

MIKE W.

1 EXECUTIVE SESSION ON THE DEFICIT REDUCTION

2 TUESDAY, FEBRUARY 28, 1984

3 U.S. Senate

4 Senate Finance Committee

5 Washington, D.C.

6 The committee met, pursuant to notice, at 10:16 a.m. in
7 room SD-215, Dirksen Senate Office Building, the Honorable
8 Robert J. Dole (chairman) presiding.

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

13 Also present: Mr. John Chapoton, Assistant Secretary for
14 Tax Policy, and Mr. George Schieber, Deputy Assistant
15 Secretary for Tax Policy, Department of the Treasury.

16 Also present: Mr. Roderick DeArment; Mr. Michael Stern;
17 Ms. Sheila Burke; Mr. Richard Belas; Mr. David Brockway;
18 Mr. James Wetzler; and Mr. David Hardee.

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1 The Chairman. Mr. DeArment. I have been handed a letter
2 by Senator Metzenbaum which I would ask the Treasury to take
3 a look at. It indicates that, based on a Forbes Magazine
4 article, with reference to the DISC program, if in fact we
5 pass the legislations now pending, some of these companies
6 will escape about \$13 billion in taxes, and I am not certain
7 whether or not that is accurate, but I would hope that maybe
8 Treasury might take a look at the letter and the article,
9 plus he includes a letter from a Kansas expert who indicates
10 that all this does is help the big, big business concerns
11 -- it does nothing for small business. Maybe if Treasury
12 could take a look at that and respond.

13 Mr. Chapoton. We would be happy to, Mr. Chairman.
14 Obviously, there are going to be some tax benefits. That is
15 what the program was designed for -- to provide tax benefits.

16 The Chairman. All right. There have been benefits,
17 but I think perhaps -- I am not certain whether we will get
18 to DISC in this particular package, but it is a matter of
19 some interest. I am wondering -- there are probably a lot
20 of people -- I understand there is a room full people in
21 what room?

22 (No response)

23 The Chairman. The overflow room for those who are here,
24 and I think it is fair to say that we are not going to get
25 into any add-ons today. I mean, there are about 100 items

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1 that members want to add to any package we put together.
2 That would include such things as anything in the insurance
3 area, anything in the add-on area. So, if there is anyone
4 here concerned about that, anyone representing insurance or
5 any other group, we might be able to relieve them of that
6 worry this morning. What I would like to do this morning
7 is to go back to two or three items that are pending on the
8 spending side and then move into the tax reform areas that
9 Treasury has recommended and try to agree to those that we
10 can agree on and set aside those, for the time being, we
11 can't agree on, so we won't consume all the time if somebody
12 has an objection to a certain provision, and we haven't been
13 able to resolve that. I think we can resolve some of the
14 differences. Then, we might move on and take up some other
15 matters. We have got probably, all together, a couple of
16 hundred different items to consider, and if we can finish up
17 at least the original assault on the spending side, and then
18 move to the reform side, maybe we can accomplish quite a bit
19 this morning. Do you have any agenda, Rod? I think we are
20 just going back to that same agenda. It is the same material
21 that we had. We will give you copies of that.

22 Senator Roth. Mr. Chairman.

23 The Chairman. Senator Roth?

24 Senator Roth. Could I make a couple of observations?

25 First of all, with respect to DISC, I too have had a lot of

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1 concern as to whether the proposal will be of any real help
2 to small business, and I think anything we do in the area, it
3 is extraordinarily important that we help small business
4 that heretofore has not been able to participate in trade
5 that much. And I will be very much interested in having
6 your comments on the impact on small business -- whether it
7 really does cover them. And if not, what we can do to ensure
8 that it does.

9 The Chairman. Okay.

10 Mr. Chapoton. Senator, the concern of small business
11 -- and it is a concern that we have given a good deal of
12 attention -- is that by requiring a foreign presence which
13 is required to make the proposal, GATT, legal, that that is
14 difficult for small business to comply with. We recognize
15 that that is a legitimate concern of small business, and we
16 have said that we want to try to develop a way that they
17 can use the foreign sales corporation mechanism, and we
18 recognize that, without some special provision, small
19 business will have difficulty doing so.

