

EXECUTIVE SESSION

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TUESDAY, JULY 24, 1979

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United States Senate
Committee on Finance,
Washington, D.C.

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8 8 The committee met, pursuant to notice, at 10:15 a.m. in
9 room 2221, Dirksen Senate Office Building, Hon. Russell B.
10 Long, chairman of the committee, presiding.

11 9 Present: Senators Long, Talmadge, Moynihan, Baucus,
12 Boren, Bradley, Dole, Packwood, Roth, Chafee, Heinz, and
13 Wallop.

14 10 The Chairman: This meeting will come to order.

15 11 It is my understanding, Mr. Stern, that the nomination of
16 Susanna B. McBee has been withdrawn?

17 12 Mr. Stern: That is correct, sir.

18 13 The Chairman: The next order of business, then, is the
19 targeted fiscal assistance.

20 14 Would you explain that, Mr. Morris?
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1 Mr. Morris: Mr. Chairman, in 1976 and 1977, the Congress
2 adopted a program of anti-recession fiscal assistance which
3 distributed approximately \$3 billion to state and local
4 governments with high rates of unemployment during that
5 period.

6 Last year, the Finance Committee reported a bill, H.R.
7 2852, that would have modified and extended that program for
8 an additional period of time. That legislation was passed by
9 the Senate but was not acted upon by the House.

10 This year, two bills have introduced, S. 200 and S. 566,
11 that would once again put into place a targeted fiscal
12 assistance program and an anti-recession fiscal assistance
13 program.

14 On page 2 of the materials that hve been distributed to
15 you, there is a chart showing the fiscal impact for fiscal
16 year 1980 of a targeted fiscal assistance program and a
17 possible countercyclical assistance program under S. 566,
18 under S. 200 and under a possible alternative for committee
19 consideration.

20 The unemployment figures that are used in connection with
21 these estimates are those supplied by the administration and
22 in footnote number 1 in that table, you will see that
23 projected rates of unemployment for 1979, the second quarter,
24 are 5.9 percent; 6.3 percent for the third quarter of '79 --
25 that is on page 2 of the materials on supplementary fiscal

1 assistance and anti-recession fiscal assistance in footnote
 2 number 1 -- and it shows unemployment projected at 6.6 percent
 3 for the fourth quarter of '74 and 6.8 percent for the first
 4 quarter of 1980.

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1 Those are the quarters which would determine the amount
2 of money that would be distributed under these programs if the
3 Committee were to approve these programs. There are somewhat
4 more pessimistic estimates on unemployment made by the
5 Congressional Budget Office and outside forecasters.

6 Under the proposed alternative for Committee
7 consideration under targeted fiscal assistance, it would be
8 distributed \$150 million for fiscal year 1969 and \$340 million
9 for fiscal year 1980.

10 If unemployment goes over 6.5 percent, the
11 countercyclical assistance program would trigger into effect
12 and would distribute about -- based on the administration
13 estimates, \$195 million in additional funds.

14 Based on a somewhat more pessimistic assumption with
15 respect to the rate of unemployment, that amount of money
16 could jump to a maximum of \$800 million in total for both
17 targeted fiscal assistance and countercyclical assistance.

18 On page 3 of the materials is a chart that compares the
19 differences between S. 200, S. 566 and an alternative proposed
20 for committee consideration. I am sorry; page 4 of the
21 materials.

22 Under each of the progrms there would be an amount
23 distributed for fiscal year '79 under the alternative that has
24 been proposed for the Committee and \$150 million will be
25 distributed for fiscal year 1979; \$340 million for fiscal year

1 '80.

2 In order to be eligible to receive funds, a unit of local
3 government would have to have an unemployment rate of 6
4 percent or above, and for 1978, this would be based on an
5 average rate of unemployment for the entire year of -- for
6 1979, it would be based on the average unemployment for 1978
7 and for periods after 1979, it would be based on a moving six
8 month average unemployment rate.

9 There would be 1 percent of the total amount set aside to
10 be distributed to the territories based on population and in
11 order to participate in the program, each local government
12 would have to receive at least \$10,000 on an annual basis, or
13 \$2,500 per quarter and in order to make sure that certain very
14 wealthy areas would not receive assistance, there is a cap, so
15 any area with per capita income above 150 percent of the
16 national average would not receive assistance.

17 There would be one exception. If an area had
18 unemployment over 10 percent, regardless of their per capita
19 income level, they would receive assistance.

20 For fiscal year 1979, there would be one payment made for
21 the entire year to each recipient. For fiscal year 1980, the
22 allocations would be made quarterly and if there were
23 allocations of less than \$10,000 per quarter their allocation
24 would be sent out along with their general revenue sharing
25 payment.

1 Under the countercyclical assistance part of the program,
2 that program would go in effect if national unemployment would
3 go above 6.5 percent. It would turn off if unemployment went
4 below 6.5 percent for one quarter.

5 The amount of money that would be distributed would be
6 \$125 million dollars plus an additional \$30 million for each
7 one-tenth of a percentage point that unemployment exceeds 6.5
8 percent for the quarter.

9 The maximum amount that could be distributed under this
10 countercyclical program would be \$1 billion for a calendar
11 year. The recipients, both state and local governments, would
12 receive money under the countercyclical program, and they
13 would each have to have unemployment above 6 percent for two
14 quarters.

15 Under the countercyclical part of the program, the states
16 would get one-third of the amounts distributed and the local
17 governments would get two-thirds and there would be a 1
18 percent amount set aside for the territories. Again,
19 there would be a \$125 minimum quarterly allocation in order
20 for local governments to receive funds, and there would be a
21 similar cap with respect to the per capita income level of the
22 recipient governments and the distribution of funds would be
23 on a quarterly basis.

24 The Chairman: Senator Bradley, you are Chairman of that
25 Subcommittee. You might favor us with your suggestions.

1 Senator Bradley: Mr. Chairman, we had three hearings on
2 this subject and tried to work out a compromise among all of
3 the parties on the two bills that were submitted, and I feel
4 that the committee alternative meets the specifications of
5 both Senators Danforth and Durenberger and also Senator
6 Moynihan and myself who were cosponsors of S. 200.

7 It seems to me that this legislation is directed at a
8 real problem and that is the problem of communities that are
9 still in the last recession, and when we cut off
10 countercyclical and targeted last September, these communities
11 were excessively hurt.

12 These are communities with shrinking tax bases, high
13 unemployment, with populations very old and very young in
14 large numbers. It places a real burden on the local community
15 budgets that do not have the revenues that can be raised from
16 a local tax base.

17 What this legislation does is try to prevent job
18 lay-offs, higher taxes and reduced services which is what has
19 happened to many of these communities that have experienced a
20 cut-off in fiscal assistance last year.

21 When you get into the old cycle of reducing police and
22 fire and then having citizens leave the city and having the
23 tax base reduced more and more, what we find in these
24 communities is that things get worse faster and better slower.

25 I think particularly as we approach the possibility of a

1 recession that the targeted fiscal assistance is particularly
2 needed for these 2,100 communities in the country and the
3 countercyclical is needed for all the communities that will be
4 affected adversely as we move into a recession.

5 Senator Packwood: How much is this over the concurrent
6 budget resolution?

7 Senator Bradley: Well, the concurrent Budget Resolution
8 is for Function 850 and in the in the Function, there are not
9 specifications for particular programs; there are comments,
10 but not specifications, and I think that as we approach the
11 Second Concurrent Budget Resolution, this is a particular
12 example where changed circumstances deserve the application of
13 a waiver to the Budget Resolution.

14 Senator Packwood: There is no likely way that we can fit
15 it within the \$8.1 billion for the 850 Function? It is going
16 to have to go above it.

17 Senator Bradley: It would have to go above it, or we
18 could remove other parts in that budget. You can shift
19 around the Function 850 in any way you like. Is that not
20 correct, Mr. Morris?

21 Mr. Morris: That is correct, Senator, but for fiscal
22 year 1979, the conferees did agree to \$150 million for
23 targeted fiscal assistance. The Senate conferees indicated
24 that it was part and parcel of a total agreement for '79 and
25 '80, but there are funds in the fiscal year 1979 for the \$150

1 million of targeted fiscal assistance.

2 For fiscal '80, there is an assumption that that
3 category, number 850, for state and local fiscal assistance
4 would be reduced by actually \$400 million.

5 Senator Packwood: Say that again?

6 Mr. Morris: There was an assumption on the part of the
7 House that the category would be reduced by \$400 million to
8 \$8.1 billion. The Senate conferees indicated that they did
9 not assume -- that they were making no assumption that that
10 category would be reduced.

11 Senator Packwood: The House cut-out, as I recall most
12 revenue sharing, they had a \$6.5 billion figure for this
13 function; the Senate had \$8.5 billion.

14 Mr. Morris: That is correct. The House assumed that
15 revenue sharing for the states --

16 Senator Packwood: We ended up with \$8.1 billion. If we
17 adopt this, considering the general revenue sharing is \$6.9
18 billion, I do not see where we are going to fit it into \$8.1
19 billion. I do not know what else we are going to cut out of
20 that function that we have not already cut out.

21 You are simply saying that is probably right. Let's go
22 with the waiver and ask for \$400 million more dollars.

23 Mr. Morris: That is correct.

24 Senator Long: Does this not have something to do with
25 the item about revenue sharing, as stated, the general revenue

1 sharing at the state level? Did not the House people, or
2 someone, suggest over there that they could cover the cost of
3 this thing by squeezing it out of the part of the revenue
4 sharing that the states would otherwise receive at the state
5 legislature level?

6 Mr. Morris: That is correct. The House did assume that
7 there would be a reduction in the state share of general
8 revenue sharing. However, the House is acted through its
9 Appropriations Committee and provided full funding for general
10 revenue sharing through the Appropriations process for fiscal
11 '80.

12 Senator Long: The House is on both sides of the issue,
13 full funding for general revenue sharing and also working on
14 the assumption that this would come out of the general revenue
15 sharing. Is that correct?

16 Mr. Morris: That is correct, for fiscal 1980.

17 Senator Talmadge: What would the money be used for?

18 Mr. Morris: The funds that would be distributed to state
19 and local governments, or local governments?

20 Senator Talmadge: Yes.

21 Mr. Morris: All funds must be spent very quickly for
22 such things as employment of additional personnel. It cannot
23 be used for long-term capital expenditure.

24 Senator Talmadge: Cannot be?

25 Mr. Morris: Cannot be used for that.

1 Senator Talmadge: In other words, employment of
2 personnel, it is limited to that?

3 Mr. Morris: Not necessarily just employment and
4 personnel, but for short-term items such as necessary things,
5 stationery, and other things that is a service-related
6 expenditure that a state or local government would provide.

7 Senator Bradley: I might add to that, Senator Talmadge,
8 that there are a number of communities with laid-off police
9 and fire when this was cut off last September 30th.

10 Obviously they would re-employ policemen and firemen.

11 Senator Talmadge: Would they have to hire unemployed
12 personnel, or anybody they wanted?

13 Senator Bradley: I do not think there is a specific
14 requirement.

15 Mr. Morris: No particular requirement as to who can be
16 hired. In fact, the money can be used to keep people on the
17 payroll that they might otherwise have to lay off.

