to be  
17 accepted; I just asked the question. I am going to vote  
18 for the Boren amendment, but if we don't win the Boren  
19 amendment, I would hope we could at least explore it.

20 If the major opposition the Chairman has to it is the  
21 fact that it will raise the rate by a third of a point, or  
22 some such matter -- did I hear the Chairman correctly?

23 The Chairman. That is my principal objection. I think  
24 I am opposed to it on substance, also; but I feel very  
25 strongly about keeping the rate at 33 percent.

1 Senator Symms. Well, 33-and-a-third has a nice ring to  
2 it.

3 (Laughter )

4 Senator Bradley. It does a lot for simplicity.

5 Senator Long. How could 33-and-a-third make for  
6 simplicity? Instead of multiplying by 34, you just divide  
7 three by three.

8 (Laughter)

9 The Chairman. And I will repeat the same comment I have  
10 repeated before: Even though Russell is leaving the Senate,  
11 I would like to vote him unanimously to be a member of the  
12 Finance Committee in retirement. We will not have humor like  
13 that around.

14 Senator Long. Demetrius.

15 The Chairman. Further discussion?

16 (No response)

17 The Chairman. If not, the Clerk will call the roll on  
18 the amendment.

19 The Clerk. Mr. Dole?

20 The Chairman. No.

21 The Clerk. Mr. Roth?

22 (No response)

23 The Clerk. Mr. Danforth?

24 Senator Danforth. No.

25 The Clerk. Mr. Chafee?

1 Senator Chafee. No.  
2 The Clerk. Mr. Heinz?  
3 Senator Heinz. Aye.  
4 The Clerk. Mr. Wallop?  
5 Senator Heinz. Aye, by proxy.  
6 The Clerk. Mr. Durenberger?  
7 Senator Durenberger. Aye.  
8 The Clerk. Mr. Armstrong?  
9 Senator Armstrong. Aye.  
10 The Clerk. Mr. Symms?  
11 Senator Symms. Aye.  
12 The Clerk. Mr. Grassley?  
13 Senator Grassley. Aye.  
14 The Clerk. Mr. Long?  
15 Senator Long. Aye.  
16 The Clerk. Mr. Bentsen?  
17 (No response)  
18 The Clerk. Mr. Matsunaga?  
19 Senator Matsunaga. No.  
20 The Clerk. Mr. Moynihan?  
21 Senator Moynihan. No.  
22 The Clerk. Mr. Baucus?  
23 Senator Baucus. No.  
24 The Clerk. Mr. Boren?  
25 Senator Boren. Aye.

1 The Clerk. Mr. Bradley?

2 Senator Bradley. No.

3 The Clerk. Mr. Mitchell?

4 Senator Mitchell. No.

5 The Clerk. Mr. Pryor?

6 Senator Pryor. Aye.

7 The Clerk. Mr. Chairman?

8 The Chairman. No.

9 The Clerk. Nine Yeas, nine Nays.

10 The Clerk. Nine-nine? The amendment is defeated.

11 Let us adjourn until 2:30. There is a vote at 2:00, and  
12 we will come back here at 2:30.

13 (Whereupon, at 12:39 p.m., the session was recessed.)  
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1 AFTERNOON SESSION

2 (2:38 p.m.)

3 The Chairman. The committee will come to order.

4 The chair recognizes Senator Roth.

5 Senator Roth. Mr. Chairman, because of the importance of  
6 the amendment I intend to offer, I would like to wait a few  
7 minutes until we have a few more present.

8 It is no mystery as to what I am going to offer. Maybe  
9 they will be here in a few minutes.

10 The Chairman. I can go to Senator Matsunaga for a  
11 minute.

12 Senator Roth. All right.

13 The Chairman. And if I might just explain in terms of  
14 a reestimation on some revenues. Sparky, go ahead.

15 Senator Matsunaga. Thank you, Mr. Chairman. The Joint  
16 Committee on Taxation informs me that, on the previous  
17 amendment which I offered relative to business energy tax  
18 credits, we do have enough now to extend the solar geothermal  
19 to three years, rather than two.

20 The Chairman. If the Joint Committee has reestimated,  
21 I would suggest we accept it.

22 Without objection, it is accepted.

23 Senator Matsunaga. Thank you very much.

24 The Chairman. Further amendments?

25 Senator Armstrong. Are you open for questions, Mr.



2  
1 Chairman?

2 The Chairman. Yes.

3 Senator Armstrong. This may not lead to an amendment,  
4 but we have had some discussions, I guess both on and off  
5 the record, about the property and casualty industry.

6 And at various times, I am told that they have worked  
7 out the question of this discounting issue with staff; and  
8 at other times, I have heard they have not.

9 Could we just pin that down? And then, I will know  
10 whether or not I need to offer an amendment or where we are.

11 The Chairman. Ms. Groves, property and casualty, is  
12 that yours?

13 Ms. Groves. Yes. My understanding is that the Joint  
14 Committee has revised their revenue estimate now. They think  
15 they made a mistake.

16 So, maybe they should speak to it.

17 The Chairman. All right. Dave, can you speak to that?

18 Mr. Brockway. My understanding is what we worked out  
19 turned out to be \$400 million down, if we could have a little  
20 more time on it.

21 We made an error in our computation. In the next few  
22 minutes, we will try and work something out to try and solve  
23 that.

24 Senator Armstrong. Great.

25 The Chairman. Further amendments?

1           Senator Armstrong. Mr. Chairman, could I ask one other  
2 informational question?

3           The Chairman. Yes.

4           Senator Armstrong. We have been talking about the  
5 question of grandfathering some of these life insurance  
6 policies.

7           Do we have, or can we ask staff to begin to pull together,  
8 the revenue implications of grandfathering loans on existing  
9 policies and/or grandfathering existing loans on life  
10 insurance policies?

11           The issue there, Mr. Chairman, you will recall is what  
12 is the effect on the insurance industry if we disallow the  
13 deductibility of loans on these policies?

14           Traditionally, this is a form of loan that a lot of  
15 policy holders have had. And the concern that some people  
16 in the industry have expressed is that it will result in  
17 wholesale cancellation of policies, which I think is not  
18 our desire.

19           But I am a little at sea to know how to address this  
20 problem because I don't know what the numbers are.

21           The Chairman. Did you ask two questions? One was  
22 grandfathering existing policies and/or grandfathering  
23 existing loans on present policies?

24           Senator Armstrong. Yes. That is my question. What are  
25 the numbers associated with those two items?

1 The Chairman. Let me say, in defense again of the Joint  
2 Committee, I am delighted with the expeditious manner in  
3 which we are operating. They are barely staying one jump  
4 ahead of us on revenue estimates, and they haven't really  
5 requested we slow down; and they are not suggesting that.

6 Senator Armstrong. That suits some of the rest of us.

7 The Chairman. I know. I understand that.

8 (Laughter)

9 Senator Moynihan. Mr. Chairman?

10 The Chairman. Senator Moynihan?

11 Senator Moynihan. Mr. Chairman, this is an amendment  
12 which we adopted two years ago and which I believe the Joint  
13 Committee estimates will have a five-year revenue effect of  
14 less than \$25 million.

15 And that is in present law, only a natural person can  
16 own a cooperative apartment.

17 Under present law, only a natural person can own a  
18 cooperative apartment, which is a bit of an anomaly.

19 And this would allow corporations and partnerships to  
20 do so. There are those who think it is important for the  
21 housing market in some parts of the country and in my city.

22 And the revenue effect, I believe, is negligible.

23 We had discussed and adopted this two years ago, I  
24 believe.

25 Mr. Brockway. It was adopted in the 1984 Act. The

1 revenue estimate is less than \$25 million, I believe.

2 The Chairman. Over five years?

3 Mr. Brockway. Yes.

4 The Chairman. Pat, I don't mind saying de minimus is  
5 \$10 million or less. I realize in a trillion dollar budget,  
6 25 is not a lot.

7 Senator Moynihan. I will think of something. I will  
8 vote with you on four things that are over \$1 billion.

9 The Chairman. All right.

10 (Laughter)

11 The Chairman. Let's put it aside for the moment, and  
12 let's see where we can come up with something.

13 Further amendments?

14 (No response)

15 The Chairman. If there are no further amendments, --

16 Senator Roth. Mr. Chairman, I will begin.

17 Mr. Chairman, there has been a lot of talk about the  
18 need for simplicity and fairness in the tax reform  
19 legislation; and with this, I agree.

20 But I think equally important is that tax reform promote  
21 savings; and certainly, in part, the reduction in marginal  
22 rates does help do that.

23 However, I do not think it goes far enough, and the reason  
24 I think savings is important is that it is important that we  
25 have a continuing new source of capital, not only for existing

1 business, but for the new entrepreneurs coming on the scene  
2 with the new technology.

3 And one of the, I believe, successful innovations that  
4 was introduced by this committee in 1981 was the concept--the  
5 expanded concept--of IRA.

6 At that time, it was said Congress was concerned that  
7 a large number of the country's workers, including many who  
8 are covered by employer-sponsored retirement plans, faced the  
9 prospect of retiring without the resources needed to provide  
10 adequate retirement income levels.

11 The Congress concluded that retirement savings by  
12 individuals--could I have the attention of the committee,  
13 Mr. Chairman?

14 The Chairman. I apologize, yes. That was my fault.

15 Senator Roth. Thank you, Mr. Chairman.

16 To continue the quote from the 1981 Tax Act:

17 "The Congress concluded that retirement savings by  
18 individuals during their working years can make an important  
19 contribution towards providing retirement income security."

20 Now, as I said, the concept of IRAs originated in this  
21 committee, and I believe that our decision in 1981 has proven  
22 to be a huge success. As a matter of fact, IRA savings have  
23 grown from \$20 billion in 1981 to about \$250 billion today.

24 In 1981, Mr. Chairman, only 3.4 million taxpayers had  
25 IRAs. Today, more than 28 million have IRAs. I think it is

1 important to understand that these are not tax shelters for  
2 the rich.

3 As a matter of fact, nearly 80 percent of IRA users  
4 have incomes less than \$50,000 a year.

5 Now, Mr. Chairman, I think it would be a most serious  
6 mistake for our committee now to reverse directions. We  
7 have talked long and hard about the importance of savings.

8 We have urged people to participate in IRAs, and yet,  
9 I find to my dismay that in this current package, which you  
10 know --

11 The Chairman. Can we have order, please? I don't think  
12 they can hear, Bill. Can we have quiet in the room? Go ahead.

13 Senator Roth. What I was saying is that I think this  
14 initiative has been tremendously successful and that it would  
15 be a most serious critical problem to reverse direction  
16 currently.

17 Let me just point out the participation in this program.

18 As I mentioned, today there are 28 million households  
19 with IRAs that are worth roughly \$250 billion. Now, of the  
20 members of this committee, the participation in their States  
21 is from 20 percent to as high as 49 percent.

22 The State of New Jersey, for example, has 49 percent of  
23 their households participating in IRAs. That is over 1,000,341  
24 persons.

25 I would point out, Mr. Chairman, in your own State, that

1 out of a million households, over 300,000 are participating  
2 in the IRA.

3 In my own State, it is roughly 40 percent. Out of 228  
4 households, 92,000 are participating.

5 And again, the point I want to emphasize and underscore  
6 is that this program is participated in over 50 percent by  
7 people whose income is \$40,000 or less.

8 So, this is not a rich man's shelter. This is indeed  
9 a middle class effort to take care of their retirement.

10 Now, what I propose to do, Mr. Chairman, is to amend  
11 the proposal to continue IRAs as they have in the past and,  
12 of course, that costs a bundle of money.

13 And I would like to ask Mr. Brockway: As I understand it  
14 now, to continue IRAs, what would be the annual cost of that?

15 Mr. Brockway. The revenue effect over the five-year  
16 period is \$27 billion against the package. So, it would be  
17 about \$6 billion a year in annual costs.

18 Senator Roth. It is really not quite that high, is it?  
19 I thought it was about \$26.6 billion.

20 (Laughter)

21 Senator Roth. That is an important point because we  
22 are trying to make this revenue neutral. And what I would  
23 propose to pay this cost is through increasing the gasoline  
24 tax.

25 Now, I will start out by saying, Mr. Chairman, I am not

1 particularly wedded to that source of revenue.

2 I would be very happy to consider others, but it does  
3 seem to me that the gasoline tax is one of the better  
4 prospects.

5 The reason I say that is, of course, the cost of gasoline  
6 has declined substantially, and there is agreement among  
7 conservationists that, if you put this kind of a tax on  
8 gasoline, that it is a pro-conservation move.

9 So, what I propose in my amendment, Mr. Chairman, is  
10 to continue IRAs in their present form so that 28 million  
11 Americans can continue to save along these lines, and to  
12 pay for it through an increase in the gasoline tax.

13 Could I ask you, Mr. Brockway, exactly how much would  
14 that take?

15 Mr. Brockway. My understanding is that it would be a  
16 6.6 cent increase.

17 Senator Roth. I thought for every cent we had something  
18 like \$6 billion.

19 Mr. Brockway. Unfortunately, Senator, I am getting that  
20 checked right now because the same question came to me --

21 The Chairman. Can I ask a question on the estimate on  
22 the \$27 billion? That is the five-year cost of extending all  
23 of the IRAs presently.

24 Now, for some reason, I thought it was a much bigger  
25 figure than that.



1 Mr. Brockway. You have already extended, Mr. Chairman,  
2 the IRAs for --

3 The Chairman. Oh, thank you. For those who have no  
4 other pension? All right.

5 Mr. Brockway. Senator Roth, right at the moment, I am  
6 having that double checked. The piece of paper that I have  
7 right now says it is \$26.9 on the IRA, and then 6.6 cents;  
8 and I will get the exact numbers checked.

9 Senator Roth. I think this is yours. In the excise tax  
10 options, it says there that an increase of motor fuel taxes  
11 by 6 cents per gallon would bring in--Mr. Brockway?

12 Let me just repeat what I was saying. The form we were  
13 given yesterday, which I thought came from the Joint Tax  
14 Committee, said that at a six cents increase per gallon on  
15 motor fuel taxes, it would bring in \$35.5 billion.

16 That is considerably more than the \$26.6. It would  
17 appear that the increase in the tax would have to be roughly  
18 four cents, rather than six cents--a little over four cents.

19 Mr. Brockway. We have just reconfirmed that. It would  
20 be the 6.6; and that earlier number was incorrect. Let me  
21 have them go back and check again.

22 I don't know on that sheet of revenue options--that was  
23 what raised the question to me because it did say \$35.5  
24 on that for a six cent increase; but I am told it is \$26.9  
25 for an IRA repeal and a 6.6 cent increase in the gasoline

1 tax would pay for that.

2 The Chairman. Could I ask you this, Dave? How long  
3 will it take to check that?

4 Mr. Brockway. It will just take a couple minutes. It  
5 may be that earlier lists --

6 The Chairman. Why don't we continue to discuss the  
7 issue? It may be four cents and it may be six cents, but  
8 the issue is using the gasoline tax to pay for the IRAs.

9 And we can see what the amount would be in five or ten  
10 minutes.

11 Senator Roth. That is satisfactory with me. As I  
12 said, Mr. Chairman, if anybody has a better revenue measure,  
13 I would certainly be happy to consider it; but I think it  
14 would be a very, very serious mistake at this juncture to  
15 spend several years encouraging people to save for their  
16 retirement and then suddenly say, well, we are cancelling  
17 that and moving in a new direction.

18 So, I would urge favorable consideration.

19 The Chairman. Senator Chafee?

20 Senator Chafee. Mr. Chairman?

21 The Chairman. Can we have order, please?

22 Senator Chafee. Mr. Chairman, I don't think anybody on  
23 this committee has been a more fervent supporter of the  
24 IRAs than I have, going right back to the original time  
25 when Hensen Moore in the House and I both introduced it in

1 the Senate. Let me just say this, Mr. Chairman.

2 The philosophy that I have taken, and I believe many  
3 others on the committee have taken, is that we want this  
4 bill to be revenue neutral; but we want it to be revenue  
5 neutral through eliminating preferences, loopholes--whatever  
6 they might be--not through the imposition of additional  
7 taxes.

8 And Mr. Chairman, I would support additional taxes in  
9 connection with deficit reduction, but not, Mr. Chairman, in  
10 connection with funding some program that we want under this  
11 tax reform.

12 And so, reluctantly, Mr. Chairman, I would have to oppose  
13 the proposition or proposal by the Senator from Delaware,  
14 whether it is four cents or five cents or 6.6 cents, whatever  
15 it is.

16 Now, there is a lot of merit, I know. I think also others  
17 will present contrary arguments on whether indeed IRAs, one,  
18 have increased savings. It seems, just looking at it, that  
19 they have.

20 Now, the savings rate nonetheless has decreased in the  
21 country, but I suspect that is not because of IRAs or shifts  
22 from savings accounts into IRAs. I think IRAs have helped  
23 savings in the nation.

24 Others will say that it is more for the middle income  
25 and upper brackets, and particularly upper brackets. I know

1 the Senator from Delaware would dispute that.

2 But Mr. Chairman, I hope that we would not accept this  
3 amendment because of the fact that we are sopping up revenue  
4 that we are going to need for deficit reduction and not  
5 some time in the indefinite future--this year.

6 Whether it is this form or something else, we have to  
7 get revenue this year, which obviously we hope would be in  
8 a separate bill.

9 Thank you, Mr. Chairman.

10 Senator Mitchell. Mr. Chairman?

11 The Chairman. Senator Mitchell and then Senator Danforth.

12 Senator Mitchell. Mr. Chairman, I strongly oppose this  
13 amendment, with all due respect to our friend from Delaware.

14 If enacted, this will continue a trend which has been  
15 occurring in this country for the last five years. And that  
16 is to reduce those taxes based on ability to pay and increase  
17 those taxes that are unrelated to ability to pay.

18 In 1981, we enacted a massive tax decrease in the Federal  
19 income tax, which is the principal Federal tax based on  
20 ability to pay. In 1982, 1983, and 1984, we increased  
21 virtually all other Federal taxes, almost all of which are  
22 unrelated to ability to pay.

23 We increased the gas tax. We increased the Social  
24 Security payroll tax. We increased a whole host of excise  
25 taxes.

1           The effect of those decisions, taken together, has been  
2 to dramatically shift the burden of taxation in our society  
3 down the income scale because it is high income taxpayers  
4 who have been the principal beneficiaries of the income tax  
5 reductions, while the taxes not based on ability to pay,  
6 which were increased, are all regressive in nature; that is,  
7 they consume a disproportionately large share of the income  
8 of low income persons purchasing the same services as high  
9 income persons.

10           Mr. Chairman, when you proposed your initial plan with  
11 the excise tax increases, I read to this committee excerpts  
12 from a report by the Senate Finance Committee in 1965, which  
13 denounced the effort to increase taxes unrelated to ability  
14 to pay as a means of financing reductions in taxes based on  
15 ability to pay.

16           That was sound policy then. It is sound policy now; and  
17 it is a policy, I might say, which we pursued in this country  
18 until 1980.

19           And now, we have completely reversed course, and the  
20 effect has been for almost everybody in the middle and lower  
21 income classes higher Federal taxes overall than they were  
22 paying before 1980.

23           For those in the higher income classes, the effect has  
24 been massive reductions in taxes overall, and this will  
25 simply continue that trend, which I say is an undesirable

1 trend from the standpoint of our society and is very unfair.

2 The last thing we need to do is to increase the gas tax  
3 by six cents so that we can further reduce Federal income  
4 taxes or preserve special deductions in the Federal income  
5 tax.

6 And Mr. Chairman, I strongly urge the members of the  
7 committee to oppose this.

8 I thought, Mr. Chairman, in all candor and due respect,  
9 that you were dead wrong with respect to the excise tax  
10 provisions that you proposed; and I said so.

11 The Chairman. In retrospect, so do I.

12 (Laughter)

13 Senator Mitchell. And so, I strongly urge that. Now, I  
14 have a table here that is published by the Joint Tax  
15 Committee, and it is entitled "Number of Returns and Amount  
16 of Payment to IRAs Distributed by Adjusted Gross Income  
17 Class 1983."

18 And what it demonstrates is that the principal number  
19 of returns and amount of payments utilizing the IRAs occur in  
20 the upper income classes. Now, that is what this table shows.

21 I am not going to bother to read it all. I would like  
22 to have it placed in the record at the appropriate point  
23 because it demonstrates the case very conclusively.

24 The Chairman. Without objection, it will be in the  
25 record.

(The prepared information follows:)

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1 Senator Mitchell. But again, what we are doing is we  
2 are increasing a tax that is paid equally by all and bears  
3 especially heavily on the working poor so that we can finance  
4 a preference that is utilized principally by those at the  
5 upper end of the income scale.

6 Mr. Chairman, we have been doing that for five years in  
7 this Government, and I say it is time we stopped doing it.

8 The Chairman. Senator Danforth and then Senator Roth.

9 Senator Danforth. Mr. Chairman, we are concerned here  
10 only with the tax reform bill, not with the concerns about  
11 the budget.

12 As we all know, the budget resolution that was passed  
13 last week calls for revenue increases, and it may be that  
14 we will have to increase the gasoline tax as part of a  
15 revenue increase to meet our commitments under the budget  
16 resolution.

17 But I don't think that we should blow that potential  
18 source of revenue for deficit reduction on IRAs. Now, IRAs  
19 are very popular. A lot of people have them.

20 But I think that it is stretching matters to say that  
21 they have encouraged a net increase in savings. Maybe there  
22 have been some studies somewhere indicating that that has  
23 been the case, but to me it defies common sense to say  
24 that there has been much increase in net savings as a result  
25 of IRAs.

1 I think what has happened is that people have shifted  
2 around money from one account to another to take advantage  
3 of IRAs or, in some cases, even borrowed to put money in  
4 IRAs.

5 I was at the airport a few weeks ago, and I noticed a  
6 big sign, an advertisement for a bank, and the sign said:  
7 Borrow to put money in an IRA, right before the April 15th  
8 deadline for putting money in an IRA.

9 In other words, that is no increase in savings at all.  
10 It is simply a shift from borrowing where the deal was to  
11 deduct the interest on your borrowing and then put your money  
12 in the IRA.

13 So, it is just a shifting around of funds. And finally,  
14 I would say that we have attempted to try to make sure that  
15 the bill that we report out of this committee is a bill  
16 that treats people fairly and not one that skews tax  
17 reduction for people in the upper income brackets.

18 And if what we are going to do in this bill is to have  
19 a very regressive tax--a gasoline tax--substituted for the  
20 repeal of the IRAs, then we are heading in the wrong  
21 direction.

22 And I think what this will do to the distributional  
23 tables and what it will do to the general support of the  
24 American public is very negative.

25 And therefore, I would urge the defeat of Senator Roth's



1 amendment.

2 The Chairman. Senator Roth and then Senator Matsunaga.

3 Senator Roth. Mr. Chairman, I think it was back in  
4 the 1970s when Lloyd Bentsen was chairman of the Joint  
5 Economic Committee where a major report was issued on the  
6 problem of productivity.

7 And in that report, as well as a number of subsequent  
8 studies including the President's Commission on Productivity,  
9 it has been urged that this country must become a savings  
10 nation.

11 And I listened to what the distinguished Senator from  
12 Maine had to say and talk about the ability to pay. What  
13 concerns me is that for years we followed the pattern of  
14 ever-increasing and higher taxes, and maybe there was more  
15 and more reliance on the ability to pay, but there were fewer  
16 and fewer people able to pay because there were less jobs.

17 I would point out that, since 1981, the number of new  
18 jobs created has risen very substantially. Now, I think it  
19 is about time that this committee gives some thought as to  
20 how tax reform will not only be fair, will not only be  
21 simple, but will help us to be competitive in world markets.

22 The fact is that this country is losing out, and other  
23 countries are taking over; and anyone who has travelled to  
24 the Pacific Basin, Japan in particular, or other countries  
25 know full well that it has been the individual savings of

1 the Japanese people that have enabled that country to develop  
2 the most modern industrial capacity in the world.

3 As a result, they are challenging us for the industrial  
4 leadership during the next century.

5 Now, as I said, many people--Democrats as well as  
6 Republican reports--have acknowledged that personal savings  
7 is important. I fully understand that there are those who  
8 say tax incentives don't help promote savings.

9 Yet these same people will argue long and hard that we  
10 have to give credits for energy conservation. We have to  
11 give credits for historical restoration, because they will  
12 bring about these desired action.

13 But for some reason, they don't think that it will help  
14 promote savings when, in fact, studies have shown that at  
15 least \$7 or \$8 billion additional savings is resulting from  
16 this program.

17 Now, Mr. Chairman, I am not going to ask for a record  
18 vote at this time; but I do want to put the chair on notice  
19 that it is my intent to offer this amendment--or offer a  
20 similar amendment--one that is revenue neutral--I won't say  
21 necessarily how we will finance it--because I think one of  
22 the most important things we can do is to continue the IRAs.