18 Senator Dole: Is there any limit on how much you spend
19 under the program?

20 Mr. Morris: Yes. For fiscal year 1979 it would be
21 limited to \$150 million. For fiscal year 1980, under the
22 targeted fiscal assistance program, it would be limited to
23 \$340 million. If the countercyclical program were to come
24 into effect because of high rates of unemployment then
25 additional funds would be spent, but there is an overall cap.

1 No more than \$1 billion could be distributed under the
2 countercyclical program.

3 Senator Bradley: Under the countercyclical, it is \$125
4 million a quarter; \$30 million for each one-tenth of a percent
5 over 6.5.

6 Senator Dole: \$800 million.

7 Senator Bradley: If we got a high unemployment rate
8 rapidly

9 Mr. Morris: If you went to a rate of 7.3 percent for the
10 first quarter of 1980, it could increase the expenditures to a
11 little below \$800 million.

12 Senator Dole: There is a lid on how much you could
13 spend.

14 Mr. Morris: A \$1 million cap in the authorization, and I
15 might add that any funds that are authorized under this
16 program have to be appropriated by the Appropriations
17 Committees.

18 Senator Dole: We had the same argument yesterday in Food
19 Stamps, whether or not we would have a cap on it.

20 The Chairman: Let me just get this straight in my mind.
21 Is this the same program that we sent to the House to
22 representatives in the previous Congress to have it die over
23 there, because the House committee, under the able leadership
24 of its chairman, just would not let that matter come to a
25 vote?

1 Mr. Morris: That is correct.

2 The Chairman: As far as I am concerned, if we want to do
3 business on this thing, we ought to get it over there as soon
4 as we can because the sooner it gets over there, the more hope
5 there is that those who favor the program -- unless someone
6 can pry it loose from that committee and get a vote in the
7 House on it.

8 So I would hope that we would resolve this thing as soon
9 as we can.

10 Senator Dole: Mr. Chairman, I think we should go ahead
11 and pass it. I do not have any objection, except I know
12 Senators Durenberger and Danforth have a direct interest and
13 so does Senator Moynihan. I am not certain that they would
14 want to be present, but if we are adopting a compromise they
15 worked out, they would not have any objection if they passed
16 it.

17 Senator Bradley: I do not think they would have any
18 objection if they passed it. This has been something that has
19 been worked out over a number of months.

20 The Chairman: I have never objected; I do not know
21 anyone around here who has ever objected to someone agreeing
22 to his bill even though he may be absent. I do not know of
23 anybody who really resents us putting our stamp of approval on
24 his handiwork in his absence.

25 All in favor of reporting out the measure described here

1 as an alternate for committee consideration, say aye.

2 (A chorus of ayes)

3 The Chairman: Opposed, no?

4 (No response)

5 The Chairman: The ayes have it.

6 Now, let me ask you, could we report this out as a
7 separate bill, or does this have to take a House number?

8 Mr. Stern: I do not think you have ever had a question
9 about where it was an S-numbered bill. The first
10 countercyclical revenue sharing, however, was split as an
11 amendment on a public works bill and was not returned to the
12 Senate on the grounds that it was unconstitutional.

13 I believe you could.

14 Senator Bradley: What?

15 Mr. STern: The first time countercyclical revenue
16 sharing was approved it was actually a Senate amendment to a
17 non-revenue bill in the House. I believe that it could
18 originate in the Senate.

19 The Chairman: Without objection.

20 Mr. Stern: Since it is an authorization bill affecting
21 1979 and 1978 and it is passed May 15th, you will have to
22 request a budget waiver; report out a resolution waiving the
23 point of order that would otherwise be raised. I would
24 suggest that you approve that, too.

25 The Chairman: When we report this out, this will have to

1 go over there. Would this be regarded as just an
2 authorization?

3 Mr. Stern: Authorized as appropriations.

4 The Chairman: Authorizations.

5 That being the case, it can go if there is an S-numbered
6 bill.

7 Mr. Stern: Yes, sir.

8 The Chairman: All right.

9 Senator Moynihan is not here. I did a lot to try to get
10 an additional Senator from this committee on the Budget
11 Committee to help with problems like this, so I would suggest
12 that Senator Packwood and Senator Dole -- are you still on the
13 committee, Senator Dole?

14 Senator Dole: No.

15 The Chairman: Then Senator Packwood and Senator Moynihan
16 do what they can on the Budget Committee to see to it --
17 Senator Packwood, I hope you and Senator Moynihan will do what
18 you can in the Budget Committee.

19 Senator Packwood: Mr. Chairman, I did not vote on this.
20 I am not very enthusiastic about the bill generally, but given
21 that negative, I will do what I can on the Budget Committee.

22 The Chairman: Senator Moynihan is very enthusiastic.

23 Senator Bradley: He would balance you, Senator Packwood.

24 The Chairman: With his enthusiasm, if you average it
25 out, I think you will have adequate enthusiasm between the two

1 of you to push this bill.

2 Mr. Stern: Mr. Chairman, can we say that the bill was
3 ordered favorably reported, S. 200, the Moynihan bill, as
4 modified, as agreed to today, and also has reported out a
5 resolution seeking a waiver of the budget requirement.

6 Senator Bradley: If we report out the S. 200, we still
7 retain the flexibility to move it as a separate bill, or as an
8 amendment. Is that correct?

9 Mr. Stern: You will have it reported as a separate bill,
10 if you decide it is important to use it as an amendment
11 instead, you will have the text ready.

12 Senator Bradley: All right.

13 The Chairman: All right.

14 Without objection, then, we will so report.

15 Mr. Stern: Mr. Chairman, we will word the waiver
16 resolution in such a way as not to limit it specifically to
17 that one bill but rather, to the subject as contained in the
18 bill, so it would apply equally to an amendment.

19 Senator Bradley: I think that would be better.

20 The Chairman: All right. Without objection, so agreed.
21 Now, let us turn --

22 Senator Dole: Did we take number one, the nomination?

23 Mr. Stern: The nomination was withdrawn, Senator Dole.

24 Senator Dole: There is no nomination?

25 Mr. Stern: Yes, sir.

1 The Chairman: Let us see if we can come together on the
2 Second Concurrent Budget Resolution, Staff Document C.

3 You have a memo prepared by the staff and maybe Mr. Stern
4 can suggest to us how we might try to work with the Budget
5 Committee and do our part of this budget function?

6 Mr. STern: Mr. Chairman, every year, the Committee makes
7 its recommendations to the Budget Committee for the First
8 Budget Resolution and submits a report by March 15th of the
9 year, but by the time of the Second Budget Resolution, it is
10 usually -- or in the past it has been -- pretty much a cut and
11 dried affair, what legislation is likely to pass affecting the
12 current year.

13 So it has not involved just the Finance Committee
14 recommendation process.

15 What is different this year, you have a major revenue
16 bill that you are beginning action on and if the Budget
17 Committee simply thinks up a number without Finance Committee
18 advice, that number is going to be a binding number in the
19 Second Budget Resolution.

20 So in view of that, the Budget Committee Chairman and
21 Ranking Minority Member sent a letter to the Finance Committee
22 asking for Finance Committee advice on what amounts should be
23 included for revenues and expenditures in the Budget
24 Resolution.

25 If you look at the table, which is on page 3 of

1 Attachment C, you will see that the Finance Committee had
2 originally recommended that in net, an allowance be made for
3 revenue cuts. The First Budget Resolution, in fact, wound up
4 at zero, assuming that any tax cuts would be offset by tax
5 increases for a net of zero.

6 However, the President's budget, the new review of the
7 President's budget, assumes that there will actually be \$3.8
8 billion of tax increases that will affect fiscal year 1980 and
9 the major item in there is the crude oil tax and the second
10 large item is the foreign tax credit.

11 The House has already passed a bill that added up to \$2.5
12 billion of that. The Finance Committee has not acted yet and
13 the large bill, the crude oil tax bill or the foreign tax
14 credit.

15 It is really a question of where you want to come out on
16 revenues, and the staff suggestion here is you may want to
17 assume that any amount that you raise in the Crude Oil tax,
18 you are going to use in energy-related tax reductions or
19 assistance to the poor, things of that sort.

20 The Chairman: Let me ask Mr. Shapiro if he would come up
21 here and help us with this.

22 Mr. Shapiro, could you tell me what are the areas in
23 which we will be asked to provide tax credits or tax
24 expenditures or whatever to use the money and that would come
25 in in fiscal 1980 in energy-related matters.

1 What are the kinds of things that the administration has
2 asked us to consider and what are the figures if you have
3 them, off the top of your head, and the kind of items that
4 this committee might want to be considering itself in that
5 area?

6 Mr. Shapiro: The administration, as you know, has
7 requested a trust fund in order to put the gross revenues of
8 the windfall profits tax. They are also asking you to put in
9 there the additional income as a result of the corporate
10 individual income taxes, as a result of the increased prices.

11 From those revenues that are going into the trust fund,
12 they intend to have money set aside, money to be used for
13 income assistance to the poor for mass transit; moneys to put
14 in for alternative sources of fuel.

15 The major item of that is to have \$88 billion over a
16 period of time to an energy security organization. The first
17 year, of course, they start off with a small amount of money
18 but they do want to use money for low-income assistance.

19 I am assuming the committee will also review credits as a
20 means to provide incentives for conservation and production
21 and that the assumptions that we had was what the
22 administration has requested is that the money that is raised
23 from the tax is to be used for energy and for low income
24 assistance and mass transit.

25 So there is not intended to be an increase in revenues to

1 the government, but a net effect, meaning that the money that
2 is raised is to be used back into the economy for purposes of
3 energy as well as low-income assistance.

4 The Chairman: Now, in other words, if you take the low
5 income assistance, which the administration will be
6 recommending; mass transit. Is the administration itself
7 recommending credits?

8 Mr. Shapiro: Yes. They have a series of credits --
9 woodburning stoves, solar, and several credits; the oil shale
10 tax credit; a tax credit for unconventional gas. They have a
11 series of credit that they are proposing. Not all of these
12 would have revenue consequences in 1980 because they may not
13 come onstream, but that is a part of the overall program, but
14 some of the credits clearly would have an effect in fiscal
15 year 1980.

16 The Chairman: In addition to that, I would assume that
17 this committee will want to consider some tax credits to spur
18 insulation of homes. We have voted that type of thing before.
19 I assume we will want to do some of that.

20 Let us see. We voted about how much in the way of tax
21 credits to try to stimulate production and conservation did we
22 vote the last time that we had a figure in the bill?

23 Mr. Shapiro: If my recollection is correct, in the bill
24 in the last Congress you have in the neighborhood of \$5.5
25 billion worth of tax credits that you sent in your bill to

1 conference, so there is a strong --

2 The Chairman: Most of it did not become law because we
3 did not have the revenue to pay for it. Is that not right?

4 Mr. Shapiro: That is correct. In many cases, it ws
5 because you did not have the revenues.

6 In addition to that, you reduced the years where the
7 original bills -- in 1985 and 1986 you cut off the
8 availability of the credits; in 1982, both individual and
9 business credits.

10 I am assuming there will be some interest in the
11 committee to increase the number of years whereas in many
12 years, businesses have a problem in looking ahead and seeing
13 that the cut-off date is 1982.

14 It would be a problem from the point of view of
15 increasing the availability of the credits so they could make
16 plans in the future. In addition, some of the committee
17 members may be interested in some of the conservation credits
18 in order to make those available for a little longer period,
19 as a means to take some of the pressure off the market from
20 hand the production and the supply and demand,* be able to
21 make it available to a greater extent.

22 The Chairman: Well, the thought occurs to me that with,
23 let us say, the President's budget was \$.38 billion for fiscal
24 '80. So far, the House has passed \$.26 billion.

25 They might pass this foreign tax credit proposal and

1 raise another \$3.8 billion. That would be \$3.2 billion.

2 What are these other items in here? It is the tax exempt
3 bonds and the Railroad Retirement that would fill in the rest.

4 Is that where it would come from, to get from the \$2.5
5 billion up to the \$3.8 billion?

6 Mr. Shapiro: That is correct. As I understand the sheet
7 that was prepared, that all adds up to a net change of plus
8 \$3.8 billion.

9 As you know, several items on this list have not had
10 consideration and the Finance Committee has not passed the
11 house mortgage bonds tentatively approved by the Ways and
12 Means Committee.

13 The foreign tax credit is not even begun, or the other
14 energy credits begun, on the Ways and Means Committee.

15 The Chairman: You cannot count on the foreign tax credit
16 at all, can you?

17 Mr. Shapiro: I think -- I do not anticipate that the
18 Congress would pick up \$800 million in the foreign tax credit.
19 That is even more than, I think, that the administration
20 proposal picks up.

21 If my recollection is correct, the proposal that they had
22 made to the Congress picks up, approximately \$600 million,
23 \$300 million of that is because of the retroactive feature
24 that is in the proposal. That has raised some concern.

25 They have held hearings in the House, but they have not

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1 begun a mark-up session in the Ways and Means Committee and,
2 based on the discussions that I have had with a number of the
3 House members on the Ways and Means Committee, I think it is
4 unlikely that it would pick up the \$600 million they propose.

5 The Chairman: My impression is that thus far in our
6 committee we have had testimony, and very compelling
7 testimony, against such foreign tax credits. We have not
8 heard the administration's case for it.

9 I am sure that is expected to come on later on.

10 Based on what we have heard so far, I do not see how we
11 assume that tax credit is going to pass. It might and it
12 might not. It is like a lot of other things.

13 Mr. Shapiro: The major controversial issue before the
14 committee will be the regulations. They have caused a great
15 deal of concern. You will probably consider not only the
16 legislative recommendations but, in addition, the regulatory
17 changes they have made to take the foreign tax credit away,
18 essentially, from the oil companies, that the oil companies in
19 foreign countries will not be allowed to have foreign tax
20 credit payments to the foreign countries but be treated, in
21 effect, as royalties.

22 That has become a very controversial issue since the
23 regulations were promulgated, which was this past month.

24 The Chairman: Well, I am open for suggestions. My
25 reaction would be that we should tell them that in so far as

1 we can raise money in this area we think that it would be tax
2 cuts, tax expenditures, tax credits, low income things, a
3 considerable portion of which the administration is
4 recommending and other things like it, which the Congress has
5 voted on before. We think that we will use it up.

6 How does that strike the committee?

7 Senator Dole: There are also possible tax credits for
8 increased energy costs that Senator Bradley and Ribicoff and
9 myself and others have submitted that would make more sense
10 with what we will raise, we will spent.

11 The Chairman: My thought is that it would be a matter of
12 great restraint on the part of this committee if it does not
13 have ideas of ways you could use the money that would exceed
14 what this would raise in the first year. Later on, it would
15 raise a lot more money, but in the first year, my reaction is
16 that we had better not count on doing much more with this.

17 I would be inclined to think that the committee will
18 probably recommend tax credits, tax cuts.

19 Senator Dole: Social Security?

20 The Chairman: That is right. We have a very appealing
21 suggestion among our people that we ought to roll back the
22 Social Security tax. That is more money that we will not have
23 any hope of taking in the future.

24 I think about the safest thing would be to just tell them
25 do not count on any net gain.

1 Hopefully in the energy area, we will be recommending
 2 enough tax credits, tax cuts, much of which the administration
 3 itself is already recommending that we expect to recommend a
 4 bill that would use up the revenue that we propose to raise in
 5 the first year.

6 Thereafter, there may be some, but we can worry about
 7 that when the time comes.

8 Yes, sir, Senator Wallop?

9 Senator Wallop: Mr. Chairman, am I to understand that
 10 with regard to the foreign tax credit controversy that the
 11 only route available to us is legislation countering a
 12 regulation. Otherwise, they will begin to collect it.

13 Mr. Shapiro: That is correct. There is a question as to
 14 what is the applicable law as to foreign tax credits regarding
 15 oil companies. Today, the Treasury Department carries out
 16 what they feel is the intent that denies the foreign tax
 17 credit to the oil companies.

18 I think they have been discussing and I think they will
 19 testify before the committee that they would like those
 20 regulations overturned to allow them to have at least a 46
 21 percent tax credit.

22 The problem, of course, is a very difficult one, because
 23 they actually pay somewhere between 80 and 90 percent, in many
 24 cases an average of 90 percent, that are just taxes. The
 25 Internal Revenue Service has taken the position that that, in

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1 effect, is royalties and therefore not a credible tax.

2 Senator Wallop: It is interesting to me that somehow or
3 other when you have a state-owned product, not a company-owned
4 product that it is receiving a royalty.

5 Basically, what we are faced with is ome kind of
6 legislation to counter that.

7 Mr. Shapiro: Two things. One, that the committee could
8 take a legislative route to counter the regulations; second,
9 that the admnistration proposed legislative recommendations to
10 tighten the foreign tax credit in the other areas and that is
11 before you as well.

12 Senator Wallop: Thank you, Mr. Chairman.

13 The Chairman: Is there any further discussion? Senator
14 Moynihan?

15 Senator Moynihan: Senator Packwood and I, as you know,
16 are the members of the Finance Committee who serve on Budget.
17 I just wanted to make sure that we have our instructions clear
18 here. I do think we are in some sense instructed delegates.

19 Senator Dole: Designated hitters.

20 Senator Moynihan: Is it the committee's judgment that we
21 should put forward that there would be no net increase in
22 revenues attendant on our adoption of a windfall profits tax?

23 The Chairman: What we are talking about here is to
24 report to the Budget Committee that we do not believe that
25 there is going to be any net gain in revenue because we think

1 that we are going to recommend to the Senate that in tax
2 credits and tax cuts that this \$2.5 billion that the House has
3 in its bill would be used at least that that much would be
4 used in the energy area to stimulate production and
5 conservation.

6 That includes mass transit. May I say, Senator, that
7 that is one of the recommendations.

8 Senator Moynihan: Does my distinguished senior colleague
9 understand this in the same way?

10 Mr. Packwood: I understand what the Chairman is saying.
11 You were not not here earlier when we talked about the revenue
12 sharing provisions which I have misgivings about generally.
13 That is unrelated to what we are talking about now, with which
14 I do agree.

15 Senator Moynihan: So we are instructed. Fine.

16 The Chairman: If you want to discuss it further, we can.
17 Suppose you just list out, Mr. Shapiro, the different items
18 that this committee is going to want to think about in the
19 energy area.

20 Mr. Shapiro: You are talking about the possible credits
21 and items?

22 The Chairman: Start off with the things that the
23 administration is recommending first and then take the ones
24 that the committee is going to want to consider.

25 Mr. Shapiro: Of the use of the funds, the \$142 billion

1 that the administration hopes to raise between 1980 and 1990,
2 they have broken that down into these categories.
3 Energy Security Corporation, they plan to devote \$88
4 billion to that.

5 Senator Packwood: How much?

6 Mr. Shapiro: \$88 billion.

7 Senator Chafee: Over how many years?

8 Mr. Shapiro: Ten years; 1980 to 1990.

9 Senator Moynihan: Net after the loss in income taxes?

10 Mr. Shapiro: Yes.

11 Senator Moynihan: 142?

12 Mr. Shapiro: This is actually the gross that goes into
13 the trust fund. We are talking about the gross amount of
14 windfall profit taxes. \$88 billion goes to the Energy

15 Security Corporation.

16 The oil shale tax credit, they have allocated \$1 billion.
17 Unconventional gas tax credits, they have allocated \$1

18 billion.

19 Utility oil use, \$5 billion.

20 They would like to cut the use of oil by utilities in
21 half through a form of a rationing system.

22 Residential and commercial conservation, \$2 billion.

23 Transportation efficiency -- that includes mass transit,
24 and so forth -- that would be \$16.5 billion.

25 Low income assistance would be \$24 billion.

1 The establishment of a solar bank and tax credits would
2 be \$3.5 billion.

3 Various other programs would include \$1.2 billion, and
4 that totals up to \$142 billion that the administration has
5 designated the use of the gross windfall profits tax proceeds.

6 The Chairman. Now, would you mention some of the
7 things that this Committee might want to look at in addition
8 to what the administration is recommending to us.

9 Mr. Shapiro: As far as spending programs, a number of
10 members of the committee seemed interested in credits for
11 conservation, increased availability of some of the credits
12 from nonconventional, the geopressurized methane, oil shale,
13 solar, and do different aspects, other than what the
14 administration proposed.

15 There are also problems as far as the revenues, the
16 various production incentives, meaning that the
17 administration, as you know, has a percentage tax on all the
18 so-called windfall profits.

19 A number of members of the Finance Committee have
20 indicated a concern in the committee sessions and the hearings
21 with the witnesses about the production centers that they feel
22 should not go into the trust fund and should not be a part of
23 the tax.

24 For example, members feel that a major source of
25 increased oil would be from newly discovered oil and if you

1 have a very heavy tax on that, it may provide a disincentive
2 for newly discovered oil rather than an incentive. Therefore,
3 they are concerned about alleviating the tax burden on
4 newly-discovered oil.

5 You had the same concern for incremental tertiary where
6 there is a feeling that may be a major source of production in
7 the years in the future.

8 There are also concerns about Alaskan oil, the tax that
9 was put on in the House bill which is significant. Also,
10 stripper oil. And then there is the concern about the
11 independent producers possibly providing the so-called
12 independent producer exemption from the tax. Also the concern
13 about the rate of tax. 60 percent may be too high for some of
14 the categories, and possibly that should be reduced. The
15 administration proposed a 50 percent rate.

16 I just mention those areas where some members have
17 indicated an interest in reducing some of the provisions in
18 the House bill, or the administration proposal, in an effort
19 to provide incentives for increased production.

20 It is clear that if all of those items were agreed to by
21 the committee, there would be very little left in the trust
22 fund and therefore, the committee would have to establish
23 priorities as to which of these areas would appear to be the
24 highest area of priority for increased production. Then the
25 committee would have to make a determination as to the amount

1 of money it would like to raise by tax for it to be used for
2 any of the purposes it would like to use it for -- low income
3 assistance, mass transit, or other credits, and you would have
4 to design your tax program accordingly.

5 I would think taking into account, you would also have to
6 consider that we would have increased revenues, not only as a
7 result of a windfall profits tax, but also as a result of
8 increased revenues because of the higher prices.

9 What the House did in its decision -- and this committee
10 may want to go along with that -- if you decide to have a
11 trust fund, to use that trust fund for items that typically
12 come out of the trust fund, setting aside from mass transit,
13 maybe alternative fuels, corporations or special credit that
14 you may have, synthetic fuels and so forth.

15 What the House decided to do was not to put general
16 revenues in a trust fund and increased revenues because of the
17 higher price are not in the trust fund in the House bill, but
18 rather continue to general revenues.