23 As I said, for Government, for Congress to suddenly  
24 reverse itself after years of sponsoring and promoting  
25 individual savings, all of a sudden to say that was wrong.

1 it doesn't work, is giving the wrong signal; and I think we  
2 will set this country back and not help promote jobs.

3 The Chairman. Do you want an oral vote, or do you  
4 simply want to withdraw it for the moment?

5 Senator Roth. Mr. Chairman, I will withdraw it at the  
6 moment, but reserving the right to offer it at a later time.

7 Mr. Brockway. Mr. Chairman, if I could just clarify  
8 what happened. The \$35 billion pickup at six cents was  
9 taken--this sheet that you were using was taken from an  
10 earlier sheet that had revenue options off the chairman's  
11 mark. And on that proposal, there was also a disallowance  
12 of the deduction for the gasoline tax.

13 So, any particular increase would raise that much money.  
14 So, that is what accounts for the mixup.

15 But under current law with the full deductibility, 6.6  
16 cents is the appropriate increase.

17 The Chairman. It is the what?

18 Mr. Brockway. The 6.6 cent increase is what would raise  
19 you the \$27 billion.

20 Senator Matsunaga. 6.6 cents?

21 Mr. Brockway. 6.6 cents.

22 Senator Roth. Mr. Chairman, I would ask the help of the  
23 Joint Tax Committee in trying to find adequate sources of  
24 revenue to make this revenue neutral.

25 The Chairman. In order, Senator Matsunaga, Senator

1 Baucus, and Senator Armstrong.

2 Senator Mitchell. Is this on the same subject, Mr.  
3 Chairman?

4 The Chairman. Yes.

5 Senator Matsunaga. Mr. Chairman, my sage counsellor from  
6 Louisiana and leader on this side always used to say that  
7 whenever there is a controversial issue, just vote; don't  
8 make speeches, because you can always explain your vote,  
9 but you can't explain your speeches.

10 (Laughter)

11 Senator Matsunaga. And I had not intended to make any  
12 speeches here, but I just wanted to indicate to the Senator  
13 from Delaware that I fully support his good intentions, and  
14 I think it is one which we considered wise at a time when  
15 this country needed to increase the savings among our  
16 citizens.

17 And I am fully for the encouragement of IRAs. However,  
18 the requirement that it be revenue neutral is what stymies  
19 the Senator's intentions here.

20 And as has been stated by others, the fact that you  
21 would take it out on the consumer by a regressive tax on  
22 gasoline is what I think bothers most of us who would  
23 otherwise be supporting the Senator's amendment.

24 And I am glad the Senator has withdrawn his amendment  
25 because --

1 Senator Roth. Would the Senator just yield on that  
2 point?

3 Senator Matsunaga. I would be happy to yield.

4 Senator Roth. I would point out, of course, that there  
5 has been a very substantial reduction in the cost of  
6 gasoline being paid by the American people; and that is one  
7 of the reasons that some people think that that is a  
8 reasonable source of funds for a worthy purpose.

9 I would also point out, as I did earlier, that many are  
10 concerned that we are going to become energy wasteful and  
11 might have a crisis in the future so that this is a good  
12 way to make this country more energy conscious.

13 Senator Matsunga. I commend the Senator for withdrawing  
14 his amendment and asking the Joint Committee to look into  
15 other possibilities.

16 The Chairman. Senator Baucus?

17 Senator Baucus. Mr. Chairman, I find it interesting  
18 to observe the many directions that this bill has taken in  
19 the last several months.

20 We all started out in this procedure, and it was simplify  
21 the Code. We were also at a time when our country faced a  
22 very adverse trade deficit and still does.

23 So, when this tax bill first came before this committee  
24 this year and last year and we had hearings, as I recall,  
25 I would say most of the members of this committee were asking

1 questions about our international competitiveness, and some  
2 questions about the cost of capital.

3 And basically, the concern, given our adverse trade  
4 deficit, was about where this country was going  
5 economically certainly in the next several years and even  
6 by the year 2000.

7 Then, we went down that road and we kept going down that  
8 road trying to address some of those concerns, and the bill  
9 became more and more and more complex.

10 We had more deductions and more different ways to try  
11 to skin the cat, and we finally got bogged down. The bill  
12 just didn't feel right; it didn't seem right. We seemed  
13 to be giving too much away.

14 So, we stopped going down that road. Now, we find  
15 ourselves, I think, repulsed by that exercise. We are not  
16 comfortable with that exercise.

17 So, we come back now and we come up with an approach  
18 which is much more simple, that is, we lowered the rates;  
19 and in order to get the rates lowered, we take the bulldozer  
20 on the individual side--a lot of the deductions, a lot of  
21 provisions, including the IRA deduction. That helps pay  
22 for the lower rates.

23 I just sense, as I listen to this debate, that while  
24 we are going down this road of simplicity and reform, in  
25 that direction, by the time this bill gets to the floor, and

1 later on then we are going to start addressing another goal  
2 of tax reform, which is equity.

3 We are going to find this bill, even though it is  
4 simpler in many respects, it is going to cause some people  
5 to be treated unfairly, unequitably; and we are going to  
6 try to straighten some of that out.

7 Then, I suspect we are going to go down the road and  
8 find out, my gosh, our trade deficit is still getting worse.  
9 We have to face our competitors. We have to increase our  
10 competitive position of American companies, and we have to  
11 increase savings rates and get that greater pool of savings  
12 in the country, etcetera.

13 And I think that is a very legitimate concern; and I  
14 predict that pretty soon we are going to--like a flock of  
15 birds--this committee is going to be addressing that question.

16 Today, we are not addressing that question. Today, we  
17 are addressing simplicity, true reform simplicity.

18 So, I think frankly that the Senator from Delaware has  
19 touched a real nerve here. It is a hot button; that is, it  
20 is a problem. It is our savings rate, and our low savings  
21 rate in this country.

22 And there is some question on the degree to which IRAs  
23 have actually increased savings rates. There are economists  
24 on both sides of that issue. But still, I think the tax  
25 policy does have some influence on people's decisions.

1 I don't know how much, but some effect, some influence  
2 on people's economic decisions. And I strongly feel that  
3 we have to work to devise a Code which is simple and is  
4 fair, but also addresses our savings rates and also addresses  
5 our economic competitive position.

6 So, I think that the amendment that the Senator from  
7 Delaware has offered is not quite precisely the right  
8 amendment because I don't think it is right to pay for this  
9 with a six cents or a six and a half cents gasoline tax.

10 But I do think he is on to something. And I hope that  
11 we can work this out during this next several weeks. A  
12 possible approach is to have the deduction set against only  
13 the 15 percent rate. That helps the distribution problem.

14 It also costs only \$15 billion, not the \$30 billion.  
15 There are ways to work this out, but I just feel that the  
16 Senator is absolutely correct. He is right.

17 The IRAs are basically a good idea, and we have to find  
18 a way to put it together so that we are not throwing the  
19 baby out with the bath water. So, that has to be addressed:  
20 simplicity and true reform.

21 We are also not turning our back to our international  
22 competitive position and our savings rates and all those  
23 other provisions which are so important to our international  
24 competitive position.

25 The Chairman. Senator Armstrong?



1 Senator Armstrong. Mr. Chairman, I would like to move  
2 from the broad philosophical to the quite specific provision  
3 of the bill relating to loan loss reserves.

4 It is my understanding that we have continued present  
5 law to permit the loan loss reserves of financial institutions  
6 to be charged against income; in other words, a deduction  
7 for those amounts that are added to the loan loss reserves.

8 Is that correct?

9 Mr. Brockway. That is correct.

10 Senator Armstrong. And we have extended that to finance  
11 companies. Is that also what the committee mark does at  
12 the present time?

13 Mr. Brockway. That is correct.

14 Senator Armstrong. My question is this: What do we do  
15 about the farm credit system? Do they have that same  
16 opportunity?

17 Mr. Brockway. Let me get back to you on that specific  
18 question, Senator.

19 Senator Armstrong. Mr. Chairman, I don't mind deferring  
20 while they check that; but if there is doubt about it, we  
21 have got to treat these PCAs and banks for cooperatives  
22 the same way we treat commercial banks and other lenders.

23 We can't leave them in a different status. So, I don't  
24 think the dollars involved are large. I don't know what they  
25 are, but we just can't have the production credit associations

1 have a less favorable treatment than the commercial banks.

2 The Chairman. If they can check that, Senator Bentsen  
3 has an amendment. I think he is cleared, and we can go to  
4 Senator Bentsen for the moment.

5 Senator Armstrong. Fine.

6 Senator Bentsen. Thank you very much, Mr. Chairman.

7 One that I would like to propose on the part of myself  
8 and Senator Grassley is an at-risk amendment, and it is with  
9 respect to loans by institutional lenders, that the rules  
10 would not be triggered by the fact that the lender has an  
11 equity participation in the project to which the loan relates,  
12 or the fact that the lender participates in the management of  
13 the project.

14 The reason we have put the at-risk rules in was that we  
15 were trying to hit at these fraudulent situations, or at  
16 least misrepresenting situations where they would phony up  
17 the price of a property, and the seller in turn would give,  
18 after increasing the value substantially over its true value,  
19 would then carry back a loan against it to the purchaser.

20 So, we put in the institution as a third party, figuring  
21 that they would truly value it. I think that same situation  
22 applies where the institution loans money and also has an  
23 equity participation.

24 And this amendment would take care of that kind of  
25 situation; and I would like Secretary Mentz to comment on it.

1 Secretary Mentz. Senator Bentsen, Treasury regards that  
2 amendment as very reasonable, and we would support it.

3 The only danger that we see here is where the lender  
4 is related to the seller. That is where you get your seller  
5 financing. That is not what you are talking about.

6 You are talking about --

7 Senator Bentsen. No, no. That is not a problem.

8 Secretary Mentz. Right. So, Treasury would support it.

9 Senator Bentsen. All right.

10 The Chairman. No cost?

11 Senator Bentsen. No, it is revenue neutral. There is  
12 no cost.

13 Mr. Brockway. Less than \$50 million.

14 The Chairman. What?

15 Mr. Brockway. I mean there is some cost, obviously, in  
16 the amendment, but the overall area picks up. The estimate  
17 on this would be less than \$50 million.

18 The Chairman. Does it cost or not?

19 Mr. Brockway. It would have some --

20 Senator Bentsen. Well, I am in error then. Apparently,  
21 there is a minimal cost.

22 The Chairman. The reason, Lloyd, I would ask you if  
23 you wouldn't mind withholding, I asked Pat to withhold on  
24 a \$25 million amendment; and I don't want to start even at  
25 de minimus, in my mind, I think maybe \$10 million over five

1 years might be de minimus.

2 But on things like this where there are relatively  
3 slight costs, I am hoping we can package them where there is--

4 Senator Bentsen. I had been advised by staff that  
5 there was no cost involved, but apparently there is.

6 Mr. Brockway. I guess I am not sure where that came  
7 from. The overall average provisions do not pick up  
8 substantial net revenue, but this change would have a not  
9 insignificant impact.

10 And there is a large number of transactions involving  
11 large developments, and I think this is where you have an  
12 insurance company or some other major lender also taking  
13 active participation.

14 And it is a situation where clearly, to the extent of  
15 the at-risk rules and that type of transaction, this is not  
16 a syndication transaction generally, but that type of  
17 transaction, there will be some effect because, generally,  
18 the structure is designed to have the lender come in, take  
19 an equity interest, but effectively not be treated as the  
20 owner of the property, so that the other investors would  
21 get the depreciation.

22 So, it will have an impact in the transaction of being  
23 able to shift the depreciation from the, in this case,  
24 insurance company in that example to the other investors.

25 But the overall cost we are estimating to be less than

1 \$50 million.

2 Senator Bentsen. Apparently, I was misadvised. I was  
3 told there was no cost.

4 The Chairman. Let's wait and see what we can find out.

5 Senator Bentsen. All right.

6 The Chairman. Have we got an answer yet to Senator  
7 Armstrong's question?

8 Senator Armstrong. If not, Mr. Chairman, I am ready  
9 to take up another small issue.

10 The Chairman. Well, why don't you go to the other small  
11 issue?

12 Senator Armstrong. Mr. Chairman, for years it was the  
13 practice of people who had dividend withholdings to mail  
14 the 1099 form along with the final dividend check.

15 A year ago, we changed that and required--unwisely, I  
16 think--that the 1099's be mailed in a separate first class  
17 envelope. And one firm that came to my attention spent  
18 \$980,000 to do so.

19 So, my proposed amendment simply eliminates that  
20 requirement and permits us to go back to the old system where  
21 companies, banks, public companies that have dividends, and  
22 so on would be permitted to mail those in the way they  
23 formerly did and would be required to put on the envelope  
24 "Important Tax Return Document Enclosed."

25 In the interest of disclosure, let me make two points.

1 First, this is the substance, by the way, of a bill that  
2 Steve and David Boren and I have introduced separately, and  
3 there is some dispute as to whether or not this is a revenue  
4 neutral bill or a revenue gainer or a revenue loser.

5 I think somebody thinks that it will change the  
6 compliance. I don't think we have any reason to believe  
7 that; and in fact, if a company spends \$1 million in extra  
8 postage, that becomes a tax deductible expense. And so,  
9 to that extent, it becomes a revenue loser.

10 To the extent that it changes compliance, I suppose  
11 somebody could argue that the adoption of this amendment  
12 would cost some money.

13 My own instinct is we don't know that, but that it is  
14 ridiculous for us to require all of these entities to flood  
15 the mails with separate mailings.

16 And so, that is my amendment, and I move this --

17 Senator Moynihan. Mr. Chairman?

18 The Chairman. Senator Moynihan?

19 Senator Moynihan. Could I join Senator Armstrong in  
20 this matter? We have had any number of firms that have  
21 come to say that the only consequence has been to add \$1  
22 million to postal costs. I mean, there will be a revenue  
23 loss to the Postal Service, I guess.

24 It just bothers the business folks, and they say this  
25 makes no sense.

1 The Chairman. Mr. Brockway?

2 Mr. Brockway. As to whether or not this is cost  
3 efficient is another question. As to the revenue impact,  
4 Senator, I think that when this was put in it was at a time  
5 in context with the repeal of withholding.

6 I think that the then-chairman and others felt strongly  
7 that this item be included and felt that it would increase  
8 some compliance to have it in a separate cover.

9 As to whether there is an offset for the postage, I don't  
10 think we would take that into account because, while there is  
11 a deduction on that side, there is income--whether it is to  
12 the Government or for someone buying the envelopes--clearly,  
13 it cost the banks a substantial amount of money.

14 Whether that is cost effective is another question, but  
15 we do think that some impact of less than \$50 million, if  
16 you average --

17 The Chairman. \$50 million for this, too?

18 Mr. Brockway. Less than that. What the item is-- How  
19 much it is is very difficult to quantify.

20 The Chairman. The \$50 million comes because some  
21 taxpayers don't get this and don't comply? And that is how  
22 we lose the \$50 million or less?

23 Mr. Brockway. Either they get it and it is enclosed  
24 with other items and this isn't looked at as the important  
25 thing. If it is something different than a 1099, that it

1 looks like the official form just for that, how much, Mr.  
2 Chairman, is extremely difficult to weigh that, other than  
3 the presumption is that there is some positive effect.

4 And the members, when this was considered in 1984, had  
5 I guess strongly felt views on both sides of that.

6 The Chairman. Well, I might ask this. If you are going  
7 to say \$50 million, Bill, would you be willing to do as I  
8 have with Pat and Lloyd, where these meritorious amendments  
9 --or they seem meritorious to me--let me just put them aside,  
10 and we will see what they add up to.

11 And we will go in the back room for a private meeting  
12 here and see where we come up with enough money to cover all  
13 of them.

14 Senator Armstrong. Sure, I would be glad to package it  
15 up, although in fairness, I must say I can't see how we can  
16 put a revenue estimate on it.

17 I can't prove it isn't \$30 million or \$20 million or  
18 \$45 million, but I think it is an imponderable.

19 And just to be clear, the exact purpose of my amendment  
20 would prohibit enclosing advertising materials or anything  
21 like that. So, we are not talking about things getting lost  
22 in a jumble of other paperwork.

23 I just don't see there is a compliance question myself.  
24 but sure, let's package it up with everything else.

25 Mr. Brockway. Senator, as I understand, it wouldn't be



1 with advertising or statements or that type of thing; but I  
2 think the reason why I am giving you the less than \$50 is  
3 that this is very difficult to quantify.

4       There is the assumption that there is some benefit from  
5 receiving it under separate cover. How much that is, we  
6 don't know; and whether it is justified by the cost is  
7 another question.

8       Senator Armstrong. I understand, and I would be  
9 perfectly just to put that in that little package of de  
10 minimus items.

11       The Chairman. Senator Long and then Senator Symms.

12       Senator Long. Mr. Chairman, I have discovered that we  
13 have a problem with regard to a 1984 amendment that I  
14 sponsored, having to do with employee stock ownership.

15       It was the Secretary of Treasury--Don Regan's--idea  
16 that for a nonpublicly traded company to sell stock to its  
17 employees and have the benefit of a favored tax treatment  
18 under the ESOP that they should sell at least 30 percent.

19       And I never thought there would be any problem about  
20 this, but apparently there is. Thirty percent of what?  
21 So, I would like to suggest that we should have it clarified  
22 to say that selling 30 percent of the stock means that if  
23 you have 100 shares of stock all in the same class--30  
24 shares--that would be 30 percent of 100.

25       Now, if there is more than one kind of stock, if you have

1 three kinds of stock, then it would have to be 30 percent  
2 of the value of the stock sold, except that if he has 30  
3 percent of each class--like 30 percent of Class I, 30  
4 percent of Class II, 30 percent of Class III--then that  
5 would be the test.

6 It just seems to me that that is just common sense of  
7 how that ought to be; and I don't think there is any cost  
8 at all to that.

9 The Chairman. Mr. Brockway, any costs?

10 Mr. Brockway. This would have a negligible impact on  
11 revenues.

12 The Chairman. Is there objection to the amendment?

13 (No response)

14 The Chairman. Without objection. Senator Symms?

15 Senator Symms. Mr. Chairman, we have heard two or three  
16 meritorious amendments and we keep coming up with these  
17 figures that it costs \$25 million or \$50 million.

18 And I am very concerned about these numbers of costs  
19 that are being attributed to some of these different issues.

20 And I would just like to inquire of the Joint Tax  
21 Committee: Where did you come up with the numbers? People  
22 keep telling me that it would cost \$220 billion over five  
23 years to have a differential on capital gains rates.

24 Is that an accurate number?

25 Mr. Brockway. That is the tax expenditure. That is

1 what is in the tax expenditure budget. That is going from  
2 a 20 percent capital gains rate under current law to a  
3 50 percent capital gains rate.

4 That is current law, assuming the revenue loss from  
5 the difference between taxing that income at 20 percent and  
6 50 percent, current law rates, assuming that was always  
7 the rule.

8 So, two things. You have a very substantial increase  
9 in tax. It is done without essentially any behavioral impact  
10 because this assumes the rules are always-- That is not  
11 what the impact of this legislation would be by any means.

12 Senator Symms. The point I am trying to get at, Mr.  
13 Chairman, which I think is critical --

14 The Chairman. Can we have order, please?

15 Senator Symms. This committee seems to be moving along  
16 on a fairly fast track here now, but we keep getting these  
17 numbers thrown out here that this amendment would cost money  
18 or that one.

19 I would have to agree with what Senator Armstrong just  
20 said. I, for the life of me, can't see how his amendment,  
21 which would save businesses from business expense, would  
22 actually cost any money.

23 It might increase revenue to the Treasury because they  
24 would have a higher profit instead of another business expense,  
25 but back to that capital gains question.

1 I have serious reservations that it could cost the  
2 Treasury anything in view of what has happened in the past.  
3 Every time we have lowered the capital gains rate, the  
4 high income people have paid more taxes, and it is because  
5 it has generated more transactions in the aggregate.

6 Maybe they paid a lower rate, but they paid more taxes  
7 in total dollars. If we move forward here, is there any  
8 way we can get a relook at that number?

9 I would just like to know, before we pass a bill out of  
10 here, without a capital gains differential--which in my  
11 opinion is a big mistake, not to have a differential between  
12 the highest rate and the capital gains--for risk capital  
13 and for venture capital to encourage new business ideas and  
14 so forth.

15 And you are saying, if I hear you right, that the cost  
16 you are making is on past history.

17 Mr. Brockway. No, no. I am saying you raised the  
18 question about that \$220 billion number. I am saying that  
19 is not the revenue estimate; that is something taken from  
20 our tax expenditure budget pamphlet that is solely a measure  
21 for that purpose.

22 It is not a revenue estimate at all of a proposal to  
23 repeal that. That is a number --

24 Senator Symms. Well, how much would it cost to have a  
25 capital gains differential of five or six points or seven

1 points? Say, if we left it at 20 percent on the individual  
2 side? Isn't it in this package that corporations have a  
3 capital gains treatment, but individuals don't?

4 Mr. Brockway. Individuals is at 27, yes. There is no  
5 differential. That number would be substantially less than  
6 that.

7 Senator Symms. What would the corporate capital gains  
8 rate be?

9 Mr. Brockway. 28.

10 Senator Symms. 28? And the individual rate would be  
11 27?

12 Mr. Brockway. That is correct.

13 Senator Symms. In current law, it is now 20 percent.

14 Mr. Brockway. Correct.

15 Senator Symms. What would happen if you left it at  
16 current law? What would it cost this package?

17 Mr. Brockway. I will be able to get you that number in  
18 a while, but it is really unrelated to that \$220 billion  
19 number.

20 The Chairman. Steve, let me ask this. If members have  
21 a request for some estimates, if we could get them to them  
22 ahead of time instead of just asking them kind of point blank  
23 here, it would speed things up if they had it ahead of time.

24 So, they could answer your questions a little more  
25 exactly.

1 Senator Wallop. Mr. Chairman, could I make a small and,  
2 I hope, a distinction with some meaning?

3 While it is true in the rates there is no distinction  
4 here, at my request this bill keeps the rate of capital gains  
5 separate from the rate of income taxation.

6 So, in some future time, if there is a requirement to  
7 raise anything--God forbid--to raise revenues, you are going  
8 to have to do both. And I didn't want it understood in  
9 here that we have not made a distinction between capital  
10 gains and income.

11 The distinction is very thin when the rates are the same,  
12 but there is a distinction; and it is important that we  
13 don't try to make everybody think that it is the same, no  
14 matter what.

15 Senator Symms. That is exactly, I guess, the point I  
16 am trying to make, Mr. Chairman.

17 I think that is a critical issue as to whether I want  
18 to be for this bill. I wish we could get this straightened  
19 out. I don't understand where these numbers keep coming  
20 from.

21 And I think after this is all over with, in a week or  
22 two, we are going to come back and people are going to start  
23 having a new set of numbers on the bill.

24 I just wish there was some way to get some of these  
25 numbers before instead of after the fact. I can't believe

1 that it costs Treasury any money if we actually put in this  
2 law that capital gains rates on individuals would be 20  
3 percent, instead of 27 percent.

4 Mr. Brockway. Senator, there is a substantial amount  
5 of disagreement as to what the impact is that capital gains  
6 changes make.

7 And it definitely is our assumption that capital gains  
8 tax raises revenue. To repeal capital gains tax would lose  
9 revenue.

10 How much behavioral response there is, we don't know  
11 precisely; but clearly, our view is that the capital gains  
12 tax does raise revenue, that changing the rates in the  
13 short run will have a behavioral response; and so, in the  
14 first year, you might even lose a little bit of money,  
15 the second year you might break even.

16 By the third year and the fourth year, you are starting  
17 to pick up money. There is only so much behavioral response  
18 you can have for so long.

19 Obviously, on a long run basis, people have assets and  
20 they will want to realize the income from that. They do sell  
21 assets. They do pay capital gains tax.

22 And I think that, while there is a temporary behavioral  
23 response--and a very significant behavioral response and one  
24 that is taken account of in the revenues--that it is  
25 definitely our view that on an ongoing basis, there is a

1 revenue pickup from the capital gains tax, and one does not  
2 raise money on a long-run basis, or a five-year basis, by  
3 reducing that rate, but instead there is an increase.

4 At least in these percent ranges; and it may be a  
5 different thing when you have the rate go up to 50 percent.  
6 I think your response gets increasingly higher, the higher  
7 you go on that rate.

8 Senator Symms. One more question, if I might, Mr.  
9 Chairman; and that is what is the committee's interpretation  
10 on material participation in recreation or vacation homes,  
11 to get any passive loss?

12 Mr. Brockway. What would happen on that, Senator Symms,  
13 is that, coming in as rental property, it wouldn't turn out  
14 as material participation in that situation.