19 What the House would do is save money for the poor, low
20 income assistance programs, as well as the energy projects
21 from general revenues, to keep general revenues separate from
22 the trust fund.

23 The Chairman: Now this House bill also contains -- you
24 mentioned, but among other things, this House bill contains a
25 big item for revenue from that Alaskan oil.

1 How much is that in the House bill?

2 Mr. Shapiro: Jim has the actual figures. The Alaskan
3 oil is a significant revenue item.

4 The Chairman: On the Alaskan oil, the administration did
5 not ask for --

6 Mr. Shapiro: The Alaskan oil is \$17 billion if you agree
7 with the administration proposal, rather than the House
8 proposal, not to exempt Alaskan oil, but to tax it in the
9 second tier.

10 The Chairman: What would be the difference in the first
11 tier?

12 Mr. Shapiro: The gross would be a billion dollars.

13 The Chairman: Is there a difference between the House
14 recommendation and the administration bill?

15 Mr. Shapiro: The net is \$77 billion. It is confusing to
16 talk about between the gross and net. They put the gross
17 revenues in the trust fund. Everyone is talking gross
18 revenues. It would look like this committee would cut
19 revenues, but we are just changing terminology.

20 The Chairman: We had better talk in the same terms they
21 are talking about.

22 Mr. Shapiro: That is right. For the committee, we would
23 have to call it gross revenues, but the Budget Committee talks
24 net. So when we talk about decisions, we will talk gross
25 revenues, but in your discussion of the figures for the Budget

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1 Committee, we should convert those to net figures.

2 The Chairman: In terms of net, how much money is there
3 between what the House did on Alaska and what the
4 administration recommended?

5 Mr. Shapiro: The Budget Committee would be \$577
6 million.

7 Senator Bradley: In the first year?

8 Mr. Shapiro: First calendar year.

9 Senator Heinz: Calendar what?

10 Mr. Shapiro: The first calendar year in the change of
11 the Alaskan provision between what the Administration proposed
12 and what the House bill included.

13 Senator Heinz: Would that be true for calendar year
14 1980?

15 Mr. Shapiro: Yes.

16 The Chairman: There is \$577 million that the
17 administration did not recommend. My understanding is that
18 the administration did not favor it -- are they supposed to be
19 favoring it now?

20 Mr. Shapiro: They are now favoring the reduction of \$577
21 million. They do not agree with the House bill.

22 The Chairman: They do not agree with the House. They
23 think it is irresponsible and have considered it and they
24 think it would be counterproductive.

25 There is \$577 million that they think should come out

1 now. That gives you a figure, the \$2.5 billion down to \$1.95
2 billion right there.

3 Then if you assume any of these suggestions that are
4 being made by the committee members such as to exempt new oil,
5 Senator Nelson said there, how can it be a windfall when you
6 have not even discovered something yet?

7 So if you take that one, that would be a big reduction in
8 the amount of money.

9 There are Senators who favor exempting stripper wells.
10 That involves a lot of money.

11 There are Senators who favor adjusting the small
12 independents. That would take a lot of money.

13 When you really get down to it, until we know what the
14 committee position is going to be on all of that, you cannot
15 say you are going to make any revenue gain in this area, in
16 view of the fact that you have a lot of administration
17 recommendations themselves that would reduce the thing, in
18 addition to what the Senators themselves might want to
19 suggest.

20 So I think the only thing you can do is just say that we
21 would assume that we are going to recommend tax cuts to the
22 extent that we can raise it in the energy area, to the extent
23 that we raise additional funds.

24 That does not foreclose someone from offering the
25 Roth-Kemp amendment. Nor does that foreclose someone from

1 offering an amendment to postpone the Social Security tax
2 increase come January.

3 Thinking of all the different things, I would say as of
4 now, it would be a big mistake for anyone to recommend that
5 you are going to start financing other programs with the
6 leftover on this tax.

7 The safe thing to do is to assume hopefully that we will
8 raise enough money with this tax to pay for all the different
9 things including the energy security that the President is
10 recommending and the committee might want to consider. If
11 there is any objection I would be glad to hear it.

12 Senator Dole: I am just going to ask -- we are still
13 talking about what we are telling the Budget Committee.

14 The Chairman: That is we are talking about.

15 Senator Dole: Maybe we should not get into what it will
16 cost if we do exempt strippers and new oil and incremental
17 tertiary and marginal lower tier and Alaskan. You may not
18 wind up with any money at all.

19 Mr. Shapiro: What Senator Long is suggesting, you do not
20 assume you would pick up any revenue -- not for any specific
21 reason, but that is in their program. What you raise, the
22 committee intends to use for energy or for the poor.

23 Senator Dole: I agree with that. I think we will be
24 lucky if we restrain ourselves that much.

25 Senator Bradley: Mr. Chairman, would it be possible for

1 the staff to prepare the revenue effects of exempting specific
2 kinds of oil? Also, the revenue effects with differing price
3 increases for OPEC so that we could have a mini-budget here to
4 see what revenues we have and what we might spend them on and
5 what it would cost.

6 The Chairman: For these purposes, we are talking about
7 the Joint Committee staff. The Joint Committee staff has a
8 lot more information and has been working on this thing
9 longer.

10 Senator Wallop: Mr. Chairman, if I may suggest, if they
11 do that, I think that is a good idea. But I think that the
12 other question you want to ask, on the other side, is what the
13 supply response is, so you have a judgment that is not just
14 financial but a total energy picture, which, after all, is
15 what we want to try to work with.

16 Senator Bradley: I have no objections to that.

17 The Chairman: Without objection, then, we will recommend
18 that the Budget Committee regard this energy matter as a wash,
19 that the tax is being raised for energy-related purposes and
20 we think that they ought to anticipate that that is going to
21 be used for energy-related purposes.

22 If not, there will probably be someone who will have some
23 tax suggestion in some other area that would be there anyway.

24 Senator Roth: On that point, as you know, I have
25 suggested if we have revenue, we ought to consider using that

1 for a Social Security rollback. One of the things that I
2 think would be helpful for our deliberations when we start
3 what we do with this revenue, would be to have the Committee
4 staff begin studying the cost of a rollback --

5 May I have the attention of the Committee for just a
6 minute?

7 I was suggesting that, as I proposed earlier, that we may
8 want to use revenues for a Social Security rollback, and I
9 think it would be very helpful when we begin to mark up the
10 legislation if we had some basic figures and data in this
11 area. I suggested, for example, that we roll back for two
12 years the '81-'82 increase, both with respect to the basic
13 rate and the sum it is applied to.

14 A second suggestion that has been made that there ought
15 to be some kind of a cost of living increase with respect to
16 the salary it is assessed against, that that would make t a
17 lot less expensive.

18 So I would hope that when we begin the actual mark-up we
19 might have some basic figures. I do have some figures from
20 CBO.

21 Mr. Stern: Here is some information on that, provided by
22 the actuaries in Social Security, just so that you have an
23 idea of the amounts that you are talking about.

24 The Social Security tax rate does not go up in January
25 1980, but in January 1981, and that is an increase of \$12.6

1 billion in January 1981.

2 The amount of wages subject to tax do go up, and so for
3 the relatively smaller number of people who are affected by
4 that, the amount would go up by \$1 billion in 1980 and another
5 \$2.9 billion in 1981.

6 So the largest increase is that related to the tax rate
7 increase in January 1981 and a rather smaller increase related
8 to the level of taxable wages going up.

9 Senator Roth: That was by calendar year?

10 Mr. Stern: That was by calendar year, yes, sir.

11 Senator Roth: I think one of the things that we need to
12 consider, too, if you look at the CBO predictions as to what
13 is going to happen with unemployment --

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1 Mr. Stern: These are based on the administration's
2 midyear review assumptions that are probably a little bit on
3 the optimistic end of the range.

4 Senator Roth: I guess what I would like to do, Mr.
5 Chairman, with your approval, is to work with our staff people
6 in getting some basic figures with respect to a rollback of
7 the Social Security tax so that we would have that available.

8 Thank you, Mr. Chairman.

9 The Chairman: Of course, I would like to roll back the
10 Social Security tax increase. The thought occurs to me that
11 if we do that, that is going to take money that you count on
12 putting in the Energy Security Fund. Is that not right, Mr.
13 Shapiro?

14 If you are going to roll back the Social Security tax,
15 not for this January, but the January a year from now, that is
16 \$12 billion.

17 Mr. Shapiro: That is the big increase.

18 The Chairman: If you are going to roll that back, that
19 is going to consume most of the money that you hope to put in
20 the Energy Security Corporation, would it not?

21 Mr. Shapiro: That would be almost -- maybe a little bit
22 more than the money raised in that particular year.

23 The Chairman: I find a lot of appeal to this suggestion,
24 and maybe we want to do it. The point is that if we do it,
25 that means that we cannot do the item that the President has

1 marked as a big item in that program. We will have to think
2 about it.

3 I am glad the Senators mentioned it. I would like to
4 roll back that tax, but also I know that we are going to have
5 to think about, if we do that and use this money for that,
6 that is going to mean that the big item in the President's
7 program in terms of dollars will have to be handled in some
8 other way.

9 I am not saying it cannot be done. I know that it can.
10 But that will be the big item that will go on the boards if we
11 do business that way.

12 Senator Bradley: This is similar to suggestions made in
13 previous years in taking the old crude oil equalization tax
14 and using it to offset Social Security increases. Would you
15 say that your idea is similar to that?

16 Senator Roth: I am the one who proposed that two years
17 ago when we were talking about a severance tax. That is
18 correct.

19 Senator Bradley: I see.

20 Senator Roth: We had a vote, I might say, in the Finance
21 Committee and on the Senate Floor at my instigation on the
22 proposal. I am just suggesting that this is a very serious
23 question that does have a direct impact on unemployment and
24 inflation and is something that we should look at.

25 I feel very strongly, Mr. Chairman, that we cannot really

1 divorce energy with the state of the economy, and I think,
2 according to reports I hear -- I do not know whether they are
3 accurate or not -- basically this mark-up is going to come up
4 some time after the recess.

5 Is that correct, Mr. Chairman?

6 The Chairman: That is one of the items that we will
7 discuss and we will see when we get to this matter -- we will
8 see just how fast the committee can move with this bill.

9 Mr. Stern: Mr. Chairman, in any case, the large increase
10 in tax rates occurs in fiscal year '81. As far as the
11 recommendation of the Budget Committee is concerned, we are
12 talking about fiscal year 1980.

13 That really leaves you flexible on what you are going to
14 do vis-a-vis fiscal year 1981.

15 The Chairman: The Senator's point could still be applied
16 in 1980. It would not cost a billion dollars to postpone the
17 Social Security tax increase come January, but in terms of
18 what you hope to raise with this tax, that is a major portion
19 of it the first year, a billion dollars. It would be a big
20 part of what you hope to raise.

21 If you start out by following the administration's own
22 recommendation on Alaska, that would cut the House bill from
23 \$2.5 billion to \$1.9 billion. Then if you just used the
24 Social Security item ---how much is it the first year, Social
25 Security?

1 Mr. Stern: The first calendar year, \$1 billion.
2 Actually, on a fiscal year basis, most of that occurs in the
3 last quarter of the calendar year, so I imagine the fiscal
4 year costs would be very small.