15 There it would be essentially subject to the limits,  
16 but you would get \$25,000.

17 Senator Symms. They would be able to get it?

18 Mr. Brockway. \$25,000 up to \$100,000 of income, and  
19 then it would phase out.

20 Are you talking about the typical vacation home --

21 Senator Symms. Where you have somebody renting it for  
22 you, and then you maybe use it a couple weeks of the year  
23 and don't rent it?

24 Mr. Brockway. And you have some involvement in the  
25 property?



1           Senator Symms. You have involvement in the decisions  
2 of who manages it, but you may have a real estate company  
3 or someone managing it for you. Are you materially  
4 participating or not?

5           Mr. Brockway. But this is a situation where you are  
6 making the management decisions? You have an agent that  
7 carries the items out, but you are involved in the management  
8 decisions of that. You would get the \$25,000.

9           Senator Symms. Thank you.

10          The Chairman. Senator Dole and then Senator Bentsen.

11          Senator Dole. Mr. Chairman, the President and the House  
12 and the Chairman's proposals all retain the existing 60 cents  
13 per gallon duty on imported ethanol.

14          Now, some producers have sought to circumvent the duty  
15 by bringing commodity high rated alcohol into a CBI country,  
16 dehydrating it there and then importing the ethanol into the  
17 U.S. duty free as a product of a CBI country.

18          The chairman's proposal closes that loophole, but it  
19 grandfathers some firms. And my amendment would simply  
20 tighten the grandfather.

21          Only those firms that have already made significant  
22 tangible investments in setting up a dehydrating plant would  
23 be entitled to bring in as duty free ethanol that was only  
24 dehydrated in a CBI country.

25          In addition, these firms would not be allowed to increase

1 beyond their existing capacity the amount of ethanol that  
2 they could bring in duty free.

3 The amendment is revenue neutral. In fact, it might  
4 gain some revenue since we would collect more duty on  
5 ethanol imports; and it is an amendment that I have worked  
6 on with the distinguished Senator from Louisiana, Senator  
7 Long.

8 I think he is in agreement with the amendment.

9 Senator Long. Yes, I am.

10 The Chairman. Is there objection to the amendment?

11 Senator Durenberger. Mr. Chairman, I just want to speak  
12 in favor of the amendment, having taken a position on it --

13 The Chairman. Is there objection?

14 (No response)

15 The Chairman. Adopted. Senator Bentsen, and then  
16 Senator Pryor.

17 Senator Bentsen. Mr. Chairman, I am offering an amendment  
18 that has been before this committee before and has been  
19 passed twice before, and I am offering it on behalf of  
20 myself and Senator Armstrong; and that is providing for  
21 private foundations being able to continue to operate a  
22 private business insofar as meeting the criterion for the  
23 paying out of funds to the endowment in return for charities  
24 and with some tough restrictions put on insofar as being  
25 sure that there is a limitation on the interlocking

1 directors, so it is limited to some 25 percent, so that  
2 the officers would not be receiving compensation from two.

3 And this involves the Houston Chronicle and the Houston  
4 Endowment, and it also involves the El Pulmer--and I may  
5 be mispronouncing that--the El Pulmer Foundation in Colorado  
6 that Senator Armstrong has had.

7 We have had this before the committee in 1982, 1984,  
8 and we passed it each time; and we have lost it in  
9 conference.

10 The Chairman. I think this amendment is totally  
11 meritorious. We have gone through this. We take it to  
12 conference every time with the House, and Treasury will  
13 strongly support us, won't they?

14 (Laughter)

15 Senator Dole. They will be consistent.

16 Secretary Mentz. I am not familiar with the amendment,  
17 Mr. Chairman.

18 The Chairman. Well, we will familiarize you with it.

19 Secretary Mentz. I am sure you will educate me as the  
20 process goes on.

21 The Chairman. It has great merit.

22 Senator Bentsen. And it is revenue neutral.

23 Senator Long. Mr. Chairman, in the event that that  
24 doesn't become law this time, I want to leave the wish that  
25 this committee will persevere 100 years if need be to get

1 that agreed to.

2 (Laughter)

3 Senator Long. I have voted for it several times. I  
4 hope it eventually becomes law.

5 The Chairman. Is there objection to the amendment?

6 (No response)

7 The Chairman. Senator Pryor?

8 Senator Pryor. Yes, Mr. Chairman, thank you.

9 Mr. Chairman, I would like to bring to your attention  
10 and to the committee a matter that Senator Exon passed on  
11 to me the other day from Nebraska, related to a small bank  
12 of \$68 million in assets in Nebraska--in Lincoln--being  
13 closed.

14 This bank was not insured by the FDIC, and all of the  
15 depositors in their bank, which were not too many, lost  
16 everything.

17 Now, the present law as I understand it, this loss could  
18 only be if they were individuals up to the point of \$3,000.  
19 The House bill has changed this.

20 And I think what we are talking about is asking that  
21 these depositors be able to deduct their losses in failed  
22 financial institutions and treat them as casualty losses.

23 Now, I don't know of other situations. There may be  
24 other uninsured financial situations in the country. I don't  
25 know a situation like this. It has been estimated, Mr.

1 Chairman, a \$12 million loss over five years--a revenue loss.

2 So, if I might, I would like to put that in the cracker  
3 jack barrel or box or whatever of small amendments where we  
4 would try to find an offset.

5 The Chairman. That will go in the barrel.

6 Senator Pryor. Now, Mr. Chairman, one other if I might.

7 This is no amendment; I would just like to ask questions.

8 Senator Bentsen raised the issue about foundations.

9 I can't hear, Mr. Chairman, and I want these people at  
10 the table to be able to listen real carefully because this  
11 really is a major problem in our State.

12 We have a foundation in the State that has only timber.  
13 It doesn't have any oil; it doesn't have any gas. It has  
14 timber. One hundred percent of all the proceeds of the  
15 timber go for charities--hospitals, schools, scholarships,  
16 etcetera.

17 Now, if we repeal the capital gains treatment, it is  
18 my understanding that the unrelated business income provision  
19 might have an impact on this, and I am just hoping that Mr.  
20 Brockway and Secretary Mentz and other distinguished people  
21 at this table will look into this matter so that this  
22 particular trust or foundation will not be adversely affected  
23 because of the change in capital gains in timber.

24 I wonder if they have a comment on this?

25 Mr. Brockway. If I understand the situation, it is a

1 question of whether the character of the income is changed  
2 and therefore, it would be subject to unrelated business  
3 income tax.

4 Senator Pryor. I think that would be the proper  
5 question.

6 Mr. Brockway. Pending further review on it, the  
7 proposal is designed merely to change the rate, and it  
8 should not affect that transaction.

9 Let me double check on that, but my understanding is  
10 that that transaction would not be adversely affected.

11 Senator Pryor. Fine. We will have a discussion about  
12 that. Mr. Chairman, also, I have another amendment that I  
13 may not offer at this point. I don't know if we really  
14 have the figures, and that is on the mailing lists exchanged  
15 by the Disabled American Veterans and the Red Cross and all  
16 of the tax-exempt organizations.

17 I think Senator Bentsen and Senator Wallop addressed  
18 this issue on the Senate floor about a year ago, but the  
19 Court of Claims has basically taken the position that this  
20 is income that should be taxable, and I hope that we can  
21 address this at a later time this afternoon or this evening.

22 I do have a way to pay for it. I just hope that I  
23 can explain it when I have the proper facts.

24 The Chairman. Further amendments? Are there any  
25 further amendments before we move to final passage?

1 Senator Wallop. Mr. Chairman?

2 The Chairman. Senator Wallop?

3 Senator Wallop. Mr. Chairman, I would like to inquire  
4 from the Tax Committee as to how they would score the repeal  
5 of the windfall profits.

6 We have a letter that scores it zero, and we have a  
7 letter in that same letter that scores it at \$7 billion.

8 If it is zero, I think we would like to follow the  
9 President's recommendation and the recommendation that was  
10 developed in Senator Dole's office to repeal it.

11 Mr. Brockway. In the current budgetary situation, we  
12 would be required to score it at the \$7 billion level because  
13 that is what goes into CBO's budget baseline.

14 It is based on outdated oil prices, but when they change  
15 that, it will make a number of other corresponding changes.  
16 Looking at this one time--and they carry the windfall profits  
17 tax as one item in their budget line--at current prices,  
18 however, in reality, if the prices stay at this level or  
19 reasonably in this range, there would be negligible revenue  
20 collected from the windfall profits tax.

21 And basically, once they change their budget estimates,  
22 you will end up seeing that number drop down to close to zero.

23 Senator Wallop. I guess my inquiry is would we see that  
24 in this process or some other time?

25 The Chairman. Do we see that when they do their

1 reestimates in the summer or when?

2 Mr. Weiss. Senator Wallop, as David said, our scoring  
3 assumptions are based on what the Senate Budget Committee  
4 uses for scorekeeping purposes, when this bill were to come  
5 to the Senate floor.

6 And I think, basically, what will happen will be that  
7 between now and then, it may well be that there are  
8 reestimates that go into the budget process; and at that time,  
9 all these assumptions would change.

10 But using the current assumptions that the Budget  
11 Committee uses for scorekeeping, we would be using the  
12 \$7.5 billion figure that we gave you before.

13 Senator Bentsen. A good point, as I understand it.  
14 Would the gentleman yield for just a point?

15 At this point, as I understand it, on the price, it has  
16 been, from the standpoint of economics, repealed. Once the  
17 price gets down below \$18.00 and \$19.00; but even so, you  
18 have a great deal of record keeping and a lot of red tape  
19 that continues to be involved in the reporting thereof.

20 And that is one of the reasons, certainly, that we  
21 would like to get rid of it.

22 Senator Wallop. Mr. Chairman, there is a certain  
23 frustration that when everybody knows that it is not raising  
24 any money and cannot, we score it at \$7 billion; but  
25 nonetheless, I understand that circumstance. However, I



1 would hope that the chairman would promise us that opportunity,  
2 not that he could deny us, but he wouldn't resist us in  
3 indulging that opportunity, should that scoring take place  
4 before the bill is passed on the floor.

5 The Chairman. When does it expire, anyway?

6 Mr. Weiss. At the end of 1991.

7 The Chairman. The only question I would have, Malcolm,  
8 is --

9 Senator Wallop. It expires at the end of 1991, assuming  
10 it raises the revenue that is based on this scoring estimate;  
11 and you know and I know that it is not going to be 1991.  
12 It might be 2001.

13 Mr. Weiss. No, there is a definite sunset, no later  
14 than 1991. It could have started to phase out earlier if  
15 it had raised in excess of the original estimates, but in  
16 no case --

17 Senator Wallop. I know who was responsible for those  
18 little criteria.

19 Mr. Weiss. But there is a definite sunset. In no case  
20 does it extend beyond that.

21 Senator Wallop. But if one of the goals of tax reform  
22 is tax simplification, it seems absurd to have people  
23 indulging in a lot of complex record keeping for something  
24 that raises no revenue to the Government.

25 The Chairman. Are there further amendments?

1 Senator Armstrong?

2 Senator Armstrong. Mr. Chairman, I think we are ready  
3 to just make the record on the property and casualty issue,  
4 if staff would just explain it. Then, I am ready to put  
5 that to bed and move on to the life insurance issue, if we  
6 are ready on that as well.

7 The Chairman. Is staff ready?

8 Ms. Groves. Mr. Chairman, as I understand it, the  
9 amendment would be a package that would be revenue neutral.

10 What it would do on the discount rate, it would be  
11 five percent in 1987, then 75 percent of the AFR thereafter.

12 In order to make that change revenue neutral, there  
13 would be an adjustment in how you treat the tail. Rather  
14 than having a five-year and three-year respectively kick in  
15 of income, it would have a longer discount period on long-line  
16 business and also would take the revenue offset under a  
17 premium reserve and do a seven and a half year phase in  
18 rather than a ten year. That is my understanding.

19 Senator Armstrong. I was distracted slightly during  
20 the explanation. Mr. Weiss, is that your understanding, too?

21 Mr. Weiss. Yes. The newer change--the seven and a half  
22 year phase in--was also necessary, in addition to the changing  
23 of the tail to make it revenue neutral.

24 Senator Armstrong. Is that acceptable to everybody, Mr.  
25 Chairman?

1 The Chairman. Discussion?

2 Senator Armstrong. It will be very hard to discuss  
3 because it is very hard to understand.

4 (Laughter)

5 The Chairman. I don't think there is going to be a lot  
6 of discussion on it, for that very reason.

7 Senator Mitchell. I would like to express my support  
8 for Senator Armstrong's amendment.

9 He has worked very diligently and closely with members  
10 of the industry and the staff to develop something that  
11 makes some sense, deals with a complex, difficult problem  
12 and does so in a revenue neutral fashion.

13 I hope the committee will accept it.

14 The Chairman. Is there objection to the amendment?

15 (No response)

16 The Chairman. Without objection, it is adopted. Senator  
17 Armstrong?

18 Senator Armstrong. Are we ready on the life insurance  
19 question, or if not, the PCA question?

20 Mr. Brockway. The PCA?

21 Senator Armstrong. The farm credit.

22 Mr. Brockway. Oh, the farm credit. They would have the  
23 bad debt reduction repealed under the proposal as it has been  
24 adopted. Obviously, you are in a very similar situation with  
25 the other financial institutions that a very rough look at it

1 says it is about point one. We are working with your  
2 staff to get a little bit more information, but I think that  
3 just the way it is structured, they would have not come  
4 within the exceptions.

5 But I think the facts of the circumstances are very  
6 similar to those institutions that --

7 The Chairman. You are saying that the production credit  
8 associations are like a bank, and they ought to be treated  
9 like a bank?

10 Senator Armstrong. Both PCAs and the cooperative banks.  
11 And I think Mr. Brockway is right. The dollar amount is not  
12 large, but I believe it would just be preposterous to think  
13 we are going to preserve the present reserve tax treatment  
14 for commercial banks and not do it for these cooperative  
15 banks and PCAs.

16 So, I move that amendment, if that is agreeable with  
17 everybody.

18 Senator Pryor. Mr. Chairman, I would like to associate  
19 myself with Senator Armstrong. This could be a real problem.

20 The Chairman. Now, let me ask a question. You have  
21 a \$100 million cost, though?

22 Mr. Brockway. Yes. Given the way we had estimated it  
23 earlier, we had assumed only finance companies would be taken  
24 out from the total and not this. So, if you went this far,  
25 a revenue pickup from the proposal in the package would be

1 \$100 million less.

2 The Chairman. Then, again, I would like to ask, Bill:  
3 \$100 million is a little more than 10 or 15, but I would like  
4 you to hold it. Again, it sounds meritorious to me, and I  
5 think we will find a way to do it.

6 Senator Armstrong. Fine. I just wanted to be sure it  
7 didn't get lost in the shuffle because I do not think it was  
8 the intention at any point to treat them differently from  
9 these commercial lenders.

10 Then, Mr. Chairman, are to the stage on the life insurance  
11 question that we can quantify that? I am somewhat in a  
12 dither about it, and let me just remind the members of  
13 the committee what the problem is.

14 We have got about 40 million policy-holders out there  
15 who own life insurance on which they have a right to borrow.  
16 And that has been a long-standing tradition in this country,  
17 that that is what you do when you need money to send somebody  
18 to college and so on--you borrow money on life insurance.

19 As I understand it, the bill in its present form will  
20 not permit a tax deduction for those life insurance loans.  
21 So, I guess there are four possible options.

22 One is just to leave them in the lurch, which I am  
23 loathe to do because it is represented to me that the result  
24 will be the cancellation of a lot of policies in just a  
25 wholesale fashion.

1           The second possibility would be to carve out life  
2 insurance loans as a separate category, different from banks  
3 or something.

4           A third would be to grandfather existing policies; and  
5 a fourth, I guess, would be to grandfather existing loans.

6           Can staff give us the costs of this? And I would really  
7 seek the counsel of the committee as to what we need to do,  
8 but we ought to do something to correct this.

9           Mr. Brockway. Generally, life insurance loans against  
10 life insurance policies would be treated the same as other  
11 loans; so therefore, unless it was used for investment  
12 purposes, or trade or business purposes, it would be subject  
13 to the limits, the consumer interest limits; and if you  
14 exempt it --

15           Senator Armstrong. But Mr. Brockway, didn't we take  
16 the consumer interest limit down to zero?

17           Mr. Brockway. That is what I am saying. Unless it was  
18 borrowed to use in your business or borrowed to carry  
19 investment--in which case you could net it against that  
20 income--it would be subject to the limits.

21           In other words, if you borrowed to buy consumer goods,  
22 you would not get the deduction.

23           Senator Armstrong. Right.

24           Mr. Brockway. Correct.

25           Senator Armstrong. The present limit is investment

1 interest plus \$10,000?

2 Mr. Brockway. Right, and this would take it down to  
3 zero, just in the investment income.

4 If you exempted all policy-holder loans from the interest  
5 limits, that is loans on new policies as well as old policies  
6 --about 1.5 billion over the period--if you grandfathered  
7 existing policies, existing loans and new loans on existing  
8 policies would be about \$1 billion over the period.

9 And if you grandfathered existing outstanding loans,  
10 it would be about \$500 million over the period.

11 The Chairman. Senator Bradley?

12 Senator Bradley. Nothing right now, Mr. Chairman.

13 The Chairman. Oh, excuse me.

14 Senator Chafee. Is this a proposal?

15 The Chairman. I don't think he has quite proposed it  
16 yet. There is a \$500 million cost.

17 This is one that I feel ambivalent about. We are changing  
18 rules along the way for others; and I understand people  
19 borrowing against insurance, but we are saying that they  
20 can no longer deduct to buy a car and they cannot deduct to  
21 buy a boat, and they cannot deduct on anything else; but  
22 they can deduct for insurance.

23 And I don't know if we want to say we are going to make  
24 an exception. Whether there is a unique exception for  
25 insurance that we ought to separate it out from everything

1 and say that is more meritorious --

2 Senator Armstrong. Mr. Chairman, I am somewhat in a  
3 quandry about this, too. I have not moved an amendment  
4 because I am not sure what amendment to move.

5 My sense is that this is an issue of really extraordinary  
6 importance to this industry. At least some of the people  
7 whose judgment I trust in this industry tell me that, if we  
8 don't figure out some way to help this, the result will be  
9 that there will be millions of policies that are going to  
10 get cancelled.

11 I don't know whether that is true or not, but that is  
12 what they tell me. I am wondering about this: Having  
13 presented the issue, I don't necessarily have to push this  
14 to a conclusion right now, and I don't have an offset to  
15 offer; but I didn't want to let it go by.

16 I guess I can wait and bring it up on the floor. I am  
17 reluctant to present it and have it get a poor vote and  
18 put a bunch of members on record on an issue for which the  
19 proper foundation has not really been laid and, honestly,  
20 this did not come to my attention until yesterday when I  
21 raised it with the committee.

22 So, unless somebody has got an idea, I would ask  
23 everybody to think about it, and then let's figure out a  
24 way to come up with the money to solve this problem, at  
25 least in part.



1 Senator Wallop. Bill, would you yield for a question?

2 Senator Armstrong. I would be happy to.

3 Senator Wallop. Can you deliver the rationale that  
4 was delivered to you as to why somebody would hold an  
5 insurance policy solely for the ability to borrow on it?

6 Senator Armstrong. No. There wasn't any representation  
7 to me that the only reason they would have a policy would be  
8 to borrow on it; but the reason traditionally why people  
9 buy these whole-life policies or 20-pay-life policies, or  
10 any policy that builds up a substantial cash value, in part  
11 is predicated on the fact that they looked forward to two  
12 or three times during their life--particularly in connection  
13 with college expenses--when they are going to need to borrow.

14 And it is quite a traditional thing, for example, when  
15 a young person is born, that their parents will buy a policy,  
16 a whole-life policy, that will build up enough cash so that  
17 money is there to borrow at the time of college expenses.

18 I mean, that is one rationale. It isn't that insurance  
19 generally would be cancelled, but this particular kind of  
20 policy, which has been sort of the backbone of the industry.

21 As I say, people in the industry tell me this is really  
22 going to have a serious effect, and I throw it out in those  
23 terms because I think there are people around this table  
24 who know a lot more about the insurance business than I do.

25 And I am sure not trying to hold myself out as anything

1 except the bearer of bad tidings and with the desire to work  
2 it out; but I don't have \$1 billion to come up with at the  
3 moment.

4 The Chairman. One of the things that strikes me--and I  
5 will go back to what I have said on occasion to the committee  
6 --my subjective poll over the past year to people of some  
7 wealth about how low would the maximum rate have to get  
8 before you wouldn't care about deductions. Oh, about 25  
9 percent.

10 We have it there. It is 27, but we are close. And  
11 they still care about deductions, and I guess they would at  
12 10 percent.

13 Senator Mitchell. What did I tell you?

14 (Laughter)

15 The Chairman. There is nothing worse than somebody who  
16 says "What did I tell you?" You were right.

17 (Laughter)

18 Senator Mitchell. Once again, you have come to my  
19 point of view.

20 Senator Armstrong. Mr. Chairman, the point here is not,  
21 however, the individual taxpayer; but it is an industry which  
22 has been built on contracts which are really quite unusual,  
23 if not totally unique, because most commercial transactions  
24 occur in a much shorter period of time than the 20 or 30 years  
25 or whole lifetimes that are often associated with an insurance

1 contract.

2 Usually, if you buy a car or a house, you make a deal  
3 and you close on it, and that is that. Or even if it is a  
4 term payment deal, it is a three-year payout or a five-year  
5 payout.

6 These are contracts which involve very long-term  
7 commitments which were entered into based upon a kind of  
8 historic understanding.

9 Now, it is also asserted to me by industry representatives  
10 --and I don't have any validation of this--that whenever we  
11 have made changes in insurance taxation before, we have  
12 tried to take into account policies already in existence,  
13 which is one of the reasons why I am disposed to do it.

14 Mr. Chairman, thank you for letting me raise this. What  
15 I am going to do is this. All the members have heard what  
16 the problem is. I am going to tell the people in the  
17 insurance business they had better get in touch with Senators;  
18 and if this is as big a deal as my Colorado people have  
19 indicated, then when we get to the floor there will be a  
20 general disposition to do something about it.

21 If it isn't that big a deal, then it will go away.

22 Senator Durenberger. Mr. Chaiman, on behalf of the  
23 people in my mailroom --

24 (Laughter)

25 Senator Durenberger. I don't like that idea at all.

1 Senator Durenberger. If you tell people in that  
2 industry to get a hold of us, they are going to get a hold  
3 of us.

4 They get a hold of our constituents, and they give them  
5 some half-baked notion that life insurance is going to  
6 disappear from the scene unless we vote for Bill Armstrong's  
7 amendment. I hope Bill has the good judgment to consult--

8 I mean, I thought he really did an excellent job of  
9 presenting the position, but I hope he consults with all  
10 of us before he brings it up on the floor.

11 The Chairman. Do you have an amendment, Dave? I see  
12 you hand up. Or is that just a comment on that?

13 Senator Durenberger. I was curious about the phase-out.  
14 I assumed that the phase-down on the interest is the same as  
15 all other unsecured or nonmortgage interest.

16 We are not automatically limiting interest income on --

17 Mr. Brockway. It is a three-year phase-in for this  
18 under the passive loss rule.

19 Senator Durenberger. The question is simply that their  
20 product is going to change from now on. It won't have this  
21 loan feature in it for the same purposes that existed before.

22 Mr. Brockway. Yes. And it won't be utilized to the  
23 same degree as right now.

24 The Chairman. Senator Grassley?

25 Senator Grassley. Mr. Chairman, --

1 The Chairman. I can't hear you.

2 Senator Grassley. I have a nonrevenue measure that I  
3 want to bring up.

4 My amendment would modify the Retirement Equity Act to  
5 change the interest rate assumption that plans are required  
6 to use in cashing out benefits under the defined benefit  
7 plan.

8 And under the Retirement Equity Act, the plans are  
9 required to use a rate no greater than the interest rate  
10 set by the PBGC.

11 Now, under my amendment, the plan would be required to  
12 compute the first \$3,500 of a participant's accrued benefit,  
13 using an interest rate no greater than the PBC interest rate,  
14 whether deferred or immediate, whichever is appropriate.

15 The remaining portion of a participant's accrued benefits  
16 could be computed using an interest rate no greater than one  
17 and two-tenths times the PBGC rate.

18 The amendment would apply to distributions after  
19 December 31, 1984, with a grandfather for plans that made  
20 distributions after December 31, 1984 and before enactment,  
21 in accordance with the requirements of regulations issued  
22 under the Retirement Equity Act.

23 And I would ask Mr. Strella if that is a fair statement  
24 of what my proposal does; and if it doesn't, then maybe you  
25 could broaden the understanding of it.

1 Mr. Stella. I think the only thing I would add,  
2 Senator, is that the amendment would only put a ceiling on  
3 the interest rate that a plan can use and would not require  
4 the use of that interest rate.