5 The thing you are going to have to consider when you take
6 it up is that the Social Security cash flow is not very
7 healthy as projected over the next five years and with
8 relatively more pessimistic assumptions such as the CBO makes,
9 they think that the trust fund by the end of five years will
10 only have about a month and a half's worth of benefits in it,
11 and that is a serious problem that you will have to consider.

12 Senator Roth: I will have to point out that if the
13 predictions of CBO on unemployment are realized -- and God
14 forbid; they estimate it could go as high as 8 percent.

15 The more unemployment, the less stable are your revenues
16 for Social Security.

17 All I am trying to suggest at this time, because I
18 believe very strongly that whenever we do have the mark-up we
19 cannot consider the energy proposal in a vacuum.

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1 The unemployment rates are something we are going to have
2 to give some very careful consideration to.

3 For that reason, Mr. Chairman, I am proposing that we
4 have some basic information on very different approaches, some
5 less expensive than others, be available for this committee to
6 consider at that time.

7 Mr. Stern: Mr. Chairman, the other part of the report to
8 the Budget Committee concerns expenditures. If you look at
9 that document again, at the bottom of page 3 is a small table
10 that compares what was assumed in the first resolution on
11 the spending side compared to what the House and Senate
12 Finance has done.

13 The first item, income security where the First
14 Resolution assumes savings of \$600 million. Actually, the
15 House has sent over two bills that have the effect of costing
16 \$300 million. In the health area, where the First Resolution
17 assumes savings of \$1.8 billion, the House has not taken any
18 action -- that is, any Floor action -- or reported bills for
19 Floor action.

20 The Finance Committee has ordered reported bills that
21 would have a net savings of \$.7 billion, a somewhat higher
22 savings in the one bill and the Child Health Assessment
23 Program in the other, netting \$700 million.

24 In social services, the First Resolution assumes what is
25 called here an increase of \$400 million because it is \$400

1 million above present law. However, that was simply to
2 continue the level of grants at \$2.9 billion n fiscal year
3 1980, which is the level that it was at in 1979.

4 The House actually scheduled a bill for action which
5 would raise the ceiling to \$3.1 billion and finally, in
6 Revenue Sharing, the First Resolution assumes savings of \$400
7 million and the House has not acted at all. The Committee
8 today has approved the targeted fiscal assistance, which would
9 probably cost \$400 million.

10 I guess our staff suggestion would be that you indicate
11 in the area of health that you would probably be able to
12 achieve the ambitious savings goals of the First Resolution.
13 We suggest you might want to stick to that figure.

14 In social services, you might want to stay with the
15 First Budget Resolution -- in other words, keep the program at
16 the same level, \$400 million.

17 In income security, I think, it is probably unrealistic
18 to assume large savings. \$200 million or so might be
19 achievable.

20 You probably will have an opportunity to consider
21 legislation later this year.

22 The Chairman: What you are saying does not leave
23 something to initiate health insurance, does it?

24 Mr. Stern: In order to do that, you would have to have a
25 lower savings figure in health. I think that there is not

1 very much impact in fiscal year 1980 in what you are talking
2 about, but abrupt enough that you should allow a couple of
3 hundred million dollars.

4 The Chairman: A hundred million dollars to initiate
5 that?

6 Mr. Stern: I think you were talking about only being
7 effective in the last quarter of the fiscal year. That would
8 only be the part of the program that relates to mandatory
9 coverage by employers of catastrophic health insurance.

10 I think you had considered some ideas of phasing in that
11 might have a very small budget impact in fiscal year 1980.

12 The Chairman: I would like to leave the door open so we
13 would have the potential to act in that area and we have to
14 have enough so that we can act in the area.

15 Mr. Stern: Maybe you set a net savings of \$500 million.
16 That would take care of it.

17 The Chairman: If there is no objection, I suggest we
18 make it \$500 million with the understanding that we do expect
19 to start something in the health area.

20 Mr. Stern: Minus : \$200 million, income security. Minus
21 is \$500 million in health, \$500 million in social services,
22 probably something like plus-\$400 million in revenue sharing.

23 The Chairman: Do you think we could live with that?

24 Mr. Stern: It is going to be tight. It means if you act
25 in the income security area you are going to have to find some

1 savings. But, as it is, even those numbers are pretty far
2 short of what was in the First Budget Resolution.

3 The Chairman: How far short is that?

4 Mr. Stern: \$2.5 billion.

5 The Chairman: \$2.5 billion short.

6 Mr. Stern: To put it another way, that would represent
7 expenditure levels of \$2.5 billion higher than assumed in the
8 First Budget Resolution for new legislation.

9 The Chairman: That is mainly because we do not see how
10 we can save as much money as we thought that they were hoping
11 we were able to save in the health area, I take it?

12 Mr. Stern: Health is the largest single area, and income
13 security and revenue sharing.

14 The Chairman: Income security. They thought we were
15 going to save \$600 million. As of now, the House is moving
16 for an increase of \$300 million.

17 Mr. Stern: We just checked with Mr. Constantine. He
18 suggested we would not probably need more than \$100 million
19 for the health insurance for fiscal year 1980, because it only
20 goes into effect right at the end of the year. You can make
21 that minus \$600 million.

22 The Chairman: Then just \$100 million for that purpose?

23 Mr. Stern: Yes, sir.

24 The Chairman: Without objection, we will do that.

25 All right, now.

1 This health item, was that not something that we had been
2 talking about all along, that we did not think we were going
3 to be able to save that much money?

4 Mr. Stern: The number, in the first place, came from a
5 very unrealistic estimate of how much would be saved by the
6 administration bill and so, I think everyone in the process
7 got stuck with a very high savings number.

8 As it was, you have approved a number of provisions that
9 would have very substantial savings and you have also approved
10 some offsetting provisions, as you mentioned, on catastrophic
11 health insurance, but also in terms of Senator Packwood's
12 amendment on home health services and also the Child Health
13 Assessment. Those are partly offsetting.

14 Even so, it was an ambitious bill.

15 The House has not acted on anything in that area. It
16 remains to be seen how much that would be enacted.

17 The Chairman: Is it fair to assume that the House
18 Committee is going to go in with a figure about the same that
19 we are suggesting here?

20 Mr. Stern: They will probably go in with a figure that
21 is higher because they have already approved income security
22 amendments that cost money, do not achieve any savings at all
23 and social services. They approved a bill that increases the
24 total amount.

25 I do not know what the House Budget Committee will do,

1 but the Ways and Means Committee would stand by its
2 legislative action.

3 The Chairman: We have to get the suggestion over there
4 to them. Otherwise, they will just have to act without any
5 advice from us.

6 Mr. Stern: Yes, sir.

7 The Chairman: Is there any objection to what Mr. Stern
8 is suggesting here?

9 Senator Bradley: To recommend \$2.4 billion?

10 Mr. Stern: Income security would be minus \$.2 billion;
11 health minus \$.6 billion; health service \$.4 billion and
12 revenue sharing \$.4 billion.

13 Anything that this committee recommends will be on the
14 high side compared with what the Budget Committee does,
15 because the outlook for fiscal year 1980 is worse by quite a
16 bit than it looked back in April and May.

17 The Chairman: That is because of business conditions?

18 Mr. Stern: Yes, sir. The economic assumptions are more
19 pessimistic now, and it means less taxes relatively and more
20 benefits, so the size of the deficit, if you did nothing else,
21 would wind up being larger than what they thought originally.

22 The Chairman: They will probably cut it down. If we put
23 this figure or that figure, higher or lower, they will
24 probably reduce it anyway.

25 I am afraid that we are in for that. Is that a fair

1 anticipation?

2 Mr. Stern: I think that is right, but if you come up
3 with a recommendation that you think you can achieve
4 something, it seems to me that at least indicates some good
5 faith, at least indicates good faith on the part of the
6 Finance Committee.

7 The Chairman: Well, the big part of it is that the
8 health item was unrealistic to begin with, so we might as well
9 just go ahead and just submit it.

10 Those in favor, say aye.

11 (A chorus of ayes.)

12 The Chairman: Opposed?

13 (No response)

14 Mr. Stern: We will draft a letter to Senator Muskie on
15 that basis.

16 The Chairman: That takes care of that.

17 Senator Chafee: Mr. Chairman, may I ask one question on
18 the income security? Those projections were made on the basis
19 of burial benefits. Is that where that came from?

20 The Finance Committee assumed rather less in the income
21 security and the social security rea than the administration.
22 I do not think the Finance Committee assumed they would cut
23 out the burial benefits and student benefits. They thought
24 the savings would be achieved and some of the things in the
25 cash assistance welfare programs that the Committee has

1 approved before, the earned income regard and some of the
2 others.

3 Senator Chafee: It is my understanding in the House that
4 they killed off those suggestions of the administration
5 regarding the tightening up on the social security burial
6 benefits and student assistance, and so forth.

7 Mr. Stern: They have only acted in one area --
8 disability insurance. They have not acted in the other areas.

9 I do not think that it would be wise to assume that you
10 could achieve savings in the other areas. They have not
11 killed it in any formal sense of voting them down.

12 Senator Chafee: Would we consider those to bring it up,
13 it would have to be a positive act to bring it up on some
14 other piece of legislation, or something.

15 Mr. Stern: Yes, sir.

16 The Chairman: Anytime that we can find something that
17 would save some money, that would help cover some of the costs
18 of some of the suggestions that people have in this committee
19 that would cost money -- or Senators on the Floor that would
20 cost money -- but it is not as easy to find as one might
21 think.

22 I would say, with confidence, if the House had found any
23 easy ones over there, they would have sent that one to us
24 anyway already.

25 Where the House says no, we can do if we want to, but

1 anybody ---just take one example. Anybody who wants to take
2 away that burial allowance from Grandma and Grandpa, I do not
3 think you are going to get very far in this committee, or any
4 other committee. But there must be some of that where we can
5 save some money.

6 I am certainly willing to consider it, at any point.

7 Mr. Stern: As an example, Mr. Chairman, the Ways and
8 Means Committee has reported a bill that basically tries to
9 limit what a disabled individual can get as to what his
10 take-home pay was before his disability. They have had
11 difficulty getting that brought up. It still has not been
12 brought up on the House Floor yet.

13 Senator Chafee: Do you have any material about that that
14 I might look at?

15 Mr. Stern: Yes, sir.

16 Senator Chafee: I was not considering using it as a
17 centerpiece for my re-election campaign, but I would just be
18 curious.

19 The Chairman: Right.

20 Well, if there is no objection, then, we would recommend
21 that those figures as outlined by Mr. Stern, be adopted. They
22 are a little bit more oblique than we would like to do it, but
23 that is just the facts of life.

24 Mr. Shapiro: Senator, there is one issue I would like to
25 raise that several Senators have expressed interest in, the

1 situation of amendments that have been added onto
2 appropriations bills at this particular time in the House that
3 deal with the areas of this committee's jurisdiction as well
4 as the Ways and Means Committee.

5 That particular instance was an appropriations bill on
6 the House Floor last week, an amendment added that dealt with
7 the tax exempt status of private schools that prohibited the
8 ruling that the Internal Revenue Service had promulgated to go
9 into effect that dealt with the classification of the tax
10 status of private schools.

11 The question I am raising is not whether the amendment is
12 good or bad, but the jurisdictional aspect of it, because what
13 it does is prohibit -- it is a Treasury Department
14 appropriations bill. What the amendment does is prohibit the
15 Internal Revenue Service, or the Treasury Department, from
16 using funds that have been appropriated to it for purposes of
17 implementing this regulation.

18 The appropriations bills have been used as these type of
19 vehicles in the past. Certainly issues such as fringe
20 benefits, independent contractor -- and it may become a normal
21 means of dealing with rulings on tax policy issues much
22 broader than these types of issues.

23 It may be that the committee in its next meeting
24 would like to discuss this issue as to whether or not the
25 Committee has an amendment that may do exactly the same as

1 that amendment, but that this committee will put it on a bill
2 that is germane to this committee's jurisdiction.

3 I am not necessarily saying this committee would
4 disapprove of what that amendment does, but that this
5 committee would do it by different means.

6 The Chairman: Let me say this on the merits. I favor
7 that amendment, but that is, I favor what the amendment seeks
8 to achieve. But it does raise a real jurisdictional problem
9 and that is, every time someone does not like something that
10 the IRS does, they could offer an amendment on the
11 appropriations bill to prohibit the IRS from doing it. Of
12 course, when they do that, that is a matter of the
13 Appropriations Committee taking jurisdiction of something that
14 falls into the jurisdiction of the Finance Committee, and
15 those people have thought to protect their jurisdiction where
16 they thought we were trespassing on it.

17 So even though it might be a popular proposal, I guess we
18 had better be thinking about it the same way. When they start
19 moving into our area of jurisdiction -- this is not something
20 that the Appropriations Committee raised. Nobody over there
21 had anything to do with that. Is that not right?

22 Either the Senate Appropriations Committee nor the House
23 Appropriations Committee started this jurisdictional problem.
24 Is that right?

25 Mr. Shapiro: It started on amendments on the House

1 Floor. It may very well have been that they were
2 Appropriations Committee members, but not amendments done in
3 the Appropriations Committee. Amendments added on the House
4 Floor last year -- and there are four this year. The Private
5 Schools is a major one.

6 It may very well have been Appropriations Committee
7 members in the Committee report, however, of the
8 Appropriations bill. The report language suggests that the
9 IRS not pursue this amendment until the appropriate
10 legislative committees review it.

11 That is, the Appropriations Committee said we are not
12 going to cut out the funds, but we think you should hold up
13 until the committees with jurisdiction review it. However, on
14 the House Floor, amendments were added to prohibit the use of
15 the Treasury funds for implementing the regulation.

16 The Senate Appropriations Committee, as I understand it,
17 has asked this committee for guidance in a sense that if you
18 are going to act, that the Appropriations Committee, I do not
19 think, is intending to go after it in Committee.

20 There is no way to determine what is going to happen on
21 the Senate Floor.

22 What this committee could do is write a letter suggesting
23 on the matter of purely the jurisdictional question, the
24 committee is going to consider the matter, possibly at your
25 next meeting, and not to consider the matter on the

1 appropriations bill.

2 The Chairman: What can you tell us about that, Mr.
3 Lubick?

4 I would think you would be concerned about this matter
5 over there at Treasury.

6 Mr. Lubick: We are very concerned, Mr. Chairman. We
7 would much prefer to be at the tender mercies of the Finance
8 Committee because we think that the matter involves
9 substantive tax law and a rider tacked to an appropriations
10 bill that says you cannot use money -- leaves the ruling in
11 place but says you cannot use any money to carry it out --
12 just leads to confusion.

13 We would much prefer to present to you the reasons for
14 our ruling, which we think is correct, and compelled by the
15 statute and by court decisions. But if it is to be
16 overridden, we would much prefer a change in the law to come
17 from your committee than to say the law stays the way it is,
18 but we cannot carry out the law. That just leads to chaos,
19 and the revenue agents do not know what to do, and if the
20 revenue agent raises a question out in the field, that ruling
21 is there and the interpretation is there.

22 It just leads to chaos administratively.

23 I would very strongly urge you to assert the jurisdiction
24 of the Finance Committee to deal with the issue on its merits.
25 We will present to you the reasons for our position, and if

1 you decide we are wrong, we would expect you to legislate a
2 correct rule that we are very happy to follow, but to leave
3 the whole situation in limbo and to have year after year
4 questions of substantive rules of the tax law decided by
5 riders to appropriations leads to both bad tax law and bad tax
6 administration.

7 The Chairman: I do not know the answer right now. What
8 are your thoughts, Senator Dole?

9 Senator Dole: Are there not a number of bills in the
10 committee now dealing with this issue?

11 Mr Shapiro: There are. In addition to that, both the
12 Finance Committee and the Ways and Means Committee have held
13 hearings on this issue. The subcommittees of jurisdiction are
14 both tax writing committees.

15 The Chairman: One possible thought to me occurs. I
16 wonder if we could sell this thing by just putting an
17 amendment on that amendment to simply say that the provisions
18 of that amendment shall cease to be effective as soon as
19 Congress has legislated in the area.

20 What I had in mind, we could report out something that we
21 felt would be appropriate and if we can dispose of it in this
22 session --

23 Senator Dole: That would be legislation.

24 The Chairman: It would be legislation on any bill. If
25 we passed something that says, here is what we think that the

1 rule ought to be, or whatever, then --

2 Mr. Lubick: You might very well decide not to legislate
3 in the area, so perhaps your amendment should be it would be
4 effective until Congress legislates, or does not legislate, in
5 the area.

6 In other words, you may decide that what the services
7 have ruled is correct. I would hope we could leave this
8 matter for your consideration, that it not be done and ask
9 the Appropriations Committee not to deal with it, but to
10 indicate, perhaps, to them that you will take up the matter,
11 that it will be discussed before the substantive committee,
12 the Finance Committee, that has jurisdiction. You will
13 consider it.

14 That should be of sufficient assurance to them that the
15 normal legislative process will be followed and a
16 congressional determination will be made in the area.

17 Mr. Stern: Our suggestion is that you take it up on
18 Thursday morning. You have your next session on Thursday
19 morning. We could put it on the agenda.

20 The Chairman: Let's put it on the agenda and talk about
21 it Thursday, then.

22 Frankly, I know that jurisdictional problem, but I come
23 from one of those states where people are especially concerned
24 about the matter. It would be easier to vote for what the
25 House has done than to explain why you did not.

1 And so, if you can show us a better answer, I am willing
2 to consider a better answer. I do not want to be left in a
3 position of being misunderstood about the matter. That is one
4 of those areas where you could easily be misunderstood.

5 Then we will talk about it and put it on the agenda for
6 the next meeting.

7 Mr. Stern: We will draft a letter indicating to the
8 Appropriations Committee you intend to do that.

9 The Chairman: All right.

10 Without objection, then, that is what we will do.

11 Now, wait a minute. You have to draft that letter to the
12 committee to vote on that. You are talking about drafting a
13 letter to the Appropriations Committee.

14 Mr. Stern: The problem is, they are meeting apparently
15 this afternoon, so they wanted some guidance one way or the
16 other. I think that they are a little apprehensive about
17 doing something substantive like this on an appropriations
18 bill and the suggestion would be that you indicate that.

19 The Chairman: I would simply tell them that we are going
20 to discuss the matter, but I would not suggest that we ask
21 them to withhold their decision. Let them do whatever they
22 want to do. Just say that we will discuss the matter
23 Thursday.

24 I do not want to tell them what they ought to do about
25 the matter, not right now. It seems to me we have to decide

1 for ourselves what we think we ought to do.

2 But I am not prepared, at this point, to ask the

3 Appropriations Committee not to act on that.

4 Mr. Stern: All right. We will just advise them that we

5 will take it up on Thursday morning.

6 The Chairman: I would think that they might decide well,

7 we would either go along with it or not go along with it, but

8 in any event that when the Finance Committee acts, that they

9 will consider what we suggest. They may want to even take it

10 as a Floor amendment.

11 Whatever we suggest about the matter, I do not want to

12 tell them that, as of now, I do not want to tell them that we

13 do not think they ought to act. I would just tell them that

14 we are going to consider that matter, that it is within our

15 jurisdiction and we are going to talk about it Thursday

16 morning. We do not know what we are going to recommend to

17 them, but we are going to discuss it.

18 Mr. Stern: All right.

19 The Chairman: All right.

20 Then, I guess that gets us to the crude oil tax.

21 This is the crude oil tax. Is that at Mr. Gravel's

22 suggestion?

23 Mr. Stern: Senator Gravel wrote a letter suggesting that

24 the expression "windfall profits" was not an accurate

25 characterization of what the bill did, that it was, in fact,

1 an excise tax or severance tax. And in his view, the word
2 "windfall profits" should be avoided in any official committee
3 publication.

4 At any rate, we took the words "windfall profits" off the
5 agenda.

6 The Chairman: I think that whatever we want to call it,
7 that is something that we can resolve after we decide what to
8 do about it. By the time we get through, it might be
9 something at variance with what we have here, anyway.

10 It is immaterial what you call it at this point.

11 Senator Dole: Mr. Chairman, do I understand that we will
12 be discussing the crude oil tax with the President this
13 afternoon at 4:00?

14 The Chairman: Yes. The President is inviting the
15 members of the Committee to discuss this matter with him and I
16 think that is a good idea. I just think that it is better for
17 the President to explain his view about the matter to all
18 members of the committee rather than to the Chairman and the
19 Ranking Member, to all of us what he thinks about the matter.
20 Then there is less room for misunderstanding.

21 So I hope the Senators will make themselves available.

22 I understand that the Majority Leader is going to try to
23 see that there be no votes on the Senate Floor between 4:00
24 and 5:00 and hopefully that will free us to visit with the
25 President and Senators can explain what they think as of now,

1 and the President can explain his views to them.

2 And I hope that we will have a useful exchange of views.

3 I hope all members can plan to be there.

4 This memo you gave us is good. It seems to me that we
5 ought to commence this meeting if we can -- if we do not have
6 it now, we can do it later, but I do think we need to have
7 some charts or use that old blackboard and let somebody
8 explain to us how that tax works, because I gained the
9 impression that you really have to have it explained to you
10 about three times at a minimum before you can really hope to
11 understand it, unless you are a lot smarter than I am.

12 You really need to separate out each segment of it and
13 understand how this works.

14 I sort of wish we had done that even before we started
15 the hearing because it is not as easy to understand as some
16 might want to suggest.

17 Mr. Shapiro: We have two hand-outs to the committee.
18 What you have first is the price regulations. The second one,
19 which has not been passed out yet, is an outline of the House
20 bill. You have to have an understanding of the price control
21 regulations because the windfall profits tax is designed to
22 tail on to that. So this is just a quick summary of that.

23 As you know, the President had the authority after May of
24 1979, to do whatever he wanted to as far as this is
25 concerned.

1 That was the EPCA Act. We have two proposals here to
2 give you a better understanding of the price controls. The
3 top half of the page, the regulations that were in effect
4 prior to June 1, 1979, that sets forth the controls on oil
5 pricing.

6 As you see, there are five categories there. The first
7 one is lower tier old oil which is, in effect, oil discovered
8 before 1973 and that was controlled on an average price of \$6
9 per barrel.

10 That means that there is some oil that may be controlled
11 at a price of \$4 or \$5, \$7 or \$8, but the average price ws \$6.
12 That differential was based on the grade, quality and location
13 of oil that determines that price.

14 The second category, upper tier and new oil, is oil that
15 is discovered after 1972 as well as production from reservoirs
16 discovered before 1972. That exceeds the decline curve, so
17 that is for an increase in production.