5 Senator Grassley. All right.

6 Mr. Brockway. That would be a negligible revenue effect  
7 of the amendment.

8 Senator Grassley. Mr. Chairman, I just offered an  
9 amendment.

10 The Chairman. Oh, I am sorry. I didn't hear. Wait  
11 a second, please.

12 I apologize. I was talking to Senator Boren.

13 Senator Grassley. All right.

14 The Chairman. I am sorry. Go ahead.

15 Senator Grassley. I guess I would ask if Paul would  
16 explain it, instead of my going through it again.

17 The Chairman. Paul, go ahead.

18 Mr. Stella. The amendment relates to the interest rate  
19 for the pension plan they use when an employee --

20 The Chairman. Would you talk a little louder, Paul?

21 Mr. Stella. To take a lump sum, instead of taking his  
22 pension over his retirement life. And in 1984, the Congress  
23 passed the Retirement Equity Act; and although the issue is  
24 not clear, the regulations interpreted that Act to require  
25 that the interest rate be no greater than the interest rate

1 prescribed by the PBGC.

2 This amendment would, in those cases where the employee  
3 voluntarily elects a lump sum, allow the plan to use an  
4 interest rate that is 1.2 times the PBGC rate for those  
5 amounts of the lump sum in excess of \$3,500.

6 Senator Grassley. No revenue impact, Mr. Chairman.

7 The Chairman. No revenue impact?

8 Mr. Brockway. There is no revenue effect. Negligible.

9 The Chairman. Treasury has no objection?

10 Secretary Mentz. No objection, Mr. Chairman.

11 The Chairman. Any objection to the amendment?

12 (No response)

13 The Chairman. Without objection, it is adopted.

14 Are there other amendments to be presented? Senator  
15 Chafee?

16 Senator Chafee. Mr. Chairman, are all our members in  
17 hearing distance?

18 The Chairman. No. Some are within negotiating distance,  
19 however.

20 Senator Chafee. I am throwing some pearls of wisdom  
21 out, and I wanted as much attention as possible. I hope  
22 they are pearls.

23 Mr. Chairman, we have taken very drastic action against  
24 the IRAs, and the arguments for the IRAs have been set forth  
25 here; but for some peculiar reason, there remains in effect

1 the 401(k)s.

2 Now, a 401(k) is a very specific benefit for a limited  
3 group of people. Somebody who is in a factory or a place  
4 of business and is fortunate enough to have a 401(k), that  
5 person under this provision can set aside up to \$7,000.

6 Now, am I not correct, Mr. Mentz, that that is the  
7 employee's contribution--the \$7,000 under the present system  
8 we have got?

9 Secretary Mentz. That is right.

10 Senator Chafee. In other words, if the employer wanted  
11 to match that, that doesn't affect the \$7,000 limitation?

12 Secretary Mentz. That is correct.

13 Senator Chafee. So, Mr. Chairman, the word "equity"  
14 has been bandied about here a little bit; and it seems to me  
15 to permit somebody--one group that is fortunate enough to  
16 be in a particular situation where there well could be a  
17 pension plan--this has nothing exclusionary about pension  
18 plans--there could be a very pleasant and generous pension  
19 plan in existence.

20 But nonetheless, that fortunate soul would be able to  
21 put away \$7,000, whereas the person who works in a factory  
22 without any pension plan at all, he is limited under our  
23 present situation to a \$2,000 IRA. And if there is a modest  
24 pension plan under the present system, he would have nothing.

25 Am I correct, Mr. Mentz?



1 Secretary Mentz. You are correct, Senator.

2 Senator Chafee. So, Mr. Chairman, there seems to be  
3 such a disparity there; and I know that we have seen from  
4 the figures that Senator Roth produced and the costs that  
5 Mr. Brockway came up with, that we couldn't restore IRAs  
6 completely.

7 But IRAs are extremely popular, and people can say they  
8 are for a certain wealthy group--I question that--but let's  
9 not debate that particular point here, because if we went  
10 to permitting a nondeductible IRA with only the inside  
11 buildup permitted, that is for those groups--we have already  
12 taken care of, we hope, those who have no other pension plan.  
13 They have a deductible IRA.

14 So, I am not discussing them. All I am talking about  
15 now is permitting a nondeductible IRA and allowing for the  
16 inside buildup to be tax free.

17 Now, as I understand, Mr. Brockway, that is a \$1.6  
18 billion item. Am I correct?

19 Secretary Mentz. That is correct.

20 Senator Chafee. Now, the way I propose to pay for that,  
21 Mr. Chairman, is to reduce the 401(k)s from a maximum of  
22 \$7,000 to a maximum of \$5,000.

23 Now, what you are doing under that is--no one can say  
24 we are trampling on the poor here--I mean, we are still  
25 allowing anybody who has got access to a 401(k) to have a

1 \$5,000 deduction.

2 And indeed, when he gets into the plan, the plan is  
3 far more generous in its withdrawal opportunities than an  
4 IRA is. We are familiar with that.

5 And so, Mr. Chairman, I think that what we should do is  
6 at least permit those people who have used IRAs or who might  
7 want to use IRAs in the future to have the possibility out  
8 there that they could set aside \$2,000, nondeductible.

9 All we are providing for is the inside buildup would be  
10 tax free.

11 That is my proposal, and that is a wash revenue-wise.

12 Senator Heinz. Mr. Chairman?

13 The Chairman. Senator Heinz?

14 Senator Heinz. Mr. Chairman, as I understand Senator  
15 Chafee's amendment, he is proposing to permit IRAs to exist.  
16 John, for everybody?

17 Senator Chafee. For everybody.

18 Senator Heinz. Whether or not they were in a pension  
19 plan?

20 Senator Chafee. Whether or not they are in a pension  
21 plan, but not deductible. The contribution is not deductible.

22 Senator Heinz. I understand.

23 Senator Matsunaga. And has the Senator offered an  
24 amendment, or is this just discussion?

25 Senator Chafee. I am offering it.

1 Senator Heinz. Senator Chafee has offered an amendment  
2 and it would permit anybody, whether or not they were in a  
3 pension plan, to have a IRA. It would not be a deductible  
4 IRA, but you would preserve the inside buildup, as I understand  
5 it; and that would be free from taxation.

6 Now, I must say I have been looking for a way to offer  
7 --as you know because we have discussed this on many  
8 occasions--I have been looking for a way to do exactly the  
9 same thing.

10 We both want to preserve at the very minimum IRAs and  
11 their inside buildup, even if we don't know how to afford  
12 the entire deductibility of them.

13 But on this, I have some reservations about how you  
14 propose to pay for it because what you are proposing is  
15 to reduce the limit on 401(k)s.

16 Now, superficially, it sounds attractive, if you are  
17 permitting only a \$2,000 contribution annual to an area that  
18 is not deductible--it is not deductible--and you are limiting  
19 the amount that anybody can put in to a 401(k).

20 The logical kind of common sense reaction to that is:  
21 Well, that \$2,000 ought to help the little guy, and it is  
22 the big guy who benefits from the \$7,000 maximum contribution  
23 for a 401(k).

24 I have been doing a little work in this area, and for  
25 better or for worse, I have some facts that contradict what

1 would be the conventional wisdom.

2 The Chairman. Let me interrupt just a moment to indicate  
3 at least to the staff that is here: You might want to inform  
4 your bosses. This is a relatively significant philosophical  
5 and important amendment.

6 To the extent they are around, they may want to listen  
7 to this. I think they are going to want to be recorded,  
8 in any event.

9 Senator Chafee. Yes, Mr. Chairman. It is my intention  
10 to have a record vote on this, and it is something that we  
11 have discussed and thought about and in our sessions talked  
12 about.

13 I would think it would be splendid if those who are  
14 absent could be here, could be present.

15 Senator Grassley. Could the chairman also give us an  
16 update? Where are we on what Senator Roth proposed?

17 The Chairman. He withdrew it.

18 Senator Grassley. Does that mean that he has withdrawn  
19 it forever?

20 The Chairman. No. That was the funding of the full  
21 IRAs with gasoline taxes.

22 Senator Grassley. He withdrew it for what reason?

23 The Chairman. I think because, had it gone to a vote,  
24 it would have been pretty badly defeated because it was funded  
25 with a 6.5 cent gasoline tax increase.

1 And he preferred not to push it at that time. He more  
2 or less reserved his right to bring it back with some other  
3 funding mechanism or in some other form.

4 Senator Grassley. But the chairman doesn't know if he  
5 is going to bring that back up?

6 The Chairman. No, I don't know if he is going to or not;  
7 but he did not pursue it to a vote.

8 Senator Heinz. Now, as I said at the outset, like  
9 Senator Chafee, I would like to find a way to do exactly  
10 what he proposes to do.

11 But if the assumption here is that IRA participation  
12 does a better job of getting benefits to the lower paid than  
13 401(k) participation, I have here a booklet published by  
14 the Employee Benefits Research Institute, March 1986.

15 Here is what it says: It says that for workers  
16 participating in a 401(k) plan, --excuse me--

17 "Among those workers offered a 401(k) plan, 20 percent  
18 of those earning between \$5,000 and \$9,000 and \$10,000  
19 participate.

20 "IRA participation is 8.5 percent--less than half. For  
21 workers between \$10,000 and \$15,000, 28 percent participate  
22 in 401(k)s; only 11.1 percent participate in IRAs.

23 "For workers between \$15,000 and \$20,000, 33.7 percent  
24 participate in a 401(k); 17.3--about half--participate in  
25 an IRA.

1 "Between \$20,000 and \$25,000, about 39.9 percent  
2 participate in a 401(k); and 20 percent participate in IRAs."

3 And those differentials remain and only get close once  
4 you get above \$50,000. So, what you are seeing is workers  
5 below \$25,000 have a participation rate in 401(k)s that is  
6 about twice that for IRAs.

7 Now, you can say why would dropping the maximum amount  
8 that somebody could contribute to an IRA from \$7,000 to \$5,000  
9 --why would it have that much effect?

10 Well, there will be, I submit, because of the complex  
11 nondiscrimination rules that we apply to 401(k)s--obviously,  
12 no IRAs are subjected to nondiscrimination rules.

13 The net result, I fear--I fear--and it is a judgment I  
14 think each Senator is going to have make is that employers  
15 will drop their matching contributions and efforts to  
16 educate employees to participate in 401(k)s.

17 We have to remember that 401(k)s are not like a defined  
18 benefit or a defined contribution plan established by the  
19 employer in which everybody participates.

20 They are elected by the employee. And often, the employer  
21 will have a match in order to encourage the employee to  
22 participate. A 401(k) is also known as a CODA, a cash or  
23 deferred arrangement plan.

24 So, the employee has to give up something. The employee  
25 has to give up salary or wages here and now to put it into

1 the plan.

2 Now, what I fear is that contributions by lower paid  
3 workers, if we go from \$7,000 to \$5,000, would drop.

4 Now, Mr. Chairman, I trust the committee will forgive  
5 what is inherently a very complicated explanation of the  
6 nondiscrimination rules, but if we don't understand at least  
7 in general the way the nondiscrimination rules work, it  
8 won't be understandable to people why simply going from  
9 \$7,000 to \$5,000 could have a very serious effect, ironically,  
10 on lower paid workers.

11 But the essence of it is that the nondiscrimination rules  
12 for 401(k)s require you to divide your work force into a  
13 top third and a two-thirds--bottom two-thirds.

14 And then, if you want to pass the nondiscrimination test,  
15 the percentage of deferral of the total compensation of the  
16 workers in the top third, as a percentage--the amount  
17 deferred is a percentage of their total compensation--cannot  
18 exceed that of the bottom two-thirds by more than 150 percent.

19 I trust everybody fully understands that calculation.  
20 It took me weeks to understand it.

21 The result of having this kind of change is that the  
22 bottom two-thirds workers will not be encouraged to contribute  
23 as much to the 401(k)s; and as a result, they will get less.

24 If you really want to oversimplify it, just think that  
25 what the bottom two-thirds gets is proportional on a

1 complicated formula, but proportional to what the top  
2 one-third gets.

3 So, when you lower what the top one-third gets, you  
4 in effect lower management incentives to make sure that  
5 the lower two-thirds participate, which incentives come in  
6 the form either of education or in the form of employer  
7 matching.

8 So, Senator Chafee's amendment poses, I think, a  
9 difficult choice for members. I am convinced, although I  
10 will freely admit that none of us can prove what the result  
11 of it is going to be; but it is not on balance going to be  
12 of benefit to middle and lower income workers.

13 And since most people who establish IRAs are upper  
14 income, I suspect I have a pretty good case in that regard.

15 Again, I just want to say that I am in a very difficult  
16 position, Mr. Chairman, because I really want to do what  
17 Senator Chafee is doing, but I don't want to do it at the  
18 expense of 401(k)s.

19 And I find myself very uncomfortable arguing against his  
20 amendment, but I have.

21 Senator Matsunaga. Mr. Chairman?

22 The Chairman. Senator Matsunaga, and then back to  
23 Senator Chafee.

24 Senator Matsunaga. Mr. Chairman, for the reasons so  
25 effectively presented by Senator Heinz, I too must oppose



1 the amendment offered by Senator Chafee.

2 And just as I was in full support of the preservation of  
3 IRAs when Senator Roth offered his amendment, it is the  
4 method in which the Senator proposes to pay for it that  
5 I am solidly opposed to because, as you know, we already  
6 lowered the maximum amount from \$12,000 to \$7,000.

7 That is, Senator Grassley's amendment was adopted  
8 initially, raising the amount from \$7,000 to \$12,000. We  
9 lowered it down to \$7,000; and as was stated by Senator  
10 Heinz, we find that the 401(k) plan serves the lower income  
11 bracket much more than the upper income bracket.

12 And I think it would be--although I am in full support  
13 of preserving IRAs--that it would be wrong to do as he  
14 proposes to do by lowering the \$7,000 to \$5,000; and I  
15 strongly urge my colleagues to vote against the Senator's  
16 amendment.

17 Senator Chafee. Mr. Chairman?

18 The Chairman. Senator Chafee?

19 Senator Chafee. Mr. Chairman, I am prepared to hear many  
20 arguments against 401(k)s--against my amendment--but to  
21 suggest that the lower income people are going to be affected  
22 by this, I just think it doesn't add up.

23 I mean, they are going to be-- How many lower income  
24 people are going to be able to set aside \$5,000? And to  
25 suggest that the lower income people are somehow going to be

1 affected by this, I just think doesn't add up.

2 I listened to that complicated explanation by Senator  
3 Heinz, and he mentioned he felt uncomfortable with it; and  
4 I guess I can see why, because it just didn't--in my judgment  
5 --add up. It didn't make sense--to put it bluntly--it didn't  
6 make sense.

7 It is the contribution of the employee that figures in  
8 here. It is not what the employer accounts for. If the  
9 employer wants to triple it and make it \$14,000 for a total  
10 of \$21,000 or three times the five, make it a total of \$15,000,  
11 three cheers.

12 It is the employee's contribution that we are limiting.  
13 And if anybody can say that we are hurting somehow by  
14 restricting the lower income employee to a \$5,000 contribution,  
15 I regretfully have trouble comprehending that.

16 The Chairman. Senator Mitchell?

17 Senator Mitchell. Mr. Chairman, I would like to express  
18 my support for Senator Chafee's amendment, and I would like  
19 to ask Senator Heinz: In the explanation you read from a  
20 report a table which showed percentage participation by  
21 income classes of persons eligible for both 401(k) and IRAs.  
22 Is that correct?

23 Senator Heinz. No. I read from a table that shows the  
24 percentage of the work force participating in 401(k)s and a  
25 table of participation of the work force in IRAs.

1 Senator Mitchell. Oh, I see. All right.

2 Senator Heinz. Now, what you will find, and maybe Senator  
3 Chafee if he doesn't understand the demographics of his  
4 amendment, maybe I can put it to him simply.

5 There are 11 million workers participating in 401(k)s  
6 who are earning \$25,000 or less; and they have an average  
7 deferral of \$1,100.

8 Under his amendment, that deferral will drop  
9 substantially. People earning more than \$25,000 are going  
10 to be the ones who have the money to put into an IRA. IRA  
11 is not a salary reduction plan, the way it is going to be  
12 here.

13 And maybe this explanation is not too complicated; but,  
14 Senator, your amendment is going to hurt the little guy and  
15 help the big guy who will have the money to put into an IRA.  
16 It is that simple.

17 Senator Mitchell. Is this still in answer to my  
18 question?

19 Senator Heinz. I did answer your question, and I must  
20 say I did elaborate slightly on it, and I thank you for  
21 being so patient.

22 The Chairman. Are we ready to vote?

23 Senator Mitchell. I was going to make an argument,  
24 Mr. Chairman, but I will just say that I support Senator  
25 Chafee's position.

1 I just want to note that I think Senator Heinz was  
2 careful not to argue that persons below \$25,000 have available  
3 to set aside more than \$5,000. He was very careful to say  
4 that.

5 What he said was that if you reduce the benefit to  
6 persons in the higher income category--that is the one-third  
7 classification--you will inevitably reduce the benefits  
8 available at the lower level.

9 It does not of course necessarily follow that the benefits  
10 will be reduced at the higher classification. All that you  
11 are suggesting is that that is an option that will be  
12 increasingly available to those who establish the plans in  
13 management at the upper income levels.

14 On the other hand, I think the figures you read really  
15 establish significantly a case for Senator Chafee's amendment  
16 because, as you pointed out in your argument, the 401(k)s  
17 are frequently supplemented by contributions by the employer.

18 And the IRAs, of course, are not. Notwithstanding that  
19 enormous inducement to participate in 401(k)s, the figures  
20 really are not surprising.

21 In fact, I think the reverse could be argued as surprising  
22 that so many do participate --

23 Senator Heinz. Mr. Chairman, I have a --

24 The Chairman. Senator Heinz, you what?

25 Senator Heinz. I have a substitute for Senator Chafee's

1 amendment.

2 The Chairman. That is in order.

3 Senator Heinz. Which is the first part of his amendment  
4 without the second part.

5 It is a non-revenue neutral amendment. I have the sense  
6 that the committee wants to have inside buildup on IRAs.

7 The Chairman. A non-revenue neutral amendment is out  
8 of order, though.

9 Senator Heinz. Under what circumstances?

10 The Chairman. By the amendment we adopted earlier that  
11 all amendments have to be revenue neutral.

12 Senator Heinz. Maybe I missed something. When did we  
13 adopt that?

14 The Chairman. It was about 10:30 this morning, or 11:00  
15 this morning.

16 Senator Heinz. Did we have a recorded vote on that?

17 The Chairman. As a matter of fact, there were about 16  
18 or 17 people here. There was not a recorded vote. There  
19 were no objections.

20 Senator Heinz. Was it posed as a rule?

21 The Chairman. It was an amendment offered by Senator  
22 Chafee, seconded by Senator Mitchell.

23 Senator Heinz. What I might do is move, for the purpose  
24 of this amendment, that we waive the rule.

25 The Chairman. Say that again.

1 (Laughter)

2 Senator Heinz. I think the chairman heard exactly what  
3 I said. I said for the purposes of this amendment, we  
4 would waive the rule.

5 The Chairman. You can move to reconsider the vote this  
6 morning, but I think waiving the rule would be out of order.

7 Senator Heinz. Mr. Chairman, in all fairness, it is  
8 not a committee rule. Whatever it was we did was by majority  
9 vote, and it can be undone by majority vote.

10 The Chairman. It wasn't a rule. It was an amendment  
11 we adopted this morning.

12 Senator Heinz. And any amendment can be undone by a  
13 majority vote.

14 Senator Danforth. Mr. Chairman, I think both sides have  
15 a very good argument with respect to the Chafee amendment,  
16 but I really think that we attempted to establish this morning  
17 a rule that would guide us throughout consideration of this  
18 bill.

19 And if we are going to waive the rule, item by item, then  
20 it has no meaning whatever. I don't know what the  
21 parliamentary situation is here, but I would hope that we  
22 would not proceed on an amendment-by-amendment basis to  
23 simply waive a rule that was going to guide our proceedings  
24 for the balance of consideration of this bill.

25 Senator Grassley. Mr. Chairman, you know, I buy Senator

1 Heinz' arguments against the Chafee amendment, but I would  
2 not want to change either the rule or the procedure or  
3 whatever it is.

4 And I would urge that we would not. I think that it is  
5 going to make us be responsible in our approach of adopting  
6 amendments. It is going to work to my detriment on a couple  
7 of amendments I am going to offer yet today.

8 But I think, in order to keep some orderly process here,  
9 we have to keep the revenue neutrality of the amendments.

10 Senator Heinz. Mr. Chairman, I will withdraw my  
11 substitute, but I want it understood that I think there is  
12 nothing to prevent a member from doing what I proposed to do,  
13 which is by majority vote waive with respect to a specific  
14 amendment.

15 And I think the chair would agree with that. Before I  
16 withdraw it, would the chair not agree that it is in order  
17 to do that?

18 The Chairman. I would want to consult before I would  
19 agree with this.

20 Senator Heinz. Well, then, I will just hold on to my  
21 amendment, until you consult.

22 The Chairman. At the moment, we are on his amendment.

23 Senator Heinz. Yes, and my substitute is pending to it.

24 The Chairman. All right. Let's put it to a vote.

25 Senator Heinz. Mr. Chairman, I am asking a question of

1 parliamentary procedure.

2 The Chairman. Because we did not reconsider and table,  
3 we are bound by the Senate rules to the extent that they  
4 are in harmony--we did not do that this morning.

5 Whereas on the Senate floor, that would preclude it  
6 from being reconsidered; so I think it can be reconsidered  
7 in the form of asking that we reconsider it for this  
8 amendment.

9 Senator Heinz. All right. Since we have established  
10 that, I am not going to press my amendment.

11 The Chairman. Senator Chafee, are you ready to vote?

12 Senator Chafee. I just want to say, Mr. Chairman, that  
13 I have a table here from the Joint Economic Committee which  
14 says that IRAs are used by those with adjusted gross incomes  
15 less than \$10,000, 4.7 percent; \$10,000 to \$20,000, 14.6  
16 percent; \$20,000 to \$30,000, 21 percent; and \$30,000 to  
17 \$40,000, 21 percent.

18 So, Mr. Chairman, we also know that far more IRAs-- I  
19 think the statistic given by Senator Roth was that--was it  
20 28 million? I don't have that specific figure. As I recall  
21 there were 28 million people who had IRAs in the United States.

22 And here is a chance, Mr. Chairman, to do something for  
23 that group. It is a modest something, but it is something;  
24 and particularly as we can see, many of these people are in  
25 the lower income brackets.



1 Without doing any harm, I am convinced, to those that  
2 have 401(k)s; so I would move my amendment, Mr. Chairman.

3 Senator Matsunaga. You would --

4 Senator Grassley. Mr. Chairman?

5 The Chairman. Who seeks recognition?

6 Senator Grassley. Grassley.

7 The Chairman. Oh, Senator Grassley.

8 Senator Grassley. Yes. You had earlier urged members  
9 to be here. This is such a key vote. I wonder, as you urged  
10 the members to be here to hear these arguments, if we can't  
11 either get the members here or put this off until they can  
12 be here, because this is quite a departure from what this  
13 committee has done previously.

14 Senator Matsunaga had already referred to a vote  
15 previously on an amendment that I had adopted in which we  
16 actually increased from \$7,000 to \$12,000 in the limit.

17 And now, we have an effort here that is going to take  
18 that limit down from \$7,000, down further yet to \$5,000.  
19 And it would seem to me like this is a significant departure  
20 from this committee had previously voted for, that members  
21 ought to take note of it.

22 And also, when considered in conjunction with what  
23 existing law is, nobody would argue any more that existing  
24 law ought to be maintained.

25 But to go from \$30,000 down to \$7,000 and then back to

1 \$12,000 and now down to \$5,000, with just five or six members  
2 here, when we had a full house when we voted on this  
3 previously, I would ask that the chairman would hold off the  
4 vote on this until everybody could be here.

5 The Chairman. There is a group of Senators meeting in  
6 back. Six of them have sent in proxies. They are about  
7 split on it, but they have sent in proxies on this and know  
8 that it is in discussion.

9 Senator Grassley. It is quite obvious that they didn't  
10 hear the arguments.

11 The Chairman. No.

12 Senator Chafee. I am not so sure they didn't hear the  
13 arguments.

14 Senator Grassley. Have you ever been in the back room  
15 and tried to listen to the arguments?

16 (Laughter)

17 Senator Chafee. Mr. Chairman, for better or for worse,  
18 I would like to vote. We sent out the word previously.  
19 You gave the message to the aides that are here, and there  
20 is a plethora of them, to alert the Senators.

21 And up or down, I would like a roll call vote.

22 Senator Heinz. Mr. Chairman, a question. The chair has  
23 been very silent on this. Does the chair have a position on  
24 this amendment?

25 The Chairman. I intend to support Senator Chafee.

1 Senator Heinz. May I ask the staff? What is the cost  
2 of this amendment again?

3 Mr. Brockway. This is essentially revenue neutral. I  
4 think it maybe picks up --

5 Senator Heinz. What is it on Senator Chafee's inside  
6 buildup on IRAs? What is the cost of that that is offset  
7 by the 401(k)?

8 Mr. Brockway. I think that both numbers are approximately  
9 \$1.6.

10 Senator Heinz. And what do we get by extending the  
11 telephone excise tax, that would otherwise expire?

12 Mr. Brockway. If you had extended it at the three  
13 percent rate, that would be \$8.8 billion over the period.

14 Senator Heinz. So, how do I get \$1.6?

15 Mr. Brockway. You can either extend it at a rate --

16 Senator Heinz. I just wonder. How many months do I  
17 have to extend it at three percent?

18 Mr. Brockway. It would be something like eight months.

19 Senator Heinz. Mr. Chairman, I have a substitute for  
20 Senator Chafee's amendment, which would do what he wants to  
21 do on IRAs and extend the three percent telephone tax for  
22 eight months.

23 The Chairman. I am going to ask staff again. We have  
24 11 members. We are going to vote on the substitute and  
25 extending the telephone tax to finance this. And I sense

1 we will call the roll relatively soon.

2 Senator Grassley. Mr. Chairman?

3 The Chairman. Senator Grassley? I am not trying to  
4 force the vote; I just want the members in the back room  
5 and elsewhere to be alert that the method of financing has  
6 been changed, or a suggested change.

7 Senator Grassley. First of all, some question about  
8 revenue here. What is the number that you are raising from  
9 401(k)s by going down from \$7,000 to \$5,000?

10 Mr. Brockway. I think it is about \$1.5 billion if we  
11 go from \$7,000 to \$5,000. It is also about \$1.5 billion  
12 to give to nondeductible IRAs for employees that are not  
13 qualifying for the \$2,000 --

14 Senator Grassley. So, we are going to raise \$1.5 billion  
15 by reducing the 401(k) from \$7,000 to \$5,000; and then, that  
16 is going to be offset by allowing the interest that  
17 accumulates on IRAs, the \$2,000 will be taken under there?

18 Mr. Brockway. That was Senator Chafee's amendment.  
19 Senator Heinz has a substitute now. In lieu of paying for  
20 it that way, to do it through the telephone excise tax.

21 Senator Grassley. All right, but I am leading to a  
22 question. I want to know-- That figure of \$1.5 billion  
23 just does not square with a figure that was given to me  
24 yesterday, that if you go from \$7,000 to \$12,000 that the  
25 estimate of that is only about \$1 billion.

1 Mr. Brockway. It is not at all linear, Senator. The  
2 lower the limit gets, very few people put in more than,  
3 let's say--of total participants in IRAs--very few people  
4 put in more than, let's say, \$5,000.

5 You have a situation. One is you are limited to 25  
6 percent of pay, so anybody making less than \$25,000 isn't  
7 even allowed to put in more than \$5,000.

8 But then as you go up, you have to have a substantial  
9 amount of money to give \$6,000--even more money to give  
10 \$7,000--in terms of how much disposable income you have left.

11 So, between \$7,000 and \$12,000, there would be a pretty  
12 quick drop-off. As you go down below \$5,000, the revenue  
13 begins to pick up more and more. So, it is a sliding scale.

14 Senator Mitchell. Mr. Chairman?

15 The Chairman. Senator Mitchell?

16 Senator Mitchell. Mr. Chairman, I would hope that  
17 Senator Chafee and yourself would oppose this substitute  
18 amendment.

19 I spoke in favor of Senator Chafee's proposal because I  
20 thought it made sense to do and the method proposed to finance  
21 it. But once again, we are back to a mechanism which  
22 increases taxes unrelated to ability to pay on an essential  
23 service.

24 It bears heaviest on the poorest in our society, as a  
25 means of paying for something that provides a special benefit

1 for--while admittedly large numbers--nonetheless clearly  
2 those certainly in the upper middle and higher income classes.

3 And it is just unfair to do that. And I would hope that  
4 those who support Senator Chafee's amendment will see this  
5 substitute for what it is--an effort to kill it--and defeat  
6 this substitute and then vote squarely on the Chafee  
7 amendment as proposed.

8 I hope very much that we don't go down that path. I  
9 spoke about it earlier. I won't repeat myself. We have  
10 been doing it now for five years--raising taxes unrelated  
11 to ability to pay, which bear heaviest on the poor, so that  
12 we can reduce taxes based on ability to pay, which benefit  
13 the wealthy.

14 And this is another effort to go down that course, and  
15 I do urge that this substitute be defeated for that purpose  
16 and that we vote squarely on the merits of the Chafee  
17 amendment.

18 Senator Chafee. Mr. Chairman, I second everything the  
19 Senator said.

20 The Chairman. Question is on --

21 Senator Grassley. Mr. Chairman?

22 The Chairman. Senator Grassley?

23 Senator Grassley. All right. I want to ask a question  
24 on the intent on the part of Senator Chafee.

25 Now, you say that the goal you seek here is people who

1 are not vested can then have an IRA and then save it that  
2 way and not have the interest taxable.

3 What about the people who are just covered by a 401(k)  
4 but not vested? Is it your judgment that they should qualify  
5 for your IRA?

6 Senator Chafee. I don't know what the term "not vested  
7 in a 401(k)" is. I think as soon as you put into a 401(k),  
8 it is per se vested. There is no vestment problem in  
9 connection with a 401(k).

10 Senator Heinz. But I think what Senator Grassley is  
11 asking is: If you are participating in a 401(k) or covered  
12 by a defined benefit or defined contributions plan, I think  
13 is the substance of his question.

14 Senator Chafee. Oh, sure. Sure, you could use this--  
15 nondeductibly.

16 The Chairman. Further discussion?

17 Senator Heinz. Mr. Chairman, I do have one question of  
18 staff. What proportion of the telephone excise tax is paid  
19 by corporations?

20 Mr. Brockway. I simply don't know the answer to that,  
21 Senator.

22 Senator Heinz. My understanding is that it is a  
23 relatively high proportion.

24 Mr. Brockway. Again, I simply don't know.

25 Senator Heinz. It is something like two-thirds corporate,

1 one-third individual.

2 Mr. Brockway. I think a meaningful proportion of it,  
3 but I have no idea whether it is more or less than half.  
4 I can find that out.

5 Senator Heinz. I think, therefore, it can be argued  
6 quite rightly that-- How soon can we find out that  
7 information? We think it is a substantial proportion. You  
8 think it is a substantial proportion.

9 Mr. Brockway. I know it is a very meaningful proportion.  
10 Whether it is more or less than half, I don't know.

11 Senator Heinz. Let's do this. I am going to modify  
12 my amendment to pay for this by extending the excise tax.  
13 I don't imagine it will extend for much more than 16 months,  
14 just on the corporate portion of the telephone excise tax.

15 Mr. Brockway. It would just be corporate then --

16 The Chairman. Extend it far enough that it will cover  
17 the cost of the amendment. If that is 18 months or 14  
18 months --

19 Senator Heinz. Yes, whether it be 14 or 18 --

20 Mr. Brockway. Just so you --

21 Senator Heinz. Because I want to address George  
22 Mitchell's concern. It is my concern, too. What I am  
23 trying to do, and I think the Senator from Maine understands  
24 what I am trying to do, and I am not against what Senator  
25 Chafee is trying to do--I just don't want to see people in



1 the 401(k)s--and it is not the top one-third I am worried  
2 about; it is the bottom two-thirds I am worried about here.

3 So, I am trying to find a nonregressive way to pay for  
4 John Chafee's amendment. I hope you people will view it  
5 as a friendly amendment.

6 Senator Mitchell. No, I understand that, Senator, and  
7 I don't think there is any question as to what your intention  
8 or motive was. I merely wanted to raise that point about the  
9 excise taxes.

10 Mr. Brockway. We would need a fair degree of drafting  
11 authority on that, Senator. The difficulty is that the  
12 current tax is imposed on everyone, and so the telephone  
13 company doesn't need to know who its customer is. Clearly,  
14 it is better --

15 Senator Heinz. Unless it is you?

16 Mr. Brockway. Right.

17 Senator Heinz. And then they know.

18 Mr. Brockway. It is clearly better that the  
19 differentiation be between corporate and noncorporate, rather  
20 than business and nonbusiness because that distinction, one  
21 couldn't do.

22 Senator Heinz. What if we make it corporate and  
23 noncorporate?

24 Mr. Brockway. Hopefully, we can draft it in a way that  
25 it would be administrable so that it would be only corporate

1 users who would be subject to the tax.

2 And then, there would be obviously some period you could  
3 extend it through that would make this revenue neutral. And  
4 as long as we have sufficient drafting authority --

5 Senator Heinz. That is the way, Mr. Chairman, I would  
6 want my amendment to so state.

7 The Chairman. It is so amended.

8 Senator Chafee. Mr. Chairman, let me just say once  
9 again that we have got a lot of deficit reduction we have  
10 got to do, hopefully. We have got a budget that we have  
11 to raise revenue for, and I think we make a great mistake  
12 in this committee to start funding tax reform measures on  
13 the basis of new revenue that we currently don't have or  
14 that is destined to drop and that we are looking for for  
15 some other reason.

16 And for that reason, I would hope that this would not  
17 be approved, regardless of whether it is --

18 The Chairman. The clerk will call the roll on the  
19 amendment, as amended, to finance the extension by the  
20 extending the corporate side of the telephone excise tax  
21 a sufficient period of time to pay for the cost of the  
22 amendment. Those in favor will say "Aye," those opposed "No."

23 The clerk will call the roll.

24 The Clerk. Mr. Dole?

25 (No response)

- 1 The Clerk. Mr. Roth?  
2 (No response)  
3 The Clerk. Mr. Danforth?  
4 Senator Danforth. No.  
5 The Clerk. Mr. Chafee?  
6 Senator Chafee. No.  
7 The Clerk. Mr. Heinz?  
8 Senator Heinz. Aye.  
9 The Clerk. Mr. Wallop?  
10 (No response)  
11 The Clerk. Mr. Durenberger?  
12 Senator Durenberger. Aye.  
13 The Clerk. Mr. Armstrong?  
14 (No response)  
15 The Clerk. Mr. Symms?  
16 (No response)  
17 The Clerk. Mr. Grassley?  
18 Senator Grassley. Aye.  
19 The Clerk. Mr. Long?  
20 (No response)  
21 The Clerk. Mr. Bentsen?  
22 (No response)  
23 The Clerk. Mr. Matsunaga?  
24 Senator Matsunaga. Aye.  
25 The Clerk. Mr. Moynihan?

1 Senator Moynihan. No.

2 The Clerk. Mr. Baucus?

3 (No response)

4 The Clerk. Mr. Boren?

5 (No response)

6 The Clerk. Mr. Bradley?

7 (No response)

8 The Clerk. Mr. Mitchell?

9 Senator Mitchell. No.

10 The Clerk. Mr. Pryor?

11 (No response)

12 The Clerk. Mr. Chairman?

13 The Chairman. No. And Senator Roth is "No."

14 Senator Grassley. Now, I would move my amendment, Mr.

15 Chairman.

16 The Chairman. Wait until she announces it.

17 The Clerk. Four yeas; seven nays.

18 The Chairman. The amendment is defeated.

19 The vote is now on the Chafee amendment as proposed,

20 which would drop the 401(k)s to \$5,000. Right?

21 The clerk will call the roll.

22 The Clerk. Mr. Dole?

23 The Chairman. Aye, by proxy.

24 The Clerk. Mr. Roth?

25 (No response)

1 The Clerk. Mr. Danforth?  
2 Senator Danforth. Aye.  
3 The Clerk. Mr. Chafee?  
4 Senator Chafee. Aye.  
5 The Clerk. Mr. Heinz?  
6 Senator Heinz. No.  
7 The Clerk. Mr. Wallop?  
8 (No response)  
9 The Clerk. Mr. Durenberger?  
10 Senator Durenberger. No.  
11 The Clerk. Mr. Armstrong?  
12 (No response)  
13 The Clerk. Mr. Symms?  
14 (No response)  
15 The Clerk. Mr. Grassley?  
16 Senator Grassley. No.  
17 The Clerk. Mr. Long?  
18 (No response)  
19 The Clerk. Mr. Bentsen?  
20 Senator Chafee. Aye, by proxy.  
21 The Clerk. Mr. Matsunaga?  
22 (No response)  
23 The Clerk. Mr. Moynihan?  
24 Senator Moynihan. Aye.  
25 The Clerk. Mr. Baucus?

1 Senator Chafee. Aye, by proxy.

2 The Clerk. Mr. Boren?

3 Senator Chafee. Aye, by proxy.

4 The Clerk. Mr. Bradley?

5 Senator Bradley. Aye.

6 The Clerk. Mr. Mitchell?

7 Senator Mitchell. Aye.

8 The Clerk. Mr. Pryor?

9 Senator Chafee. Aye, by proxy.

10 The Clerk. Mr. Chairman?

11 The Chairman. Aye.

12 Roth is "No"; Wallop is "No"; Armstrong is "No"; Symms

13 is "No."

14 Senator Heinz. Are those available on the previous  
15 vote, Mr. Chairman?

16 The Chairman. No. They were not. I just go as the  
17 staff instructs me on them.

18 Wait a minute; wait a minute.

19 What is the roll call?

20 The Clerk. Eleven yeas; eight nays.

21 The Chairman. The amendment is adopted. Further  
22 amendments?

23 Are there any further amendments?

24 Senator Moynihan. Mr. Chairman, could I say that I  
25 believe we are working out an arrangement on the net

1 operating loss for thrifts. It is going to be revenue  
2 neutral, but we are not quite there.

3 The Chairman. Thank you. Are there any further  
4 amendments?

5 Senator Mitchell. Mr. Chairman, as you know, the members  
6 of my staff and I have been working with the Joint Committee  
7 staff and the Treasury on a low income housing amendment.

8 And we are trying to get some better revenue numbers.  
9 I am not ready with it yet, but I will be in the very near  
10 future.

11 The Chairman. I would suggest we take about a 25-minute  
12 break then right now. About 25 minutes; come back at 5:15  
13 p.m.

14 (Whereupon, at 4:51 p.m., the meeting was recessed.)  
15  
16  
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1 AFTER RECESS

2 (11:19 p.m.)

3 The Chairman. The committee will come to order, please.

4 With the exception of I think two amendments that will be  
5 voted on here, we have, I think, reached agreement on a  
6 package. I am going to ask the Joint Committee to present the  
7 package.

8 Why don't you start with the revenue-losing provisions?  
9 Let me go down some of them, Dave, and you can correct me if  
10 I am wrong and add others that I may have forgotten on the  
11 list. These are the revenue-losing provisions:

12 We have eliminated the requirement that the state and  
13 local governments report to the Federal Government on the  
14 collection of local income taxes -- \$50 billion.

15 Transitional rules -- \$5.5 billion.

16 Technical corrections -- \$400 million.

17 Low-income housing -- what was the figure we finally  
18 ended up with?

19 Mr. Brockway. That was deleted from the package,  
20 Mr. Chairman.

21 The Chairman. We went to spreadsheet, though, as I  
22 recall.

23 Mr. Brockway. You went to the spreadsheet as modified  
24 in your package that you distributed this morning.

25 The Chairman. All right.



1 The housing cooperatives -- \$50 million.

2 The title insurance -- \$50 million

3 The repeal of FIRPTA -- \$1.6 billion.

4 The earned income credit -- \$1.2 billion, because when  
5 we round it down to the nearest \$50, we did not mean to include  
6 the earned income credit.

7 Mr. Brockway. Mr. Chairman, I believe that was \$700  
8 million.

9 The Chairman. That's right. I take it back.

10 Adoption expenses -- \$30 million.

11 Agricultural bonds -- \$50 million.

12 The repeal, the separate mailing of the 1099s -- \$50  
13 million.

14 The at-risk equity participating exception -- \$50 million.

15 Treating farm credit like production credit, associations,  
16 like other financial institutions -- \$100 million.

17 Moving the 401(k) limits back up to 7000, \$1.4 million.

18 The banquet exception on the 80-percent for meals and  
19 entertainment -- \$100 million.

20 The single-purpose? We left the single-purpose  
21 agriculture at 10 years, didn't we?

22 Mr. Brockway. Correct.

23 The Chairman. And the builder bonds, what did we do at  
24 the end on the builder bonds?

25 Mr. Brockway. That remained as in the mark; there would

1 be no delay.

2 The Chairman. No delay. We took out any delay.

3 Mr. Brockway. Correct.

4 The Chairman. Then we had targeted jobs credit of about  
5 a billion?

6 Mr. Brockway. That is a \$1.3 billion total.

7 The Chairman. One-point-three billion.

8 We had the passive loss. That was a self-contained, the  
9 five-year or four-year phase out, depending on how you count  
10 it.

11 Mr. Brockway. Correct.

12 The Chairman. But it was self-contained, so that there  
13 was no revenue loss on that. And then working interest of  
14 about \$1.4 billion.

15 Mr. Brockway. Correct.

16 The Chairman. Now, have I left anything out on the  
17 revenue-losing provisions?

18 Mr. Brockway. One, I don't think you read off Medivac  
19 helicopters.

20 The Chairman. Oh. I apologize. That's right. That is  
21 \$10 million.

22 Mr. Brockway. There is a set of proposals dealing with  
23 (1) mailing lists of veterans' associations, installment sales  
24 of vacation homes, and failing thrifts, allowing a casualty  
25 loss that would be paid for with an extraordinary-dividend

1 deduction provision. That was from the spreadsheet, and it  
2 was part of the package.

3 Also, that nonprofit corporations would be allowed to have  
4 401(k)s.

5 There was a self-contained package dealing with thrift  
6 institutions -- (1) allowing additional carryforward for  
7 thrifts with a compensating payment in that area, dealing  
8 with bad debt reserves.

9 The Chairman. Is that it?

10 Mr. Brockway. That is my list, Mr. Chairman.

11 The Chairman. All right. Now, let me go through the  
12 revenue raising. How much does that come to?

13 Mr. Brockway. It is 14.6, I believe.

14 The Chairman. All right.

15 Now let me go through the revenue-raising provisions as  
16 I have them, and you correct me if I'm wrong:

17 Repeal of the investment tax credit, effective January 1,  
18 1986 -- 6.2.

19 Raise the substantial-underpayment penalty from 10 to  
20 20 percent -- .9.

21 IRS voluntary tax payment programs -- .2.

22 Limit the business tax credits to offset 50 percent of  
23 the regular tax, which was the 1975 law -- \$2 billion.

24 Require current recognition of cancellation of indebted-  
25 ness income of insolvent businesses -- .3.

1 Place computers and telephone switching equipment in the  
2 five-year class -- 2.3.

3 Delete deduction for health insurance, self-employment,  
4 from the self-employment tax -- 1.1.

5 Require a Section 338 basis-allocation rule to apply to  
6 all acquisitions, one, and take the pace-off credit back to  
7 January 1, 1987 -- \$1 billion.

8 Now, what does that come to?

9 Mr. Brockway. Mr. Chairman, there was also, I believe,  
10 the repeal of political contributions credit.

11 The Chairman. That is correct. I forgot. That's  
12 a billion.

13 Mr. Brockway. Did you read off financial institutions on  
14 the accrual method?

15 The Chairman. Five hundred million.

16 Mr. Brockway. Trademark and trade name --

17 The Chairman. A hundred million.

18 Mr. Brockway. -- five-year amortization.

19 Royalty reporting was \$100 million.

20 Computer schedule switching equipment in the three-year  
21 class I believe you read.

22 Senator Bentsen. But that was nothing like the \$2  
23 billion. I thought they went back and corrected that estimate.

24 The Chairman. No. We had it at two to three, and they  
25 held it at two.

1 Mr. Brockway. No, Mr. Chairman; Senator Bentsen is  
2 correct on that.

3 The Chairman. Oh, you are right -- my mistake. That's  
4 off altogether, because it didn't produce any money at all.

5 Senator Bentsen. That is correct.

6 The Chairman. Lloyd, you are right. I apologize.

7 Senator Bentsen. Just a little matter of \$2 billion.

8 The Chairman. Well, but we picked it up someplace else.

9 Senator Chafee. Mr. Chairman, during the gap here, I  
10 would like to stress that we repealed all of the political  
11 contributions totally.

12 The Chairman. Correct.

13 What does that revenue come to?

14 Mr. Brockway. There is a \$1 billion item, the repeal of  
15 the political contributions credit.

16 The Chairman. And now, with the revenue-raising  
17 provisions and the revenue-losing provisions, we are neutral.  
18 Is that correct?

19 Mr. Brockway. That is correct.

20 The Chairman. All right. We have at least one and  
21 perhaps two amendments, and we are open for amendments.

22 Senator Baucus. Mr. Chairman, aren't you going to have  
23 a vote on the package first, and then go back?

24 The Chairman. This entire package.

25 Senator Boren. We have only asked the question now;

1 for example, the working-interest amendment -- is that  
2 included in the package? Or does that need to be raised?

3 The Chairman. The 1.4 billion is included in the package.

4 Senator Boren. So, that does not need to be raised as a  
5 separate amendment?

6 The Chairman. Not as a specific, because we decided to  
7 include it in here, and it is in the package. I have a  
8 feeling there is going to be an amendment offered about it;  
9 but it is in the package at the moment.

10 Senator Mitchell. Well, Mr. Chairman, you said that we  
11 would have a vote on that.

12 The Chairman. I am perfectly happy to vote on the whole  
13 package, if you want to vote on this package.

14 All those in favor of this package that we have on both  
15 revenue-raising and revenue-losing will say Aye.

16 (Chorus of Ayes)

17 The Chairman. Opposed, No.

18 (Chorus of Noes)

19 The Chairman. The package is adopted.

20 Senator Bradley?

21 Senator Bradley. Mr. Chairman, I would propose to take  
22 the section of the package that was just adopted that deals  
23 with working interests, and I would propose to reduce the  
24 revenue in that package from \$1.4 billion to \$700 million.

25 Now, working interest is a way to finance oil and gas

1 drilling. The purpose of my amendment is to product the  
2 person in the active business of oil and gas. That is  
3 \$700 million.

4 What I would propose to do is to eliminate the passive  
5 investors and their ability to take losses from intangible  
6 drilling costs.

7 I would take the \$700 million that we would get from  
8 eliminating the passive losses under the working-interest  
9 provision and spend it to increase the earned income tax  
10 credit.

11 I think that the premise of this bill is that we are  
12 disallowing passive losses. We are disallowing passive losses  
13 for limited partnerships in oil and gas and in other limited  
14 partnerships, and I think that is a major step forward.

15 But what we have here is a special provision, carved out  
16 for a certain number of investors. And my hunch is that,  
17 when the limited partnerships are eliminated, that this will  
18 be a magnet to attract tax-shelter dollars to the oil and gas  
19 business. I do not think that is what the committee intended  
20 when we suggested the passive loss provision of the bill, and  
21 we have an opportunity under this amendment to protect those  
22 people who are really in the oil and gas business and do incur  
23 losses.

24 That is a brief explanation of the amendment.

25 The Chairman. Discussion on the amendment?

1 Senator Boren. Mr. Chairman?

2 The Chairman. Senator Boren?

3 Senator Boren. Mr. Chairman, I will be very brief, as  
4 we have had a rather lengthy discussion on this matter  
5 already.

6 I would point out that when we are dealing with working  
7 interests, we are not dealing with purely passive investors;  
8 we are dealing with those who are actually investing in the  
9 working interests of the bill -- they assume full liability,  
10 if there are problems with the bill, if there are environmental  
11 problems and costs; they also must participate in decisions,  
12 for example as to drilling deeper and requiring more money to  
13 be invested by those. We are not talking about limited  
14 partnerships.

15 So this is a very different situation from the kind of  
16 investment that we have referred to in the past as "purely  
17 passive investment."

18 Now, those who are familiar with the industry know that  
19 those who take a part of the working interests assume the  
20 good part of the liability and must participate in some of the  
21 most basic and important decisions.

22 As I have indicated to all of you, we are in a very  
23 desperate situation at this time in the independent sector of  
24 the industry.

25 I come from a state that, if it had not changed its tax



1 base over the last three years, would have lost 43 percent of  
2 all of its revenue collections, and over a three-year period,  
3 under the same tax system.

4 There is also a matter of debate about whether or not  
5 we want to maintain the structure of the industry. It is one  
6 that includes independent producers that are not able to  
7 raise all of their capital from their own funds, self-  
8 generated funds. Or, if we want to have an oil industry that  
9 is totally dominated by the major oil companies, the major  
10 integrated companies.

11 It is a very important policy decision before the  
12 committee, and I think it is a very important policy decision  
13 for the country in the long run. I would hope that my  
14 colleagues would join me in keeping the provision as it is  
15 now included in the package, and in rejecting this amendment.