18 So on an old property, if they ceded that, they would get
19 a higher price, \$13 a barrel on the average under the old
20 regs.

21 The third category is stripper oil, which is defined by
22 statute. That definition is a property on which there was 10
23 barrels or less oil produced over a 12-month consecutive
24 period. Under the price controls for stripper oil that was
25 decontrolled, you have the world price. It sold at an average

1 price of \$14 per barrel in 1978 and today the world price is
2 \$22 per barrel. That is what stripper oil is getting today.

3 The general definition, once you are a stripper, you are
4 always a stripper. Once you have met that definition, meaning
5 you have produced 10 barrels or less over a 12-month
6 consecutive period, you can produce 50 to 100 barrels or more,
7 once you have met that definition in a prior 12-month
8 consecutive period.

9 The next category, Alaskan oil. This has a special
10 situation. Alaskan oil is controlled at an upper tier ceiling
11 price, \$12.91. However, Alaskan oil, up until recently, has
12 not been able to get the full control price because of the
13 very large transportation costs that apply to Alaskan oil.

14 The reason for that, if a refinery wants to buy oil, he
15 will be willing to pay as much as the world price. The world
16 price in 1978 was \$14.

17 While Alaskan oil has a transportation cost of
18 approximately \$9 and no refinery is going to pay \$14 for
19 Alaskan oil plus \$9 transportation costs, which is \$23, if the
20 can go to the world market and buy it for \$14.

21 Therefore, even though Alaskan oil could have gotten a
22 control price of almost \$13, it actually sold for a little
23 over \$5.25.

24 The Chairman: You now, right here it seems to me that
25 we really need to have a blackboard and a chart so that you

1 can draw that thing out and then you can explain it to
2 someone. At the next meeting, I would hope that between you
3 and Mr. Wetzler and Mr. Stern and Mr. Lighthizer that you
4 fellows would sort of rehearse what you are going to present
5 to us and then let's use some blackboards and some charts if
6 you want some charts, or a blackboard that we can flip over
7 and use two sides.

8 We need to be able to separate these problems out, issue
9 by issue, and talk about it, and then when we consider these
10 amendments, we need to do the same things on the amendments.

11 When people can see a picture of what they are talking
12 about, a diagram of it, so that they understand what it is.
13 You take this Alaskan problem. That is of concern to Senator
14 Gravel here, of course. It is of concern to the President and
15 the Secretary of Energy and I think all of us would want to
16 take a look at that and see how just how that works out.

17 And I think you need a diagram to show that.

18 Mr. Shapiro: We do have some diagrams. We do not have
19 all of them that you may be interested in, so for Alaska, we
20 will just put it on the blackboard showing the controlled
21 price of transportation costs and why the Alaskan oil was
22 getting less than the controlled price.

23 We can put that on the blackboard for you, as well as
24 some of the other examples you may want.

25 The Chairman: When members are going to bring their

1 amendments up, if we need some sort of a chart or diagram to
2 explain what this is and how it works out, it would be very
3 helpful. We could have it explained in a way that not only
4 the Senators, but people in the audience, the media and the
5 assistants who are here monitoring this meeting for their
6 Senators who may necessarily be absent, or may not even be on
7 the committee, can explain that to other people.

8 Otherwise, I do not see how we are ever going to do
9 justice to it.

10 Let us go back to the Alaskan thing again, since you
11 mentioned that.

12 You say that the transportation costs in Alaska is \$9.

13 Mr. Shapiro: Between \$8 and \$9, probably around \$8.50.

14 The Chairman. \$8.50.

15 All right. Mind you, is that \$8.50 to get to the
16 pipeline, to Valdez, or get it to the point of delivery?

17 Mr. Shapiro: It is about \$6.25 to the pipeline and the
18 extra dollar and a quarter or so, the rest of the \$2.25 is for
19 shipping and other transportation costs.

20 It depends where it actually goes.

21 The Chairman: What you are saying is that with a ceiling
22 price of \$12.91, is that it?*

23 Mr. Shapiro: Yes.

24 The \$8.50 on top of that, that would get to \$21.41.

25 The Chairman. \$21.41.

24
1 Mr. Shapiro: When the well price was \$14, nobody was
2 willing to pay \$21 to buy Alaskan oil when they could buy
3 foreign oil at \$14. That was last year.

4 Now that the world price is up to \$22, then Alaskan oil
5 will now be selling for its control price, because the
6 transportation costs, plus the controlled price, is less than
7 a refiner would have to pay for foreign oil.

8 The Chairman: So the world price that the Alaskan oil can
9 now sell and manage to sustain their transportation costs?*

10 Mr. Shapiro: That is correct.

11 The Chairman: All right.

12 How did the House Committee handle that in the House
13 bill?

14 Mr. Shapiro: When the House Ways and Means Committee
15 acted, the world price was not at \$22; it was at \$18.

16 The way the House looked at it was that last year, 1978,
17 Alaskan oil was selling for \$5.25. The administration
18 proposed an exemption for Alaskan oil. At the hearing,
19 several Ways and Means members asked the administration some
20 of the reasons for the exemption. They were not completely
21 satisfied with the responses as to the purposes of the
22 exemption.

23 The reason the administration actually exempted Alaskan
24 oil, if you tax in the upper tier, the base price would be
25 \$13. Since Alaskan oil was selling for, at that time, \$7.25,

1 it was so far below its base price, the administration said
2 there would be no tax. You might as well exempt them in
3 addition to trying to provide an incentive. There was no
4 reason to have a tax because they would not be taxed until the
5 price was above \$13. Since the price was \$7, it was so far
6 below its base price that the administration just exempted it.

7 House members wanted to increase the amount of revenue
8 from the tax and they were concerned about the exemption for
9 Alaskan oil. Therefore, they tried to view what they thought
10 was the situation being that the Alaskan oil was making a
11 profit at \$5.25 in 1978.

12 When the Ways and Means Committee acted, the price of the
13 oil was \$7.25 and it had gone up to \$8 a little after that
14 because there are some price changes in the shipping.

15 The Ways and Means Committee set a base price of
16 approximately \$7.50 with several adjustments so that there
17 would be no rollback, meaning that the tax would not require
18 that the producer make any less profit than they are making
19 now.

20 No windfall profits tax, and the amount of price they
21 were getting at that time.

22 Now, when the world price went to \$22, Alaskan oil shot
23 up from \$8 to very close to its control price. If you
24 consider the House bill right now, the House bill picks up a
25 very significant tax on Alaskan oil that was not

1 necessarily intended by the Ways and Means Committee to roll
2 the price back, although the Ways and Means Committee wanted
3 to have a tax on Alaskan oil.

4 Now, the problems that occurred, the Ways and Means
5 Committee believed since Alaskan oil was making a profit at \$5
6 and \$7, they should pay some tax. The industry, on the other
7 hand, is making two arguments.

8 First, on the other side, when Alaskan oil was being
9 produced and being explored in the early 1970s, there was no
10 expectation that the price would be as high as it was since
11 they were projected to make a profit on a much lower price,
12 that there should be some windfall profits on Alaskan oil
13 rather than an exemption.

14 That is the argument of the Ways and Means members that
15 advocated a tax on Alaskan oil.

16 On the other side of that, those producers who are in
17 Alaska -- and essentially there are three major producers.

18 SOHIO owns approximately one-half of the Alaskan oil. ARCO
19 and EXXON own the other half equally, one-quarter each.
20 There are many other producers in Alaska, but those three
21 own the majority, almost 100 percent of that, 97, 98 percent
22 of the Alaskan oil.

23 The other side of the argument made by these major
24 producers is that the transportation costs, meaning the
25 pipeline, so far exceeded the expected costs, that even though

1 they may not have expected the price to go as high as it has,
2 the pipeline cost far exceeded what they expected it to be.

3 The second argument by the producer, in Alaska they had
4 only spent -- and part of what they have spent, too, in the
5 drilling in Alaska, they have a significant amount of capital
6 expenditures for increased drilling.

7 As a result of that, there should not be a significant
8 tax that the House put on.

9 The administration modified its position with regard to
10 Alaska and does not support the House bill. They are not
11 asking for an exemption for Alaska, but to treat Alaska in the
12 second tier.

13 That would mean that, essentially, there would be no
14 rollback in price, the base price, the tax would be
15 essentially what Alaska is getting today, which means to the
16 extent that Alaskan oil would have a windfall profits tax
17 imposed, it would only be on price increases above what the
18 level is today.

19 Senator Dole: Different from the revenues, the
20 \$577 million?

21 Mr. Shapiro: On a net basis, a net of \$577 million for
22 purposes of the trust fund. The administration proposal, as
23 well as the House bill, put the gross tax into the fund. That
24 would be \$1 billion.

25 Senator Bradley: The tax would also ultimately be on the

1 difference between the OPEC price decisions and the base
2 price.

3 Mr. Shapiro: The base price is adjusted for inflation,
4 but you are correct. The OPEC price increases.

5 Senator Bradley: It assumes an OPEC price increase of 1
6 percent above inflation.

7 Mr. Shapiro: The revenues do, that is correct.

8 Senator Bradley: For every 1 percent above inflation,
9 how much more would that raise?

10 Mr. Shapiro: We are giving a rough estimate of between
11 \$20 and \$30 million for each 1 percent above the inflation
12 rate.

13 Senator Bradley: The price increase from December to now
14 is 63 percent. Inflation was about what -- 8 percent, 10
15 percent?

16 Mr. Shapiro: Between 8 and 10 percent, in that range.

17 Senator Bradley: If this formula was in place next year
18 and there wa a price increase similar to the one we have
19 experienced now, you are talking about 50 times \$20 million.

20 Mr. Shapiro: That is correct.

21 Senator Bradley: An extra \$5 billion, right?

22 Mr. Shapiro: That is right. The administration has been
23 very shy about having estimates much higher than that because,
24 as we can appreciate, if you start estimating what OPEC is
25 going to do, it gives them a base to start from and they at

1 least would have increases to the level of that base.

2 The administration, for that reason, has been somewhat
3 conservative in the figures. They may reasonably expect the
4 revenues to be higher, but they do not want to advocate that.

5 At the staff level, we project a little bit higher, but
6 then again, we are not projecting the increases that occurred
7 this past year, or do we suggest that they may be doing that
8 in the future.

9 But if they do, your analysis is correct that the
10 revenues would be increased significantly.

11 Senator Bradley: Mr. Chairman, that is why I suggest, as
12 we look down the road as to what we might entertain to accept
13 or reject that there be a revenue stream projecting based on
14 different OPEC price increases so that we can see how much
15 revenue might be raised.

16 Senator Gravel: It is very difficult to do that,
17 because, as OPEC increases its prices, you have a wave of
18 reaction that goes right into the global economy and causes
19 inflation at varying rates in varying sectors, depending on
20 how much you use of that specific quantity of energy.

21 So that when you project, you assume you are going to get
22 some revenues because everything else is frozen, but nothing
23 is frozen in society. Immediately there is a response that
24 takes place.

25 That is the reason you saw when they had a fourfold

1 increase in prices in foreign oil in early '73 and '74 that yo
2 had a threefold response in inflation in just the cost of
3 looking for more energy. That was within a short period of
4 time.

5 It is impossible for them, I would think -- maybe Mr.
6 Shapiro would think differently -- to give you any figures
7 that would have any real meaning to the real world.