16 The Chairman. Senator Dole?

17 Senator Dole. Mr. Chairman, let me just second very  
18 quickly what Senator Boren has said. I know there is always  
19 a frenzy in the media. They perceive the oil people to be  
20 big, big oil wells and a lot of rich people around.

21 In our State of Kansas, the average well produces about  
22 two and a half, or less than three barrels per day. And I  
23 believe what we are trying to protect here is, if you have an  
24 economic loss, if you invest in an oil well and have an  
25 economic loss, you ought to be able to deduct the loss. Toat's

1 all. We are not trying to shelter artificial losses; we are  
2 talking about real economic losses.

3 It would seem to me that we debated this issue for about  
4 an hour and a half in the back room. I know that states that  
5 don't produce oil have a different view; but there are other  
6 things in this bill that we have taken care of in states,  
7 including insurance and the completed contract for big  
8 defense contractors. We are asking for some help for very  
9 small producers with an average of about three barrels a day.

10 The Chairman. Senator Bentsen?

11 Senator Bentsen. Mr. Chairman, let me speak to it for  
12 just a moment from a national security standpoint.

13 Last year we used 29 percent foreign oil in this country.  
14 Back in 1973 and 1974 we were using 47 percent foreign oil.  
15 We became hooked on foreign oil, and we became very vulnerable.

16 We had the embargo, and we found out how vulnerable we  
17 were. And we had the long lines at the gas pumps.

18 This year, early on, we were producing 8.9 million  
19 barrels a day. It is estimated that by the end of this year  
20 we will be down by a million barrels, and we will once again  
21 begin to be dependent on foreign oil. We don't seem to have  
22 learned anything from what has happened to us in the past.

23 At one point we had 4500 rigs working in this country.  
24 It is estimated that at the present time we have a little over  
25 800 and that by the end of this year we will be down to as

1 low as 600 rigs. There is certainly no magnet attracting  
2 people to invest in oil wells at this time.

3 So I really think it is terribly important that you have  
4 such incentives as you can have to encourage that capital.

5 I must also tell you that there are not any banks that  
6 are loaning money -- unsecured money, in effect, non-recourse  
7 money -- to go out and drill oil wells. So it means that you  
8 have to raise all of that capital. And it is important that  
9 you have outside capital coming into that industry, which is  
10 in real trouble, and, again, trying to develop some national  
11 security protection in this country with sufficient reserves  
12 here.

13 The Chairman. Senator Wallop?

14 Senator Wallop. Just one very brief further obser-  
15 vation.

16 I think, as I said before, that the revenue estimate is  
17 wrong, and I suggest that one other reason why the revenue  
18 estimate is wrong is that, given the lower rate of individual  
19 tax, which is the only one that is going to be affected by  
20 this, there really is no reason in this day and age, with  
21 this price of oil, to shoulder the risk that is attendant upon  
22 a working interest.

23 Keep in mind that there is no escape from the risk; once  
24 you enter that agreement with the remaining partners in the  
25 field, if a well that is supposed to cost \$1 million costs

1 eight, your share is eight times higher than you thought it  
2 was going to be.

3 So, as these tax rates lower, the reason for people to  
4 seek shelter is diminishing rapidly.

5 The Chairman. The Clerk will call the roll.

6 Senator Mitchell. Mr. Chairman?

7 The Chairman. I'm sorry; I apologize, George. Yes?

8 Senator Mitchell. Mr. Chairman, I think it ought to be  
9 clear that what we are doing here is establishing one rule for  
10 every American business, every American interest except oil  
11 and gas, and then a special rule for those in the oil and gas  
12 business.

13 An American who invests in a project involving real  
14 estate, under legal circumstances identical to those with  
15 another person who invests in oil and gas, will be treated  
16 differently and to his disadvantage.

17 An American who invests in an extractive industry, an  
18 American who invests in any other business but oil and gas,  
19 even though under identical circumstances, will be treated in  
20 a wholly different fashion, and those who invest in oil and  
21 gas will be treated in a preferential fashion even though the  
22 circumstances are identical.

23 I can see no justification for that. No rational basis  
24 has been offered. No standards by which such a distinction  
25 can be made has been suggestion. All we are saying is that

1 we are going to give special treatment to one industry and  
2 one category of persons, and everybody else will be treated  
3 differently.

4 The Chairman. Senator Long, then Senator Chafee, and  
5 then Senator Danforth.

6 Senator Long. Mr. Mitchell is a great lawyer and a great  
7 judge. He had a lifetime job as a judge, and he sacrificed  
8 that to serve in the Senate. Why a man would do it, I don't  
9 know.

10 (Laughter)

11 Senator Long. But from a legal background and a lifetime  
12 in the judicial -- most of his life in the law and the  
13 judiciary -- he tends to look upon this tax law as that statue  
14 over there in front of the Supreme Court, at a lady holding  
15 a scale. She's blindfolded. She don't know whose weights  
16 are on the lefthand side and whose are on the righthand side.  
17 And that's how they are supposed to decide cases over there,  
18 not knowing who they are helping or who they are hurting; just  
19 whoever puts the most weights on this side, he wins on his  
20 end, and whoever puts the most weights on that side, he wins.  
21 And that lady don't know whose weight is on which side.

22 To say that we ought to pass laws the way they decide  
23 their cases over there is as wrong as anything can be. We  
24 fellows are law makers. We are supposed to know who we are  
25 helping and do it deliberately, and know who we're hurting and

1 so that deliberately.

2 (Laughter)

3 Senator Long. Now, the people in the oil and gas  
4 business are in the most depressed industry in the United  
5 States. And if you are sitting over there in that corner,  
6 I can understand your saying, "Well, I'm blindfolded; I'm  
7 going to treat them all the same. This fellow is broke,  
8 down and out, God knows he needs help; but to hell with him,  
9 I'm blindfolded and can't do anything about it." If you  
10 were a judge, that's how you would do it. If you are a law-  
11 maker, you'd say, "That poor fellow needs help; let's help  
12 him."

13 (Laughter)

14 Senator Long. "This fellow is doing well; let's make  
15 him pay more taxes." That's how you would do it.

16 (Laughter)

17 Senator Mitchell. Well, when we pass the next tax bill,  
18 will we then look around and see if the shoe industry is  
19 hurting or the textile industry is hurting and say, "We'll  
20 give them special treatment"?

21 Senator Long. Why do you think we just got through  
22 passing a bill to give the shoe industry in your state  
23 relief? And the textile people? They've done nothing for  
24 my fishermen in Louisiana.

25 Senator Mitchell. We haven't given them a thing.

1 The Chairman. Senator Chafee?

2 Senator Chafee. It's all right.

3 (Laughter)

4 Senator Chafee. That is coming on the stage after a  
5 star performance.

6 (Laughter)

7 Senator Chafee. Mr. Chairman, let me just say this: I  
8 agree with what Senator Bradley has said, that we are prepared  
9 to go half-way here, to give special treatment to a group here  
10 who are actively involved in the industry. But this isn't  
11 what is involved here -- that is not what we are dealing with.  
12 We are right back to that dentist fellow back there in St.  
13 Louis, who is going to put his money into a deal out there.

14 Senator Dole. The rehab credit is where he is going to  
15 put it.

16 Senator Chafee. In some Texas or some oil patch some-  
17 where and is going to be able to have that income sheltered.  
18 That is what we are trying to eliminate in this measure.

19 So, this isn't the active fellow who we're prepared to  
20 go half-way with with. I think this total measure before us  
21 is \$1.4 billion and we were willing to go \$700 million. But  
22 that wasn't enough. Therefore, I decided I am not in favor of  
23 the proposal.

24 The Chairman. Senator Danforth?

25 Senator Danforth. Mr. Chairman, as I explained earlier

1 in the evening, I have real doubts about the provision that  
2 is in this package.

3 The question I raised at our earlier meeting is whether  
4 this would serve as a magnet, as Senator Bradley has put it,  
5 for shelter money that previously has been in barges or in  
6 boxcars or in real estate.

7 I am not sure about the answer to that question. There  
8 was considerable discussion in the back room, and people who  
9 know far more about this issue than I know believe that this  
10 is not like a limited partnership, that people who have  
11 these interests have real risks and that their losses are real  
12 losses and not paper losses.

13 I am not sure about that, but I do know this: I am for  
14 the bill. I think this is a major tax-reform bill. I think  
15 it accomplishes a very fundamental shift in our whole way of  
16 doing tax law in the United States.

17 I believe that, at least at this point, the package that  
18 the Chairman has presented to us is one that is necessary if  
19 we are going to get the bill out of this committee, and if  
20 we are going to have a chance to move forward with this  
21 legislation.

22 Therefore, I am going to vote for the package. I am  
23 going to vote against the Bradley amendment. But I reserve  
24 the right to vote differently on the floor.

25 The Chairman. Clerk, call the roll on the Bradley



1 amendment.

2 The Clerk. Mr. Dole?

3 Senator Dole. No.

4 The Clerk. Mr. Roth?

5 Senator Roth. No.

6 The Clerk. Mr. Danforth?

7 Senator Danforth. No.

8 The Clerk. Mr. Chafee?

9 Senator Chafee. Aye.

10 The Clerk. Mr. Heinz?

11 Senator Heinz. No.

12 The Clerk. Mr. Wallop?

13 Senator Wallop. No.

14 The Clerk. Mr. Durenberger?

15 Senator Durenberger. Aye.

16 The Clerk. Mr. Armstrong?

17 Senator Armstrong. No.

18 The Clerk. Mr. Symms?

19 Senator Symms. No.

20 The Clerk. Mr. Grassley?

21 Senator Grassley. No.

22 The Clerk. Mr. Long?

23 Senator Long. No.

24 The Clerk. Mr. Bentsen?

25 Senator Bentsen. No.

1 The Clerk. Mr. Matsunaga?  
2 Senator Matsunaga. No.  
3 The Clerk. Mr. Moynihan?  
4 Senator Moynihan. Aye.  
5 The Clerk. Mr. Baucus?  
6 Senator Baucus. No.  
7 The Clerk. Mr. Boren?  
8 Senator Boren. No.  
9 The Clerk. Mr. Bradley?  
10 Senator Bradley. Aye.  
11 The Clerk. Mr. Mitchell?  
12 Senator Mitchell. Aye.  
13 The Clerk. Mr. Pryor?  
14 Senator Pryor. No.  
15 The Clerk. Mr. Chairman?  
16 The Chairman. Aye.  
17 The Clerk. Six Yeas, 14 Nays.  
18 The Chairman. The amendment is defeated.  
19 Are there further amendments?  
20 Senator Bradley. Mr. Chairman?  
21 The Chairman. Senator Bradley?  
22 Senator Bradley. Mr. Chairman, the tax reform bill that  
23 this committee is about to enact is a very significant bill.  
24 And, Mr. Chairman, you have provided very great leadership  
25 in getting this bill to this point.

1           The premise of tax reform is that you give people lower  
2 tax rates, and that in exchange for that they give up loop-  
3 holes. That's the deal. You give up loopholes so that you  
4 get your tax rate down.

5           In this bill, the rates are 15 and 27 percent. We also  
6 have a minimum tax in this bill, an individual minimum tax of  
7 20 percent.

8           But, Mr. Chairman, with the working-interest loophole  
9 still in the law, we will say to a small group of investors  
10 in oil gas -- now, we have made big strides in closing the  
11 limited partnership, but we will say to a small group of  
12 investors in oil and gas -- that "on your salary, your  
13 interest, your dividends, you pay a 27-percent rate, and  
14 that's it. On your oil and gas, related to working interests,  
15 the losses, you don't even have to pay a minimum tax on that.  
16 You don't even have to pay a minimum tax."

17           Mr. Chairman, I don't think that is what tax reform is  
18 all about. So, the second amendment that I would offer is  
19 for the purpose of the minimum tax. Losses in a working  
20 interest would be counted as a tax preference.

21           The Chairman. Discussion on the amendment?

22           Senator Boren. Mr. Chairman, I will just be brief. This  
23 is the very same issue, really, that we have just debated and  
24 that we have just voted on. The question is a matter of  
25 real economic loss. We have already established, I think,

1 that those who are involved in workign interests have a stake  
2 in it, they have full liability.

3 We are not talking about limited partnerships; we are  
4 talking about those who are liable, who have to make decisions  
5 to put in additional money, and all the rest of it. We are  
6 talking about the future of the structure of the industry --  
7 we don't have to worry about Mobils or Exxons or the large  
8 neergy corporations; they don't have to go out and seek  
9 people to invest nor to have working interests nor to  
10 participate in this fashion; they have their own sources of  
11 income.

12 I would just say, again, that if we want to have an  
13 industry that is totally dominated by those giants, then this  
14 is the way to go. If we want to totally negate the actions  
15 which we have previously taken, then this is what we should  
16 do.

17 It would be devastating to the independent sector. It  
18 would penalize people who have real economic losses, as  
19 opposed to paper losses. It would go far beyond what we have  
20 done in the area of limited partnerships and others.

21 So I would hope, rather than to debate the matter again,  
22 it is the very, very same, identical issue, and I would hope  
23 the amendment would be defeated.

24 The Chairman. Senator Bentsen?

25 Senator Bentsen. Mr. Chairman, if you have a true

1 economic loss, you get to take that against your ordinary  
2 income, and that's the way it ought to be.

3 When he says that it is not subject to the alternative  
4 minimum -- if you are talking about accelerated depreciation,  
5 you are talking about IDCs, you are talking about those kinds  
6 of tax losses, that is subject to the alternative minimum, and  
7 I see no reason to change that.

8 But if you are talking about classifying the entire loss,  
9 whatever that might be, as something that pays an alternative  
10 minimum tax, I really don't understand the rationale for that.

11 The Chairman. Clerk, call the roll on the Bradley  
12 amendment.

13 The Clerk. Mr. Dole?

14 Senator Dole. No.

15 The Clerk. Mr. Roth?

16 Senator Roth. Aye.

17 The Clerk. Mr. Danforth?

18 Senator Danforth. Aye.

19 The Clerk. Mr. Chafee?

20 Senator Chafee. Aye.

21 The Clerk. Mr. Heinz?

22 Senator Heinz. Aye.

23 The Clerk. Mr. Wallop?

24 Senator Wallop. No.

25 The Clerk. Mr. Durenberger?

1 Senator Durenberger. Aye.  
2 The Clerk. Mr. Armstrong?  
3 Senator Armstrong. No.  
4 The Clerk. Mr. Symms?  
5 Senator Symms. No.  
6 The Clerk. Mr. Grassley?  
7 (No response)  
8 The Clerk. Mr. Long?  
9 Senator Long. No.  
10 The Clerk. Mr. Bentsen?  
11 Senator Bentsen. No.  
12 The Clerk. Mr. Matsunaga?  
13 Senator Matsunaga. No.  
14 The Clerk. Mr. Moynihan?  
15 Senator Moynihan. Aye.  
16 The Clerk. Mr. Baucus?  
17 Senator Baucus. No.  
18 The Clerk. Mr. Boren?  
19 Senator Boren. No.  
20 The Clerk. Mr. Bradley?  
21 Senator Bradley. Aye.  
22 The Clerk. Mr. Mitchell?  
23 Senator Mitchell. Aye.  
24 The Clerk. Mr. Pryor?  
25 Senator Pryor. No.

1 The Chairman. Grassley is No.

2 The Clerk. I'm sorry. Mr. Chairman?

3 The Chairman. The Chairman votes Aye.

4 Senator Heinz. Mr. Chairman, do you have mine?

5 The Chairman. Heinz is Aye.

6 The Clerk. Nine Yeas, 11 Nays.

7 The Chairman. Defeated.

8 Senator Armstrong?

9 Senator Armstrong. Mr. Chairman, by the last two votes  
10 we have affirmed a principle with respect to the oil and gas  
11 industry, that if you have a real loss, you get to take it  
12 as a deduction against other income. And I think that is a  
13 wise decision.

14 I want to point out -- and I will do it very, very  
15 briefly, because we have discussed this at great length.

16 By the way, Mr. Chairman, I really regret that the bulk  
17 of today's session occurred behind closed doors, because we  
18 had a good debate, and really a better debate than we are going  
19 to have in the middle of the night. I am sorry that everybody  
20 isn't going to get the benefit of it.

21 For the record let me just point out that other investors  
22 in other kinds of business enterprises, who suffer true  
23 economic loss, not paper losses, not artificial losses, not  
24 phony losses, not accelerated depreciation, but real economic  
25 loss, where they put up money in productive job-creating

1 enterprises and then they have losses, will not be able to  
2 net those losses against other income.

3 Let me be just completely specific: Whether you are  
4 talking about real estate, or a passive investment in an  
5 operating business, or anything of that kind, losses which  
6 have been always, traditionally and historically, subject to  
7 netting against earned income or against other kinds of  
8 investment income, we're not going to be able to do that.

9 Now, it is obvious that I feel pretty strongly about  
10 this, and yet I am not going to offer an amendment. The  
11 reason is simply, because the dollar cost of fixing that is  
12 so large that I can't round up the votes to do that tonight.

13 But I just want to point it out, Mr. Chairman, so that  
14 the record is complete, because on another occasion we are  
15 going to have to come back and fix this problem -- first,  
16 because it is unjust, second, because it is illogical, and  
17 third, because it is going to have enormous economic  
18 consequences.

19 What we are really talking about is collapsing some large  
20 segments of the real estate market. Now, we think we are  
21 going to head it off because we are phasing it in over four  
22 years; but it is still unjust, even though we do it over four  
23 or five years. And every person who owns an interest in the  
24 kind of real estate and other business enterprises that are  
25 affected in this way is going to find out tomorrow morning --



1 not four years from now but tomorrow morning -- that the  
2 value of their business investment has been reduced, has been  
3 marked down as a result of the action we are taking.

4 So, though I am not going to offer an amendment, I will  
5 just tell you I may offer an amendment on the floor, if I  
6 can think of an amendment that might have a chance to pass.

7 The Chairman. Other amendments?

8 Senator Heinz. Mr. Chairman?

9 Senator Long. Mr. Chairman?

10 The Chairman. Senator Long?

11 Senator Long. The Senator from New Jersey said that the  
12 oil and gas industry pays no minimum tax. I would like to  
13 refer him to the so-called "65-percent rule" which I per-  
14 sonally offered. I have some doubts about the wisdom of it  
15 now, because it cuts back on drilling; but, it is, in effect,  
16 a minimum tax on oil and gas.

17 Would you like to explain how that works with the  
18 65-percent rule, Mr. Wilson?

19 Mr. Wilson. Yes. The 65-percent rule, in Section 1613  
20 (a) (D) provides that percentage depletion may not exceed 65  
21 percent of the taxpayer's taxable income computed without  
22 regard to any depletion.

23 So, the percentage depletion could not zero out a  
24 taxpayer's position on oil and gas.

25 Senator Bradley. Mr. Chairman, that makes my point:

1 percentage depletion can't but intangible drilling costs can,  
2 and intangible drilling costs go to 31,000 people in this  
3 country who have incomes over \$100,000, and they get an  
4 average benefit of \$28,000.

5 So I don't think that that applies to the minimum tax  
6 as it relates to intangible drilling costs. I don't know  
7 why we reopened this; the vote was taken.

8 Senator Long. Well, intangible drilling costs is an  
9 actual out-of-pocket expense. That is money you have spent.  
10 That is money you have separated yourself from -- it's gone.  
11 If you compare it to advertising, it works out about the  
12 same way.

13 You say why did I raise it? Well, because I just didn't  
14 want it to appear in the record that there is no minimum tax  
15 on this industry, because there is.

16 Senator Bradley. Mr. Chairman, could we ask Mr. Brockway,  
17 just so we clarify this?

18 Is intangible drilling costs subject to the minimum tax?

19 Mr. Brockway. Yes. There are several things going on.  
20 The rule Senator Long is talking about is the rule in the  
21 regular-tax limiting depletion.

22 There is also, in the minimum tax, that intangible  
23 drilling costs are treated as a preference. In the minimum  
24 tax, the amendment -- well, in the package, it provides that  
25 working interests are not passive losses. So, that would

1 change the approach to that part is not in the minimum tax.

2 But intangible drilling costs itself is a preference in  
3 the alternative minimum tax.

4 Senator Bradley. But passive losses are not?

5 Mr. Brockway. Oh, yes. I should clarify one thing.  
6 However, there is a net income offset in the alternative  
7 minimum tax, so you are allowed to use the intangible  
8 drilling costs without cutdown. You can expense your  
9 intangible drilling costs right away, to the extent you have  
10 income from the oil and gas industry.

11 Senator Bentsen. Well, then, if you had accelerated  
12 depreciation and that type of thing on your equipment, then  
13 you would have some additional, wouldn't you?

14 Mr. Brockway. You can use the intangible drilling costs  
15 to the extent you have oil and gas income; however, if you had  
16 other accelerated depreciation, for example, in the oil and  
17 gas business, that would be subject to the general  
18 depreciation rules that apply to all businesses.

19 Senator Bentsen. That is right.

20 Mr. Brockway. And it could be limited.

21 In addition, also, if you had an interest in a limited  
22 partnership, for example, in oil and gas, that would again  
23 be subject to the passive-loss limitations.

24 Senator Bentsen. Right. Sure. So, you could get some  
25 alternative minimum tax out of it.

1 Mr. Brockway. Very definitely, depending upon the  
2 circumstances.

3 Senator Boren. Mr. Chairman?

4 The Chairman. Senator Boren.

5 Senator Boren. Mr. Chairman, just to short-circuit this  
6 debate, let me say that I don't have any amendments to offer.  
7 The hour is late. I have some of the same concerns that  
8 Senator Armstrong has expressed, some things that I think need  
9 to be fixed with this bill later on.

10 But let me say I think you have made remarkable progress;  
11 we have moved much closer to tax reform; and in the hopes  
12 that we are moving toward that moment that we should be  
13 approaching very shortly, let me just say that, in spite of  
14 some individual provisions with which I have a difference of  
15 opinion, I think we have moved a long way, and I intend to  
16 vote for final passage of your product. I hope we will be  
17 able to do that very shortly.

18 The Chairman. Are there further amendments?

19 Senator Symms, and then Senator Heinz.

20 Senator Symms. Mr. Chairman, earlier today we did the  
21 amendment that Senator Boren and Senator Heinz had offered,  
22 and it ended up that the second go round was the Heinz-  
23 modified Boren proposal for the corporate-individual minimum  
24 tax. And it was voted 10-to-10. Now, in the back room we  
25 didn't seem to have the support.

1 I just want to first say that I think that is a critical  
2 problem still in this bill, and it is still going to have to  
3 be addressed.

4 There are some proposals that I am not quite prepared to  
5 introduce tonight where we could maybe stretch out the  
6 depreciation on some of these items and have it be almost  
7 self-financed, but to avoid getting some of these companies  
8 in this minimum tax that are under a lot of pressure from  
9 foreign competition.

10 So, I won't offer that tonight, because I think that is  
11 somewhere around a \$2-3 billion issue, if I understood it  
12 right earlier today.

13 But there is one small part of it that I do want to  
14 offer tonite is with respect to mining.

15 Now, all of us know that we heard Senator Long and others  
16 make a real appeal for the way the oil and gas business is,  
17 and I agree with them. I think we should help them, and I  
18 voted with them.

19 But for everything that can be said about the problems in  
20 Oklahoma and Louisiana and other places, all you have to do is  
21 come to someplace like Shoshone County in Idaho, where we had  
22 4000 miners working seven or eight years ago and we now have  
23 400 minors working. This industry is absolutely in a  
24 disastrous state of affairs, and it is. From a national  
25 security standpoint, the same thing can be made as the

1 argument in oil and gas.

2 Now, this is a very small cost amendment, but I believe  
3 it would be a tragic mistake to pass this package out of here  
4 and not have mining exploration and development costs --  
5 which are front-end costs -- for new mines and new jobs in  
6 the United States, if we do not remove that from being a  
7 preference items in the minimum tax.

8 I hope the committee would accept that amendment. The  
9 staff has said it is in the neighborhood of a \$50-million  
10 figure. That is just anybody's guess.

11 If we don't have a mining industry, I think the cost to  
12 the Treasury will be much more than a \$50-million figure. But  
13 we need to encourage exploration and development costs of new  
14 mines and not have that considered a preference item under the  
15 minimum tax.

16 I would move that amendment at this point.

17 The Chairman. Discussion on the amendment?

18 (No response)

19 The Chairman. Well, Steve, much as I would like to  
20 support you, I didn't support the oil amendments; I supported  
21 Senator Bradley, which makes, in my judgment, a slight  
22 imperfection in the bill. And I hate to start down the road  
23 of any further exceptions in the minimum tax. I am going to  
24 oppose it.

25 Senator Symms. Well, Mr. Chairman, I am sorry that the

1 Chairman is not going to support it. I would like to have a  
2 rollcall on it. If I lose it here, I am going to bring it  
3 back on the floor.

4 The Chairman. Absolutely.

5 The Clerk will call the roll on the amendment.

6 The Clerk. Mr. Dole?

7 Senator Dole. Aye.

8 The Clerk. Mr. Roth?

9 Senator Roth. Aye.

10 The Clerk. Mr. Danforth?

11 Senator Danforth. No.

12 The Clerk. Mr. Chafee?

13 Senator Chafee. No.

14 The Clerk. Mr. Heinz?

15 Senator Heinz. Aye.

16 The Clerk. Mr. Wallop?

17 Senator Wallop. Aye.

18 The Clerk. Mr. Durenberger?

19 Senator Durenberger. Aye.

20 The Clerk. Mr. Armstrong?

21 Senator Armstrong. Aye.

22 The Clerk. Mr. Symms?

23 Senator Symms. Aye.

24 The Clerk. Mr. Grassley?

25 Senator Grassley. Aye.

1 The Clerk. Mr. Long?

2 Senator Long. Aye.

3 The Clerk. Mr. Bentsen?

4 Senator Bentsen. Aye.

5 The Clerk. Mr. Matsunaga?

6 Senator Matsunaga. No.

7 The Clerk. Mr. Moynihan?

8 Senator Moynihan. No.

9 The Clerk. Mr. Baucus?

10 Senator Baucus. No.

11 The Clerk. Mr. Boren?

12 Senator Boren. Aye.

13 The Clerk. Mr. Bradley?

14 Senator Bradley. No.

15 The Clerk. Mr. Mitchell?

16 Senator Mitchell. No.

17 The Clerk. Mr. Pryor?

18 Senator Pryor. No.

19 The Clerk. Mr. Chairman?

20 The Chairman. No.

21 The Clerk. Eleven Yeas, nine Nays.

22 The Chairman. The amendment passes.

23 Senator Moynihan. Mr. Chairman, I move to request the  
24 bill.

25 The Chairman. The bill is still open for amendment.



1           Let me say, though, I think we are making unwise  
2 decisions as we start down this path, and I would hope that  
3 the Senator from Pennsylvania does not have another exception  
4 on the minimum tax.

5           Senator Heinz. No, the Senator from Pennsylvania does  
6 not. The Senator from Pennsylvania has a revenue-neutral  
7 amendment, Mr. Chairman, and it is guaranteed revenue-neutral  
8 by the staff.

9           (Laughter)

10          Senator Heinz. Where'd they go?

11          The Chairman. Is there a little seal that they put on  
12 it?

13          Senator Heinz. Of approval. But the one that counts is  
14 up here.

15          Mr. Chairman, on one other occasion I pointed out that,  
16 under the current tax laws, we have a preference for  
17 residential rental real estate, as compared to commercial  
18 real rental real estate.

19          Under current law we established that by giving rental  
20 residential real estate 150-percent declining-balance  
21 depreciation, 19 years. We only permit straight line  
22 depreciation for commercial rental real estate. There is  
23 a reason we do that.

24          The reason is that commercial real estate usually, and  
25 can, and does, prelease. They get their commitments from

1 their rentals upfront.

2 Secondly, commercial rental real estate usually operates  
3 on fairly long-term leases -- at least several years; often  
4 five years, sometimes longer than that. Rental residential  
5 property, on the other hand, is necessarily short-term  
6 rental; it is usually not rented until after it is  
7 constructed; it is management-intensive -- you've got a lot  
8 of people in a lot of small apartments, as opposed to large  
9 tenants in fairly substantial blocks of space -- and so I  
10 think we were wise under current law to give a modest  
11 preference to residential rental real estate.

12 As the bill stands before us now, we have essentially  
13 neutered that preference. The amendment I am proposing on  
14 behalf of myself and Senator Durenberger would introduce a  
15 modest and appropriate preference, and it would be as follows:

16 Instead of under the Chairman's draft, the 30-year life  
17 for both commercial and residential real property, we would  
18 have 31.5 year life for commercial rental real estate -- a  
19 31-and-a-half year life, for depreciation -- and for  
20 residential real property, and for tax-exempt bond-financed  
21 multifamily housing, the depreciable life would be 27-and-a-  
22 half years. The result of that would be to reestablish the  
23 kind of preference we had previously.

24 I think I have explained why that preference is a good  
25 idea, and I would hope the committee -- which I think on one

1 other occasion basically supported the philosophy behind this  
2 amendment -- would do so again.

3 Senator Durenberger. Mr. Chairman, it is revenue-neutral.

4 The Chairman. Let me just make a statement in apology:  
5 on the Symms amendment, I simply forgot that it was not  
6 revenue-neutral. I am tired, and I did not consider it. I  
7 apologize. It is the first time I haven't raised it, and I  
8 am embarrassed.

9 Senator Bradley. Mr. Chairman, should we reconsider it,  
10 if it isn't?

11 The Chairman. It is open for reconsiderations. I simply  
12 apologize. It slipped my mind.

13 Senator Wallop. Mr. Chairman?

14 The Chairman. Senator Wallop?

15 Senator Wallop. I can offer an amendment that will make  
16 it revenue neutral and give you \$350 million more.

17 The Chairman. I would be very appreciative if you would,  
18 because I feel embarrassed about having forgot it.

19 Senator Wallop. It had been my intention all along, in  
20 the repeal of PURPTA, to repeal it from here forward. The  
21 revenue estimates that we have been having were for a  
22 retroactive repeal, and it had never been my intention that  
23 we refund people money that they have already paid under that  
24 tax. To my understanding, that is approximately \$400 million.

25 Mr. Brockway. That is correct, Senator.

1 Senator Wallop. Senator, I would be willing to offer  
2 that amendment to get you out of a box, and Lloyd and I had  
3 no intention of that.

4 The Chairman. I am very, very appreciative. And without  
5 objection we will accept the amendment.

6 Now on the Heinz amendment, Senator Durenberger?

7 Senator Durenberger. Mr. Chairman, I am waiting for the  
8 admiration for Malcolm to die down.

9 (Laughter)

10 Senator Durenberger. I am sure it never will.

11 A little while ago Russell, in his inimitable fashion,  
12 told us that we don't sit up here as judges and make blind  
13 judgments, and he is absolutely right; we make very specific  
14 decisions.

15 Some of us are uncomfortable about some of the decisions  
16 we make; but the decision that we are asking you to make  
17 tonight, we are asking you very deliberately to make, and  
18 that is to continue to draw some distinction in the  
19 depreciation treatment between housing in this country and  
20 commercial property.

21 In 1981, when we took depreciation down -- drastically,  
22 down to 15 years -- we handed to the commercial and housing  
23 industry in this country a bonanza, in effect. That got  
24 combined with a variety of tax shelters, and we started  
25 getting property coming out of our ears.

1           And I think we helped to accentuate a problem that was  
2 building up in this country for the 10-15 previous years, in  
3 just substantially pricing ourselves and our children out  
4 of the housing market.

5           And in order to access people to that housing market, we  
6 have had to come up with a variety of subsidies. We talked  
7 about them all tonight. George may still talk about some of  
8 them while we are here, at some other time.

9           The reality, though, is that there is a terrible  
10 distinction in this country and in this bill between owned-  
11 housing and rental-housing, and we have just accentuated that  
12 problem here.

13           The owners not only get unlimited interest on their  
14 principal home, they get it on a second home. They get all of  
15 the real estate deductions, and so forth. The renter gets  
16 none of that.

17           I think the reality, as most of you know, is that we have  
18 priced our children out of owning homes in America, at least  
19 about 90 percent of our kids. And we force them into the  
20 rental market. And it is a rental market they can't afford  
21 without some subsidy.

22           So, whether the subsidy is this little bit of a break  
23 between 27.5 and 31.5 on depreciation, it is still a lot less  
24 than 19, which is what it has been. Or, maybe the subsidy is  
25 the tax-exempt bond financing combined with the 27.5. But it

1 still is a relatively small subsidy compared to the huge  
2 subsidy that in effect we give to owned-housing.

3 So I would plead with my colleagues: You are not doing  
4 any damage to commercial property in this country by permit-  
5 ting this distinction, but you can help in a somewhat  
6 substantial fashion those who have to rent property in this  
7 country if you will vote for John Heniz's amendment, and I  
8 hope that you do.

9 The Chairman. Could I make a unanimous-consent  
10 request? Because I still feel badly about forgetting that  
11 Steve's amendment was not revenue-neutral.

12 Anybody who voted No on that amendment because it was  
13 not revenue-neutral, and it is now revenue-neutral, who would  
14 like to change their vote, I would like to request unanimous  
15 consent they be allowed to be so recorded.

16 (No response)

17 The Chairman. I appreciate it.

18 Further discussion on the Heinz amendment?

19 Senator Chafee. Mr. Chairman, in the proposal that  
20 Senator Durenberger made here, he is allowing this dif-  
21 ferential in the depreciation to apply to those buildings that  
22 have been constructed with tax-exempt bonds; is that right?

23 Senator Durenberger. Yes, which is the current  
24 situation. At the present time, tax-exempt bond multifamily  
25 rental housing has a 19-year life. This bill would take that

1 to a 40-year life. You might as well forget about multi-  
2 family housing.

3 That is why we have the amendment. We are taking it  
4 from 19 to 27.5.

5 The Chairman. Further discussion on the amendment?

6 (No response)

7 The Chairman. If not, the Clerk will call the roll.

8 The Clerk. Mr. Dole?

9 Senator Dole. No.

10 The Clerk. Mr. Roth?

11 Senator Roth. No.

12 The Clerk. Mr. Danforth?

13 Senator Danforth. Aye.

14 The Clerk. Mr. Chafee?

15 Senator Chafee. No.

16 The Clerk. Mr. Heinz?

17 Senator Heinz. Aye.

18 The Clerk. Mr. Wallop?

19 Senator Wallop. Aye.

20 The Clerk. Mr. Durenberger?

21 Senator Durenberger. Mr. Armstrong?

22 Senator Armstrong. No.

23 The Clerk. Mr. Symms?

24 Senator Symms. Aye.

25 The Clerk. Mr. Grassley?

1 Senator Grassley. No.  
2 The Clerk. Mr. Long?  
3 Senator Long. Pass.  
4 The Clerk. Mr. Bentsen?  
5 Senator Bentsen. Aye.  
6 The Clerk. Mr. Matsunaga?  
7 Senator Matsunaga. No.  
8 The Clerk. Mr. Moynihan?  
9 Senator Moynihan. Aye.  
10 The Clerk. Mr. Baucus?  
11 Senator Baucus. Aye.  
12 The Clerk. Mr. Boren?  
13 Senator Boren. Aye.  
14 The Clerk. Mr. Bradley?  
15 Senator Bradley. Aye.  
16 The Clerk. Mr. Mitchell?  
17 Senator Mitchell. Aye.  
18 The Clerk. Mr. Pryor?  
19 Senator Pryor. Aye.  
20 The Clerk. Mr. Chairman?  
21 The Chairman. Aye.  
22 Senator Roth. Mr. Chairman, I vote Aye.  
23 The Chairman. Roth -- Aye.  
24 Senator Long. Mr. Chairman, Aye.  
25 The Chairman. Senator Long -- Aye.



1 Are there others who wish to be recorded?

2 Senator Moynihan. Mr. Chairman, once again I move to  
3 put the bill.

4 The Chairman. I want to ask the Administration's opinion  
5 before we do that. And I want to get the count on this,  
6 obviously.

7 The Clerk. Fifteen Yeas, five Nays.

8 The Chairman. Fifteen Yeas, five Nays, the amendment is  
9 adopted.

10 Secretary Darman, can you give us any impression of the  
11 Administration about this bill?

12 Secretary Darman. Thank you, Mr. Chairman.

13 The President, as you know, is in Tokyo. He has, however,  
14 been kept informed of the deliberations of the committee, at  
15 least in a general way, and in some detail -- not complete  
16 detail.

17 As many of you know, he has already this evening, in a  
18 nationally televised press conference, commended the work of  
19 the committee in anticipation of the consensus package. And  
20 I have been authorized on behalf of the Administration to  
21 state the following:

22 "We congratulate you, Mr. Chairman, and the distinguished  
23 members of the Senate Finance Committee for your bold tax-  
24 reform proposals.

25 "A preliminary review by the Administration indicates

1 that the proposal reflects the President's objectives.

2 "The proposal dramatically simplifies the tax rate  
3 structure, and reduces personal income tax rates to the lowest  
4 levels in over half a century.

5 "It removes millions of working poor from the tax rolls.  
6 It raises the personal exemption to \$2000. It does away with  
7 unproductive tax shelters. It substantially increases  
8 incentives for productive investment, relative to the House  
9 bill.

10 "It reduces the overall cost of capital, relative to  
11 both the House bill and current law, and it provides a  
12 minimum tax to assure that all individuals and corporations  
13 pay their fair share.

14 "While we may have reservations about a few features of  
15 the bill, we are confident that these can be addressed in  
16 subsequent stages of the process.

17 "We feel the committee's proposal is a major step toward  
18 achieving meaningful tax reform, and urge the committee to  
19 act promptly and pass the proposal.

20 "We look forward to continuing to work with you, Mr.  
21 Chairman, and the Senate, as we move closer to historic tax  
22 reform. And again, we congratulate you and the members of the  
23 committee for your hard work and hard choices on behalf of  
24 meaningful tax reform."

25 Thank you, Mr. Chairman.

1           The Chairman. We are delighted to have the President  
2 on board.

3           Senator Bradley?

4           Senator Bradley. The President knows how to steal a  
5 headline 10,000 miles away.

6           (Laughter)

7           Senator Bradley. Mr. Chairman, I was going to say that  
8 I obviously don't like the working-interest portion of this  
9 bill, and I will obviously attempt to make a change of that  
10 on the floor.

11           But I will say that I think this is indeed an extremely  
12 significant bill -- six million people off the rolls at the  
13 low end; families of four in a 33-percent rate down to a  
14 15-percent rate; most tax shelters, with the exception of  
15 that working interest, gone.

16           And Mr. Chairman, I think it is a significant day. I  
17 am pleased to be here and be a part of it, and I salute you  
18 for your effort.

19           The Chairman. Mr. Colvin? What do you have?

20           Mr. Colvin. Mr. Chairman, I just wanted to indicate that  
21 there are two technical packages, on the Retirement Equity  
22 Act, which are cleared with both the Majority and the Minority  
23 side, and also several clarifications of the spreadsheets.  
24 Also, to ask for discussion for the committee staff to make  
25 the necessary technical and conforming changes in drafting

1 the legislation.

2 The Chairman. Without objection.

3 I believe we are there.

4 Clerk, call the roll on final passage.

5 The Clerk. Mr. Dole?

6 Senator Dole. I want to thank the Chairman for this  
7 historic effort, and I vote Aye.

8 The Clerk. Mr. Roth?

9 Senator Roth. Aye.

10 The Clerk. Mr. Danforth?

11 Senator Danforth. Aye.

12 The Clerk. Mr. Chafee?

13 Senator Chafee. Aye.

14 The Clerk. Mr. Heinz?

15 Senator Heinz. Aye.

16 The Clerk. Mr. Wallop?

17 Senator Wallop. Aye.

18 The Clerk. Mr. Durenberger?

19 Senator Durenberger. Aye.

20 The Clerk. Mr. Armstrong?

21 Senator Armstrong. Aye.

22 The Clerk. Mr. Symms?

23 Senator Symms. Aye.

24 The Clerk. Mr. Grassley?

25 Senator Grassley. Aye.

1 The Clerk. Mr. Long?

2 Senator Long. Like Senator Dole, I want to congratulate  
3 the Chairman on the fantastic job that he has done with this  
4 bill, and I vote Aye.

5 The Clerk. Mr. Bentsen?

6 Senator Bentsen. Aye.

7 The Clerk. Mr. Matsunaga?

8 Senator Matsunaga. Aye.

9 The Clerk. Mr. Moynihan?

10 Senator Moynihan. Aye.

11 The Clerk. Mr. Baucus?

12 Senator Baucus. Aye.

13 The Clerk. Mr. Boren?

14 Senator Boren. Aye.

15 The Clerk. Mr. Bradley?

16 Senator Bradley. Aye.

17 The Clerk. Mr. Mitchell?

18 Senator Mitchell. Aye.

19 The Clerk. Mr. Pryor?

20 Senator Pryor. Aye.

21 The Clerk. Mr. Chairman?

22 The Chairman. Aye.

23 (Extended applause)

24 The Chairman. The committee will meet at 8:30 in the  
25 morning -- no, no, no, no.

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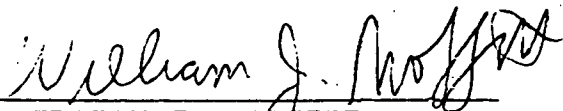
(Laughter)

The Chairman. We are adjourned.

(Whereupon, at 12:19 a.m., the Executive Committee session was adjourned.)

C E R T I F I C A T E

1  
2 This is to certify that the foregoing proceedings of an  
3 Executive Session on Tax Reform of the Senate Committee on  
4 Finance, held on May 6, 1986, were as herein appears, and that  
5 this is the original transcript thereof.  
6  
7

8 

9 WILLIAM J. MOFFITT  
10 Official Court Reporter  
11

12 My Commission expires April 14, 1989.  
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# United States Senate

COMMITTEE ON FINANCE  
WASHINGTON, DC 20510

WILLIAM DIEFENDERFER, CHIEF OF STAFF  
WILLIAM J. WILKINS, MINORITY CHIEF COUNSEL

Press Release No. 86-042

## P R E S S   R E L E A S E

FOR IMMEDIATE RELEASE  
Monday, May 5, 1986

Contact: Betty Scott-Boom  
(202) 224-4515

### FUNDAMENTAL TAX REFORM -- THE 27% SOLUTION

A new proposal for fundamental tax reform supported by a bipartisan group of Finance Committee Members includes the following elements:

- Simplicity - There will be only two rates for individuals: 15% and 27%. This will cut the top rate almost in half.
- 80% of Americans will have a top rate no higher than 15%;
- This will be the lowest individual top rate in over half a century;
- Approximately 6 million of the working poor will be moved off the Federal income tax rolls;
- A family of four making up to \$13,000, \$530 above the poverty line, will pay no Federal income taxes;
- Fairness is restored to the tax system through tough anti-sheltering and minimum tax rules.

While significantly reducing Federal income tax rates, the proposal also permits the following deductions:

- Home mortgage interest;
- State and local income taxes;
- State and local real property taxes;
- Charitable contributions/medical expenses;
- Casualty losses.

The following benefits will be retained and/or increased:

- Standard deduction for single, joint and head of household taxpayers - increased;
- Personal exemption - increased to \$2,000;
- \$600 standard deduction for the elderly and blind;
- Earned income tax credit for lower income taxpayers - increased;
- Child care credits - retained.

How is all of this paid for?



## EXTENSION OF RENEWABLE ENERGY TAX CREDITS

Present Law: Energy tax credits for qualifying renewable energy property, including solar, geothermal, biomass, ocean thermal energy conversion systems (OTEC), and wind, expired on December 31, 1985. Tax credits for qualifying hydroelectric property remain available until December 31, 1988 if an application for a hydro project was docketed at FERC before January 1, 1986.

Chairman's Proposal: The current proposal deletes the Chairman's prior recommendation which called for an extension of the business and residential energy tax credits until 1995.

House Bill: Extends through 1988 the residential solar credits at reduced rates -- 30% in 1986 and 20% in 1987 and 1988; and, extends through 1988 the business solar and geothermal energy tax credits, also at reduced rates of: solar -- 15% in 1986; 12% in 1987; and 8% in 1988; and geothermal -- 15% in 1986 and 10% in 1987 and 1988. Tax credits for other renewable energy property, i.e., biomass, OTEC and wind would not be extended; although the affirmative commitment rule for hydro -- allowing eligibility for the credit through 1988 -- would remain.

Proposal:

1. Re-instate and extend the business energy tax credits for solar, geothermal and OTEC as follows:

	1986	1987	1988	1989	1990
Solar	15%	12%	12%	8%	8%
Geothermal	15%	10%	10%	10%	10%
OTEC	15%	15%	15%	15%	15%

2. Re-instate and extend the business energy tax credit for wind and biomass and provide an affirmative commitments provision as follows:

	1986	1987	1988	1989	1990
Wind	15%	10%	provide an affirmative commitments provision for a qualifying project		
Biomass	15%	10%	provide an affirmative commitments provision for a qualifying project		

3. Re-instate and extend the residential solar credit as provided in the House-passed tax bill; i.e. 30% in 1986 and 20% in 1987 and 1988 with a limit of \$5000.

Rationale: The amendment is intended to retain some semblance of parity between the renewable energy industry and traditional oil, gas and other fossil fuel industries. The current proposal retains incentives for fossil fuel production. Elimination of the most important renewable energy industry incentive -- the energy tax credit -- would have a devastating impact on renewables, already deeply depressed by the steep decline in energy prices.

May 6, 1986

**HEINZ PROPOSAL ON CORPORATE RATE AND MINIMUM TAX**

1. For the corporate and individual minimum tax, the depreciation preference for both real and personal property would be changed to require straight-line treatment, not over the ADR midpoint life as under the Chairman's proposal, but instead over the ACRS life.

2. Investment credit carryovers and transition investment credits would be allowed to offset up to 70 percent of minimum tax liability.

3. The corporate regular tax rate would be raised by the amount necessary to pay for the first two changes.

~ 3/4

## ARMSTRONG/MOYNIHAN AMENDMENT

### TO RETAIN THE FULL DEDUCTION FOR BUSINESS MEAL AND ENTERTAINMENT EXPENSES

#### CURRENT LAW

Deductions are allowable for ordinary and necessary expenditures paid or incurred in carrying on a trade or business or for the production or collection of income.

Expenditures generally considered to constitute entertainment, amusement, or recreation are deductible only if the taxpayer establishes that 1) the item was directly related to the active conduct of the taxpayer's business or 2) associated with the active conduct of the taxpayers business.

Expenses for food and beverage are deductible without regard to the "directly related" or "associated with" requirements generally applicable to entertainment expenses, if the food or beverage is consumed in a place conducive to business discussion.

Substantiation requirements apply to deductions for travel, entertainment, and certain gift expenses.

#### ARMSTRONG/MOYNIHAN AMENDMENT

The amendment would retain 100% deductibility for business meals and entertainment.

The amendment would retain provisions in the Packwood proposal directing the Secretary of Treasury to tighten substantiation requirements and apply them to business meals. Special fraud and negligence penalties would apply to improper transactions.

#### REASONS FOR THE AMENDMENT

1. It's fair. With all other business expenses remaining fully deductible (advertising, marketing, art work, etc.) why single out this one area?
2. The hospitality industry is diverse and is an important segment of our economy. It employs millions of people, creates jobs in related industries and provides revenues to both state and federal governments. Chase Econometrics has found that industry sales would decline by \$32 billion over the next two years, jobs would be lost and state and local tax revenues would decline by \$1 billion. Australia's experience verify's this.
3. The cultural and sports facilities available to our citizens; performing art centers, playhouses, symphonies, stadiums and the like, are largely supported by the business community. These groups are extremely concerned about the consequences of the proposal to restrict entertainment deductions.
4. Abuses can be handled by more vigorous substantiation requirements rather than by targeting the cultural, restaurant, hotel and sports industries for differential treatment under the tax code..

MOYNIHAN AMENDMENT ON STATE AND LOCAL GENERAL SALES TAXES

The proposal would be amended as follows:

Two-thirds of all itemized state and local general sales taxes would be deductible. The top corporate tax rate would be raised from 33 to 34 percent.

The amendment is revenue neutral.

**BAUCUS COMPLIANCE AMENDMENTS**

1. Direct Secretary of the Treasury to implement a publicly announced Voluntary Disclosure policy, i.e., full disclosure of violations of the tax laws made before the eligible disclosing taxpayer (or related party) receives IRS notice of inquiry or investigation of his tax affairs would guarantee immunity from prosecution for tax crimes. The Secretary is directed to issue regulations regarding eligibility and other administrative requirements by December 31, 1986.

2. Direct the Secretary of the Treasury to implement a comprehensive publicity campaign about the Voluntary Disclosure policy and a continuing public relations program to restore public confidence in the federal tax system. Voluntary disclosure policy publicity to include, as a minimum, public press releases, annual notices to taxpayers, and notice in IRS publications for general public usage.

3. Increase substantial understatement penalty from 10% to 20%.

## FUNDAMENTAL TAX REFORM -- THE 27% SOLUTION

A new proposal for fundamental tax reform supported by a bipartisan group of Finance Committee Members includes the following elements:

- Simplicity - There will be only two rates for individuals: 15% and 27%. This will cut the top rate almost in half.
- 80% of Americans will have a top rate no higher than 15%;
- This will be the lowest individual top rate in over half a century;
- Approximately 6 million of the working poor will be moved off the Federal income tax rolls;
- A family of four making up to \$13,000, \$530 above the poverty line, will pay no Federal income taxes;
- Fairness is restored to the tax system through tough anti-sheltering and minimum tax rules.