8 Mr. Shapiro: We have to have some figures to give the
9 Committee some idea. We do not really feel, or have
10 assurance, that these figures are accurate.

11 Let me give you another example to just tag on what you
12 just said, Senator.

13 If the import quotas stay in effect and are effective in
14 keeping imports down, that means that the domestic supplies
15 may cost more. That means if you cannot import but so much,
16 the domestic prices may be booted up to a high level where
17 domestic oil is selling at more than OPEC prices. That is a
18 factor that may have to be taken into account.

19 It is very difficult for us to make a complete
20 assessment, but we will try to crank it in to some extent.

21 Senator Gravel: Mr. Chairman, could I try to use an
22 example? That Alaskan experiment is very complicated and it
23 really leaves somebody hanging off the limb, and I tried to
24 understand it. I have one example I would like to make.

25 It is like comparing a farmer who has some chickens and

1 they are now laying eggs. I am not a farmer, but I know you
2 have to get chicks, you have to feed them, you have to house
3 them. I assume there is some point in the life of a chicken
4 it tries to lay eggs and then when it gets too old, it does
5 not lay any more eggs.

6 When people are looking at last year that there may have
7 been a profit on oil at \$5.25, what they are looking at, they
8 are looking at the chicken who is in front of them who is
9 laying eggs. They have forgotten the fact that somebody had
10 to invest the money and pay out constantly to get the chicken
11 to that point in time, and had to drill some holes and not
12 find any oil. They are just looking at the cost of that one
13 chicken, nothing else at that one point in time, and then
14 measuring that to the feed that they give the chicken and the
15 egg that comes out the other end.

16 They say, boy, is that not an interesting thing.
17 Senator Bradley: In the Senator's example, how fast do
18 we write off the chicken?

19 Senator Gravel: If you truly want to know what the cost
20 is, you have to know what it costs you to bring up the chicken
21 to a chicken, and know how much it costs to heat the barn and
22 put the lights on to keep those things alive until -- anybody
23 who takes economics and ever measures what is there and gives
24 no consideration of what it took to get there does a great
25 disservice, and secondly when you turn around and say it looks

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1 like it is good, you have to accept that the cost in Alaska is
2 exorbitant compared to other parts, and we will have a chart
3 that will show that. And that, in itself, should give you
4 some indication that there is something wrong with the
5 superficial computation that is made, particularly when Bob
6 here said that there was an unusual cost that is going to
7 be added to the continual pumping of oil.

8 We are not talking about discovery. Bobby said
9 additional costs. We are not talking about exploration for
10 new oil. We are not talking about anything but the cost of
11 taking the oil which is in the pool and bringing it to the
12 head of the Alaskan pipeline.

13 The Alaskan pipeline was the largest project in the
14 history of the world -- \$8 billion. The oil companies have
15 got to spend in the future to get the oil from the pool to the
16 head of the pipeline is somewhere between \$12 billion to \$19
17 billion.

18 That is the prospective cost that they have yet to
19 undertake to just pump that pool out.

20 That, of course, is the question. That cost is not
21 considered, if you put a tax on it based on inflation. What
22 about the increased cost?

23 Senator Bradley: Let me just ask one more question that
24 relates to your earlier point where you said that the OPEC
25 price increased fourfold in 1973. Did you say that the cost

1 of doing business in Alaska in that period exceeded 400 .
2 percent?

3 Senator Gravel: Well, there is an eightfold increase in
4 the Alaska pipeline during that same period. That is exactly
5 -- the pipeline approval was signed into law in November of
6 '73. The boycott took place within days of that event. And
7 so the pipeline was constructed in '74, '75 and '76 during the
8 whole period, and it went from \$900 million to \$8 billion.

9 There were a lot of environmental problems and
10 oversized. Fairbanks, in '75, in one year, had an 18
11 percent inflationary push in one community.

12 Senator Bradley: In such an inflationary environment,
13 what was the return on equity for the companies?

14 Senator Gravel: In '74, it was for international
15 companies, the same ones in Alaska, 19.9 percent, and
16 domestics, 18.3 percent. That precipitously came down in '75
17 to today.

18 It is one point below average manufacture.

19 SOHIO enjoyed a good period last year because they had
20 been so low before that this is the first time they have been
21 healthy. They liquidated literally everything they could get
22 their hands on, so they would be able to invest in the
23 pipeline.

24 I read the loan agreements. They are tighter than what
25 you would pay or what I would pay to go down and borrow from a

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1 Beneficial Finance or a Household Finance. You cannot believe
2 how these companies had to put themselves into hock and to
3 hamper any possible economic activity contingent upon the
4 success of that line.

5 So now, the first year they have a good show, immediately
6 the Congress wants to tax them and they obviously can foresee
7 what they have to spend in order to continue that good show.

8 Senator Bradley: What is the anticipated rate of return?

9 Senator Gravel: I asked this question of Salomon
10 Brothers. Nobody can anticipate the rate of return when you
11 are talking about a cost differential between \$12 billion and
12 \$19 billion. Literally, the differentials and estimates in
13 the companies is the cost of the entire pipeline. That is,
14 right now it is a tariff of \$6.25 -- which, incidentally, is
15 being litigated. The government wants to push the tariff down
16 and as an aside, the reason why I have been pressing for a new
17 Canal through Panama, I have done calculations to show with a
18 new Canal we can lower the cost of oil by \$1.50 a barrel, just
19 to get it to New Jersey.

20 Senator Bradley: It could not come soon enough, Senator.

21 Senator Gravel: It is coming there now. It is coming at
22 an increased cost, and the cost with the regulated price is
23 being eaten by the companies.

24 Mr. Shapiro: I do not know where the Committee wants to
25 go right now. I think it would be helpful for the Committee

1 to have the charts and graphs.

2 Right now, we have passed out a very cryptic outline of
3 the price controls to give you an understanding of the old
4 regs and new regs and we also have somewhat of a short summary
5 outline of the windfall profits tax.

6 Senator Gravel: Mr. Shapiro, I sent a letter to the
7 Chairman. I noticed on the schedule, he was going to have to
8 have the schedule reflect that it is not a windfall profits
9 tax. I noticed on our booklet here -- do we have to say it is
10 a windfall profits when the last part of this is a lie? Do we
11 have to perpetrate these lies?

12 Or, to be more accurate, it is the responsible body of
13 the Congress.

14 Mr. Shapiro: What the pamphlet describes is exactly the
15 title of the House-passed bill which is what the pamphlet is,
16 and what the Senator referred to before you came in was until
17 the Committee acts on it, it may want to call it a number of
18 different things, and he indicated that there will be no
19 distinction.

20 Senator Gravel: I will have a first amendment, I hope,
21 Mr. Chairman, which will be to strike the title of the House
22 bill and to correct the demagogic language that the
23 unfortunate House insisted upon foisting upon the American
24 psyche. I think we, in the Senate, can be a little bit more
25 accurate. That will be the first amendment I will propose.

1 The Chairman: Maybe we could make the tax such a good
2 tax, Senator, that by the time you are through you will like
3 the name, or want to improve on it, that you can think of a
4 more attractive name, one that would have more appeal.

5 I am not counting on that right now.

6 Anyway, we will talk about that after we see what kind of
7 bill we are going to write.

8 Now, I am going to have to leave and I think Senator Dole
9 indicated likewise. I have an appointment.

10 When do we discuss this matter next?

11 Mr. Stern: Your next scheduled meeting is tomorrow
12 morning, a hearing on Patricia Harris, the nominee for
13 Secretary of HEW. Thursday morning at 10:00 you will take up
14 this matter of the tax exempt status of private schools and go
15 on to the crude oil tax and we will have material on the
16 blackboard and so forth, as you directed, Mr. Chairman.

17 The Chairman: I want to ask people to think in terms of
18 getting us some charts together and some diagrams to show us
19 what we are talking about here because this is very difficult.
20 Naturally, we have Mr. Lubick here.

21 I want to suggest, Mr. Lubick, you see if you can get us
22 just a little chart, some numbers, some columns of figures
23 together.

24 I, for one, want to see how much tax all of this amounts
25 to. I think where you are, you could take some oil company

1 tax returns and give us some average figures and see how much
2 the individual pays, how much the corporation pays, how much
3 the shareholders pays on \$100 of additional income, under
4 whatever the logical assumptions should be.

5 We had a man who had about the same job that you have
6 got, Mr. Lubick, up here, Edward Cohen. I do not know where
7 he got his figures.

8 I asked him -- was his job the same as your job?

9 Mr. Lubick: At one time it was.

10 The Chairman: At one time he had the same job before you
11 had it.

12 One time he came as a witness and I think we can
13 stipulate he is a good lawyer, just as you are; he knows
14 something about taxes just as you do and he is a good
15 professor ---you are a professor also, Mr. Lubick?

16 Mr. Lubick: I have been from time to time.

17 The Chairman: So you are both good professors, so that
18 we can stipulate that. We can all agree to that. As far as I
19 am concerned, either one of you could represent me in a tax
20 case.

21 I asked him would he please get up some figures and try
22 to show us what the real tax is? For example, if you take a
23 12 percent severance tax in my state, 12.5 -- I think Alaska
24 is 12.25 -- they did not want to say they had the highest
25 severance tax. They made it one quarter of 1 percent lower

1 than the Louisiana tax, but they hired our lawyers to show
2 them how to pass their tax.

3 They then -- if you assume Alaska, or assume Louisiana,
4 or assume Texas or Oklahoma, as the case may be, and start out
5 ---take what the severance tax would be and then take what the
6 state income tax would be and then if they have one, you would
7 take what the Federal income tax is, assuming what people in
8 that bracket would likely be, and then take what this tax
9 would be and come down to the bottom line and say on \$100 of
10 additional income, how much would they have left?

11 People will have a depletion allowance. Where they have
12 a depletion allowance, I think that should be taken into
13 account.

14 I think you need to show us how it would be when they are
15 putting that money back in the drilling and when they have
16 intangible drilling costs, and how it works out when they do
17 not have an intangible drilling cost, because everybody tends
18 to put the whole thing together to suit his own purpose.

19 And I think that Treasury ought to give us their figures
20 assuming both ways -- assume that he is putting it into more
21 energy and assume that he is not, and say that we could look
22 at both sides of it and, I hope, come up with a pretty
23 balanced understanding of this. That is going to take quite a
24 bit of homework on your part, Mr. Lubick. I am sure you have
25 some able assistants in trying to get that up.

1 I would hope we could run that past experts on the
2 committee staff and let private industry take a look at it and
3 see if that is an honest presentation.

4 We can argue about the philosophy and about politics and
5 all of that, but we should not have to quarrel about what the
6 facts are. The facts are something, and what the law is, and
7 what the existing law is.

8 If we get to how much people are paying, you people in
9 Treasury could pull those tax returns and see whether they are
10 telling us the truth or not, and we have the facts and we
11 ought to be able to reach a better conclusion and think just
12 in general terms and speculating out without anything having
13 any relevance to the next thing in front of it.

14 We want you to help us write a good bill. I know that
15 you will.

16 Well, if there is no further suggestion at this moment,
17 we will adjourn to meet tomorrow morning.

18 (Thereupon, at 12:15 p.m. the Committee recessed to
19 reconvene at 10:00 a.m. on Wednesday, July 25, 1979.)

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