While significantly reducing Federal income tax rates, the proposal also permits the following deductions:

- Home mortgage interest;

- State and local income taxes;
- State and local real property taxes;
- Charitable contributions;
- Medical expenses;
- Casualty losses.

The following benefits will be retained and/or increased:

- Standard deduction for single, joint and head of household taxpayers - increased;
- Personal exemption - increased to \$2,000;
- \$600 standard deduction for the elderly and blind;
- Earned income tax credit for lower income taxpayers - increased;
- Child care credits - retained.

How is all of this paid for?

- By closing corporate loopholes and special tax privileges - approximately \$100 billion;

- By eliminating the ability of individuals to avoid paying taxes by using tax shelters - \$50 billion;
- By eliminating the individual capital gains exclusion -- a tax expenditure worth \$220 billion under present law, 71% of which is presently claimed by individuals earning over \$200,000;
- By imposing a stiff minimum tax on individuals and corporations assuring that wealthy individuals and profitable corporations will have to pay some tax - \$40 billion.

Making future IRA contributions available only to those not covered by pension plans (other than social security) - \$30 billion.

The proposal sets a top corporate rate of 33%, down from a top rate of 46% under current law.

No changes are made to current law for excise taxes.



SPREADSHEET MODIFICATIONS

(page numbers refer to pages in the spreadsheets)

I. Individual (1 - 15)

Include the provisions from the spreadsheets, except:

- A. Provide for 15% and 27% tax rates and an increased standard deduction, as follows:

	<u>Single</u>	<u>Joint</u>	<u>Head of Household</u>
Standard deduction	\$ 3,000	\$ 5,000	\$ 4,400
27% break point	\$17,600	\$29,300	\$23,500

- B. Phase out the benefit of the 15% bracket for high-income taxpayers between \$75,000 and \$145,320 for joint returns, and between \$45,000 and \$87,240 for singles, and between \$55,000 and \$111,400 for heads of households.
- C. Provide a \$2,000 personal exemption beginning in 1988 and (\$1,900 in 1987) to be phased out between \$145,320 and \$185,320 for joint returns, \$87,240 and \$127,240 for singles, and \$111,400 and \$151,400 for heads of households.
- D. Delete the limitation on itemized deductions for individuals in the highest tax bracket.

- E. Round the indexed standard deduction, personal exemption, rate brackets, and earned income credit down to the nearest \$50.
- F. Disallow the personal exemption for individuals who are eligible to be claimed as a dependent by another taxpayer.
- G. Retain the deduction for personal property taxes.
- H. Retain current law for taxation of scholarships and fellowships.
- I. Allow the charitable contributions deduction for non-itemizers to sunset as scheduled.
- J. Increase the threshold for the medical deduction from 5% to 10%.
- K. Repeal the adoption deduction.
- L. Repeal the deduction for miscellaneous itemized deductions. As in the spreadsheets, retain the deduction for unreimbursed employee business expenses currently available to taxpayers who do not itemize their deductions, subject the deduction to a 1% floor, and limit the deduction to itemizers.

INCOME DISTRIBUTION

<u>Income Class</u> (Thousands of 1986 Dollars)	<u>Percentage Change</u> <u>in Income</u> <u>Tax Liability</u> <u>1988</u>
Less than \$10	-62.2
\$10 - 20	-18.0
20 - 30	- 8.0
30 - 40	- 5.0
40 - 50	- 6.5
50 - 75	- 3.7
75 - 100	- 3.2
100 - 200	- 3.6
200 and above	- 4.7
 TOTAL	 - 6.2

Joint Committee on Taxation  
May 4, 1986

II. Accelerated Cost Recovery System (16 - 23)

Include the provisions from the spreadsheets as amended by the Committee, except:

- A. For all property in the 5 and 10-year class, apply 200% declining balance, switching to straightline.
- B. Provide a \$10,000 annual limit on expensing for small business.
- C. Place oil refinery property in the 10-year class.
- D. Place research and experimentation property in the 5-year class until December 31, 1989, and in the 3-year class thereafter.
- E. Place all real estate in the 30-year class.

- F. Reduce the investment tax credit for investment tax credit carryovers and for transition property by 30%.
- G. Delete the mandatory refund of investment tax credit carryovers.

III. Accounting (24 -29)

Include the provisions from the spreadsheets as amended by the Committee, except:

- A. Delete the dollar value LIFO provision.
- B. Delete limits on use of cash accounting.
- C. Extend the installment sales provision to real property.
- D. Limit the bad debt reserve provision to non-finance companies.
- E. Require utilities to accrue earned but unbilled income.
- F. Conform taxable years of "grandfathered" partnerships, S corporations, and personal service corporations more closely to taxable years of owners.

- G. Tax regulated investment companies on a calendar year basis, and eliminate the ability to pay spill over dividends.

IV. Capital Gains (30 - 32)

Include the provisions from the spreadsheets, except:

- A. Repeal the capital gains exclusion and replace it with a rate structure parallel to that applicable to individuals.
- B. Delete the small business participating debentures provision.

V. Compliance (33 - 44)

Include the provisions from the spreadsheets, except:

- A. Provide for increased IRS funding for agents, audits, and modernization of compliance systems, funded by the following amounts (\$ billions) of interest and penalty receipts of the IRS:  
FY 1987 -- \$6.1; FY 1988 -- \$6.2; FY 1989 -- \$6.3;  
FY 1990 -- \$6.35; FY 1991 -- \$6.4.
- B. Delete the provision requiring the IRS to pay interest on certain refunds.

VI. Corporate Taxation (45 - 63)

Delete all provisions from the spreadsheets, except:

- A. Retain the corporate tax rate provisions, but change the top rate from 35% to 33%.
- B. Retain the provision reducing the dividends received deduction to 80%.
- C. Retain the provision repealing the dividend exclusion for individuals.
- D. Retain stock redemption expense provision.
- E. Retain the NOL carryover provision.
- F. Retain the bus operating rights provision.
- G. Retain the 75% limitation on business credits.

VII. Energy and Natural Resources (64 - 75)

Include the provisions from the spreadsheets, as amended by the Committee, except:

- A. Delete the residential and business energy tax credits.

VIII. Excise and Employment Taxes (75 - 77)

Retain current law, except:

- A. Include the provision increasing the quarterly payroll threshold for agricultural wages from \$20,000 to \$40,000.
- B. Increase the threshold for accelerated payroll tax deposits from \$3,000 to \$5,000.

IX. Financial Institutions (78 - 81)

Retain current law.

X. Foreign (82 - 106)

Include the provisions from the spreadsheets as amended by the Committee, except:

- A. Retain current law for FIRPTA.
- B. Provide a study of the extent to which the U.S. reinsurance industry faces significant competitive disadvantage as a result of U.S. tax treaties, and

to the extent that significant competitive disadvantages are present, the Secretary of the Treasury shall renegotiate such treaties to eliminate the disadvantage.

XI. Insurance (107 - 114)

Include the provisions from the spreadsheets.

XII. Interest Expense (115 - 116)

Include the provisions from the spreadsheets, except:

- A. Reduce the limitation from \$1,000 (\$2,000 for marrieds filing jointly) to zero.
- B. Interest disallowed under the new provisions would become subject to disallowance by a rate of one-third in 1987, two-thirds in 1988, and fully in 1989 and thereafter.

XIII. Minimum Tax (117-123)

Include the provisions from the spreadsheets, except:

- A. Apply the passive loss preferences beginning in 1987.
- B. Delete tax-exempt bond interest as an enumerated preference.



- C. Retain amortization of pollution control equipment as a preference.

XIV. Pensions (124-173)

Include the provisions from the spreadsheets as amended by the Committee, except:

- A. Limit the deduction for contributions to IRAs to persons who do not participate in an employer's retirement arrangement.
- B. Repeal the 3-year basis recovery rule, beginning for individuals whose annuity starting date is on or after January 1, 1989. If the annuity starting date is after December 31, 1987 and before January 1, 1989, 50% of the basis would be recovered under the 3-year rule and the remaining 50% would be recovered under the new basis recovery rule.
- C. Increase retirement ages for qualified plan purposes to retirement ages applicable to Social Security with true actuarial reduction for the limit on early retirement benefits and eliminate the \$75,000 floor on actuarial reduction of the limit. This does not apply to the special classes of employees (police, firefighters, pilots, and correctional officers).

D. Do not extend 401(k) plans to state and local governments. This provision would not apply to plans adopted before March 1, 1986.

E. Reduce the cap on sec. 401(k) elective contributions to \$7,000.

XV. Research and Development (174-176)

Include the provisions from the spreadsheets, except:

A. Extend the 25% incremental credit to December 31, 1989.

XVI. Tax Shelters and Real Estate (177-185)

Include the provisions from the spreadsheets, except:

A. Include a provision to limit the deduction for passive losses by individuals and personal service corporations as follows:

1. Losses and credits from all businesses in which the taxpayer does not materially participate and from all rental activities could be used only to offset income from such activities.

2. Any net loss or credit remaining from 1 above could be carried over to future years. In addition, up to \$25,000 (phased out between

incomes of \$100,000 and \$150,000) of losses or equivalent credits from rental real estate activities in which the taxpayer materially participates could be used to offset income not subject to the limitation described in 1 above (e.g., wages, portfolio income and income from active trades or businesses other than rental real estate).

3. These rules would reduce the otherwise available deduction for passive losses by one-third in 1987, two-thirds in 1988, and fully in 1989 and thereafter.
4. The rules in 1 and 2 above would apply to the passive loss provision in the minimum tax.

B. Modify the low-income housing credit as follows:

1. No trade-in of tax-exempt bond authority would be required. The credit would not be allocated by any governmental unit. There is no volume cap on the tax credit.
2. The 5% annual tax credit for units occupied by individuals with incomes of 50% of area median income or less would be increased to an 8% tax credit (with a present value of almost 60%), available for 10 years.

3. A tax credit of 4% of the basis of units (present value of almost 30%) occupied by individuals with incomes between 50% and 70% of area median income (adjusted for family size), would be available annually for 10 years. This credit could be claimed on a maximum of 30% of all units in a project.
4. The credits would be treated as arising with respect to rental real estate activities in the operation of which the taxpayer materially participates.
5. An anti-"double-dipping" rule would be provided to preclude multiple subsidies for low-income units.

C. Include secondary mortgage market provisions to clarify rules for securitizing and reselling mortgages.

XVII. Tax-Exempt Bonds (186 - 209)

Include the provisions from the spreadsheets as amended by the Committee, except:

- A. Retain current law sunsets for mortgage revenue bonds and small issue IDB's.

- B. As under current law, reduce the IDB volume cap from \$150 per capita to \$100 per capita.
- C. Eliminate mass transit industrial development bonds.

XVIII. Trusts and Estates (210 - 217)

Include the provisions from the spreadsheets as amended by the Committee, except:

- A. Modify the tax rates applicable to trusts to conform to the tax rate schedule adopted by the Committee.
- B. Delete indexing of gift and estate tax brackets.

XIX. Miscellaneous Provisions (218 - 221)

Delete all provisions from the spreadsheets, except:

- A. Retain the architectural barriers provision.
- B. Retain the Vietnam MIA provision.
- C. Retain the title-holding companies provision.

ESOP AMENDMENT

FY 1987-91  
(\$ Billions)

<u>Deduction for ESOP dividends.</u> Extend to dividends used to repay ESOP loans.	-0.1
<u>Estate Tax Exclusion.</u> Allow an exclusion from an estate for 50% of the proceeds realized on an estate's sale of stock to an ESOP.	-0.3
<u>ESOP Loans.</u> Extend interest exclusion to loans matched by contributions of stock to an ESOP; extend exclusion to loans by mutual funds.	-0.1
<u>Early Withdrawal Tax.</u> Exempt ESOPs from excise tax on early withdrawals from pension plans.	-0.2
<u>Tax Credit ESOPs.</u> Advance expiration date from 12/31/87 to 5/31/87.	<u>+1.3</u>
	Total: +0.6

TECHNICAL AND CLARIFYING AMENDMENTS

\* Put Option for Stock Bonus Plans. Extend the ESOP put option requirement to stock bonus plans.

\* ESOP Allocations. Amend the prohibited group definition in Sec. 415(c)(6) to conform to the definition of highly compensated employee in the Chairman's Proposal.

\* Distributions on plan termination. Allow distributions upon termination of an ESOP or a 401(k) plan; alternatively, allow shares to be sold and the proceeds transferred to another plan.

\* Distributions and form of payment. Shorten the period over which distributions may be made and modify the put option rules.

\* Intent of Congress. Add to the U.S. Code a statement of Congressional intent similar to that adopted in the Tax Reform of 1976 stating: "The Congress has made clear its interest in encouraging employee stock ownership plans as a bold and innovative technique of finance for strengthening the free private enterprise system. The Congress intends that such plans be used in a wide variety of corporate financing transactions as a means of encouraging employers to include their employees as beneficiaries of such transactions. The Congress is deeply concerned that the objectives sought by this series of laws will be made unattainable by regulations and rulings which treat employee stock ownership plans as conventional retirement plans, which reduce the freedom of employee stock ownership trusts and employers to take the necessary steps to utilize employee stock ownership plans in a wide variety of corporate transactions, and which otherwise impede the establishment and success of these plans."

ESOP AMENDMENTFY 1987-91  
(\$ Billions)

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<u>Tax Credit ESOPs.</u> Advance expiration date from 12/31/87 to 5/31/87.	<u>+1.3</u>
	Total: +0.6



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BAUCUS COMPLIANCE AMENDMENTS

1. Direct Secretary of the Treasury to implement a publicly announced Voluntary Disclosure policy, i.e., full disclosure of violations of the tax laws made before the eligible disclosing taxpayer (or related party) receives IRS notice of inquiry or investigation of his tax affairs would guarantee immunity from prosecution for tax crimes. The Secretary is directed to issue regulations regarding eligibility and other administrative requirements by December 31, 1986.
2. Direct the Secretary of the Treasury to implement a comprehensive publicity campaign about the Voluntary Disclosure policy and a continuing public relations program to restore public confidence in the federal tax system. Voluntary disclosure policy publicity to include, as a minimum, public press releases, annual notices to taxpayers, and notice in IRS publications for general public usage.
3. Increase substantial understatement penalty from 10% to 20%.

New York Times, Sunday, May 4, 1986

## Tax Reform Alive Again

The battered bill to rewrite the Federal tax code suddenly breathes again. The Senate Finance Committee, which only two weeks ago seemed determined to write a worse code, is now considering a dramatic shift that comes close to true reform. The promise of such a breakthrough is exciting. What seems to be needed to move it to the floor is a strong dose of political fortitude.

Chairman Bob Packwood, an Oregon Republican, stopped committee voting on the tax bill 10 days ago when it promised only to open more loopholes than it closed. Known to be unenthusiastic about reform, he seemed ready to ditch the whole thing. Instead, and without a blush, he has introduced a new bill that is strikingly similar to the Democrats' old Bradley-Gephardt plan, the so-called flat tax that gave the reform movement much of its initial push.

The Packwood plan's most riveting feature is it would reduce the top personal income tax rate to 27 percent. That compares with 50 percent in current law, 35 percent in President Reagan's proposal and 38 percent in the House bill. To preserve revenues despite this cut — and a matching cut in the corporate rate — Mr. Packwood adopts other stunning ideas: wipe out the preferential tax rate for capital gains, sharply curtail tax shelters, discontinue most exemptions for Individual Retirement Accounts and end the deductibility of state and local sales taxes.

The rate reduction alone is radical enough to force the committee to stop and think again. If personal and corporate tax rates could really be slashed, a major assault on exemptions may be politically feasible after all.

Actually, the plan offers less real tax relief for individuals than meets the eye. The reduction in personal tax liabilities, in dollars, would be substantially smaller than under the House bill — \$105 billion over five years as against \$140 billion — because the Packwood plan eliminates more deductions. But the bills are similar in their distribution of benefits among lower-, middle- and upper-income brackets and in dropping about six million low-income taxpayers from the rolls altogether.

For corporations, the net effect of the Packwood package would be substantially less painful than the House bill, despite marked increases in some categories. Mr. Packwood's depreciation allowances would also be somewhat more generous than current law, whereas the House made them tighter. Banks would keep an important current tax advantage but would lose most of their booming business in exempt retirement accounts.

The Packwood plan could be further improved and would surely be altered in many respects on the way to final passage. As is, it marks a promising revival of a tax revision effort that had gone sour. Better yet, it rekindles the flame of true reform.

*Rowland Evans and Robert Novak*

# Packwood's Inchon Landing

Long-term political fallout will be at stake in the Senate Finance Committee this week when Chairman Bob Packwood, with Senate Majority Leader Robert J. Dole's powerful presence on his side, seeks one or two additional Republican votes needed to pass his streamlined tax-reform package.

Support has picked up quickly for the chairman's week-old package, which drops the top marginal income tax rate to 27 percent and closes \$50 billion worth of real estate and oil tax shelters. Nine of the 11 senators needed seemed on board going into today's session, with a good chance for going over the top.

That vote can determine whether this year's tax bill will have the flavor of the House Democratic bill or carry a Republican label—a political distinction transcending this year's election. While Washington's relentless lobbyists have convinced much of Congress that people don't care about tax reform, the Finance Committee is voting on a bill offering fairness, simplification and—not least important—lower taxes for millions of ordinary Americans.

This is dramatic improvement from the choice less than two weeks ago between the flawed House-passed reform and an even worse Senate bill. What changed it was Packwood's "Inchon landing" (as described by Rep. Jack Kemp in a local fund-raising speech for the chairman last week). Packwood leapfrogged Rep. Dan Rostenkowski's bill by proposing truly radical tax reform.

To cynical tax-watchers, that was a clever ruse by Packwood to kill reform but take the onus off himself by offering up an unpassable proposal. In fact, during 16 months as chairman, Packwood has converted to the goal of lowered tax rates financed by closing shelters.

What's more, his proposal instantly pulled back waverers. Sen. Bill Bradley of New Jersey, the leading Democratic tax reformer, had been ready to go political and accuse Republicans of killing reform, but now is back home. Other Democrats in support include Sens. Daniel Patrick Moynihan of New York, George Mitchell of Maine and maybe Lloyd Bentsen of Texas.

Most important was the quiet shift from neutrality to support by the majority leader, Packwood's predecessor as chairman and still a Finance Committee member. Dole's ambiguity was ended by the Inchon landing. Other Republicans on the committee are not eager to provide the decisive votes against reform.

Thanks to Oregon politics, the showdown is now. Packwood must leave Washington to face the challenge in the May 20 Republican primary from New Right candidate Joe Lutz, who accuses the chairman of selling out to special interests.

Finance members will be voting on radical tax reform, though a tad less

radical than the new scheme unveiled by Packwood April 24. Home mortgage, state and local taxes and charitable contributions are fully deductible in the new version; President Reagan's \$2,000 personal exemption is retained. To pay for this, Packwood's 25 percent rate inched up to 27. But the heavy revenue—\$50 billion—comes from closing famous tax shelters, mostly in real estate, that generate huge paper losses.

The argument by business lobbyists that this is not real tax reform no longer washes. Republicans must choose. On one hand is a bill with rates of 27 percent for individuals and 33 percent for corporations, with a 15 percent rate for families with less than \$40,000 income—about 80 percent of all taxpayers. On the other hand are special business interests traditionally generous to Republicans.

Actually, more difficult for Republi-

can senators than an up-or-down vote on the Packwood plan will be a deluge of amendments to retain tax exclusions. But the choice is not between it and no bill at all. Packwood intends as a worst-case scenario to pass a minimum tax that would go into conference with the House bill. Thus, the president's long quest for tax reform could result in either passage of a basically Democratic bill or its death at Republicans hands—in Congress or by presidential veto.

Although a preoccupied White House may not appreciate it, Bob Packwood's Inchon landing is the best hope for saving Reagan's second-term domestic priority. The Treasury understands, which is why Deputy Secretary Richard G. Darman cancelled his trip to the Tokyo summit to sit in on Finance Committee voting.

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## Mr. Packwood's New Tax Plan

**S**ENATE FINANCE Committee Chairman Bob Packwood has done a sensible thing. He has dropped the old fights he was losing on tax reform and picked some new ones he may be able to win. His new proposal still has some pretty big blanks to be filled in, and it is not clear it can pass his jaded committee. But in some ways the new plan would produce the most reform—the simplest, fairest code—of any such plan so far.

What hung the committee up as it went through Mr. Packwood's earlier ideas last month were the tax circumstances of particular industries. For favored industries, members kept wanting to vote not less preferential treatment, but more. Mr. Packwood has now cut his losses by agreeing to leave the best-protected of these provisions alone. He would repeal the investment tax credit, which now costs the Treasury \$25 billion a year; move against a page-long list of lesser preferences; then impose a fairly stiff minimum corporate income tax to limit the use any company could make of all the available preferences in any one year.

The proceeds from all this would be enough to reduce the corporate income tax rate from 46 percent to 33 percent and leave about \$100 billion over five years to pay for individual income tax reduction. The earlier Packwood plan had, in addition, used excise tax increases to pay for this, but he has now abandoned that idea. Excise taxes are regressive, and they were also costing Mr. Packwood the support of industries previously well-disposed to reform. Here again he cut his losses.

On the individual side, the chairman would leave (though in several cases curtail) the familiar and redoubtable itemized deductions for medical expenses, state and local taxes, interest and charitable contributions; limit the use of IRAs to people without pensions; then tear the roof off most tax shelters by forbidding the use of their paper losses to shelter ordinary income; and finally, take

away the preferential treatment historically accorded capital gains.

These last two steps especially would produce large amounts of revenue. That plus the excess from the corporate sector would be used to reduce individual rates to 15 percent for most people and 27 percent at the top (from 50 percent at the top now, and 70 percent when President Reagan came to office). The personal exemption and standard deduction would also be raised; for most people, the exemption would become \$2,000.

This provocative plan is good reform because:

It would help the poor. The personal exemption and standard deduction combine to set the tax threshold, below which no one pays. The new plan would lift this well above the poverty line—and while cutting the income taxes of the poor would not also raise their excise taxes. Excise tax increases would be left, if needed, to help reduce the deficit.

At the opposite end of the income scale, the rich could no longer obscure their true income for tax purposes through tax shelters. It would be harder for them not to pay. The same would be true for corporations, by virtue of the corporate minimum. Corporate income taxes would be lifted back toward the level where they belong as a source of support for the government.

With only two rates and without the distinction between ordinary income and capital gains, the system would also be much simpler. The big question is whether the committee will go along with the chairman on dropping the preferential treatment of gains. This is crucial both for fiscal and distributional reasons. Gains accrue mostly to the rich, and loss of this preference is one of the main ways they would pay for their lower rates. The argument will be made that the republic will fall without a capital gains distinction. We rather doubt that. At a top rate of 27 percent, those with investment income will still do just fine.

The Finance Committee ought to vote aye, and move its chairman's bill along.

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*Editorial Page Editor*

Monday, April 28, 1986

## At last, real tax reform

For the past couple of years when President Reagan and the tax-writers in Congress have talked about "tax reform," they have played fast and loose with the meaning of the words.

The White House and House and Senate committees have proposed tax revision, tax overhaul, tax rejiggering and even the opening of new loopholes, but not true reform, which consists of putting far more simplicity and fairness into the system.

Now, at long last, something that honestly can be called tax reform is on the table, and it comes from an unlikely source, Chairman Bob Packwood of the Senate Finance Committee.

Until last week, Sen. Packwood did a poor job of leading his committee toward tax equity. An Oregon Republican, Sen. Packwood tried to protect his timber-producing state from its fair share of taxes, which inspired committee members to slip in their own tax breaks.

The committee knew it was working on a rotten bill, one that could not stand scrutiny. Sen. Packwood suddenly stopped drafting the measure and produced a plan of radical, drastic reform of the tax code.

Instead of today's 14 income tax brackets ranging from 11 percent to 50 percent, Sen. Packwood would have only two rates for individuals: 15 percent and 25 percent. He

would pay for the sharply lower rates by eliminating all itemized deductions.

The top corporate tax rate would drop to 33 percent from the current 46 percent. Preferential tax treatment for capital gains would disappear, as would the investment tax credit.

Over five years, the proposal would cut individual taxes by \$90 billion, raise corporate taxes by \$75 billion and prevent revenue loss by boosting excise taxes \$25 billion.

Sen. Packwood would go much farther in bracket-lowering and deduction-ending than the president, who called for a top income tax rate of 35 percent for individuals and corporations. Both men would almost double the personal exemption to \$2,000.

Of course, Sen. Packwood's surprise proposals will face fierce opposition. High-tax states will struggle to retain the deductions from which they benefit.

And it may be too late in the congressional session for any tax bill to pass, let alone one as contentious as Sen. Packwood's. Nevertheless, he has performed a service.

If this country ever succeeds in treating all income and fringe benefits alike for tax purposes, it could run the government with a top bracket of 20 percent, which no one should mind paying.