20 Senator Roth. Secondly, Mr. Chairman, I would like to
21 go back to the point that Dave Boren was making at our earlier
22 meeting. Many of us are very concerned about doing anything
23 really in the tax area until we see what is going to happen
24 on the spending side, and there is a lot of, I know,
25 difference and debate as to whether TEFRA was based on \$3.00

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1 for one or not, but some of us feel that before we can support
2 it -- the taxes -- that we have to know very much where we
3 are on the spending side. Let me say that-- I have two
4 observations that I would like to make. Number one, I
5 happen to be one of the people that believe we cannot spend
6 what the Administration is asking on defense, so I would hope
7 that that is reduced -- the increase is reduced --
8 substantially. I, for one, do not see that as a spending
9 cut, and I think, if I am correct, that is the understanding
10 of the chairman as well. But secondly, I think it would be
11 very helpful to this committee if the staff could outline
12 for us exactly where we are now on the spending side. I
13 think all of us are a little bit unclear as to what additional
14 spending cuts have been made beyond what was proposed last
15 year as part of our reconciliation. So, is it possible to
16 have them not only maybe review that but to put it on paper
17 so we know exactly what we are talking about? I think that
18 was what Senator Boren was discussing.

19 The Chairman. And I suggested last time that there ought
20 to be a big blackboard over here, and we don't have it. We
21 will have it by the next meeting. Then, we can indicate
22 where we have made spending reductions and what we have
23 done and then add as we go along. I think that would be
24 very helpful. And the same on the revenue side because it
25 is a little complicated with S. 2142 on the Senator floor,

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1 where we made substantial spending reductions and tax changes
2 to keep everything in mind as we go through the present.
3 Maybe Sheila could quickly run down, and then we will get
4 the blackboard. Well, we don't have anything on it, so just
5 forget it.

6 Senator Roth. Could we also ask them to prepare a
7 memo so that we have it before us?

8 Senator Pryor. Mr. Chairman, I think this is a good
9 idea about the blackboard. Whoever is in charge of the
10 blackboard, I hope also there will be an indication as to
11 whether or not the President supports or does not support
12 each item. I think that would be a good rule of thumb for
13 us to follow.

14 The Chairman. We have done that as we have gone along,
15 and I think with one exception, the President supports
16 everything that we have done. We didn't vote on that, but
17 we will do that today. I would hope that we are not totally
18 bound just by what the President supports. If we find an
19 area to cut spending, we are going to cut it.

20 Sheila, maybe you could run down very quickly what we
21 have done in S. 2142 on the spending side, and what we have
22 done to date in the committee.

23 And I have also asked Senator Dominici if he can't do
24 it this morning, but he has indicated a willingness to come
25 to the committee and go into the questions Senator Boren

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1 raised about how much are we really cutting. So, I have
2 asked Senator Dominici if maybe he and Senator Childs might
3 come before the committee and give us a little information
4 on how they put all these numbers together.

5 Senator Long. Mr. Chairman, I was just thinking about
6 the last meeting, and it took me a while to have my own
7 thinking cleared up. It is very clear to me now that insofar
8 as we are voting for a spending cut that is already in the
9 President's budget, we are not voting to reduce the deficit.

10 The Chairman. That is right.

11 Senator Long. And therefore, I think that the burden
12 is on us to see if we are going to recommend the cuts within
13 the President's budget and if we don't recommend those, then
14 we have to raise the shortfall in addition to the amount of
15 the deficit package. in order to say that we have reduced
16 the deficit by any given amount.

17 The Chairman. That is the very point that Senator Boren
18 made -- that actually all we were doing is meeting the budget
19 request. We weren't really reducing the deficit, and that
20 disturbs him very much, and I am certain it does others on
21 the committee. Do we have-- Could we run down quickly 2142,
22 spending restraints, and then what we did last Thursday?

23 Ms. Burke. Yes, Mr. Chairman. The legislation pending
24 on the Senate floor -- S. 2062 --

25 The Chairman. Yes, 2062, excuse me.

1 Ms. Burke. Contains provisions that result in savings
2 in programs of the Finance Committee's jurisdiction of \$5.3
3 billion over a four-year period of time. Those spending
4 reductions are in the area of Medicare and Medicaid. In the
5 context of what we completed last week, I will run down
6 very quickly the items, identifying them as Administration
7 proposals and what the additional savings were in addition
8 to 2062.

9 Senator Baucus. Mr. Chairman, while we are at that
10 time, could you distinguish between Medicare and Medicaid
11 -- how much was the Medicare cut and how much was the Medicaid
12 cut?

13 Ms. Burke. Of course.

14 Senator Moynihan. May I ask, Mr. Chairman, can we sort
15 of go -- can we ask Sheila to speak to this document. I
16 mean, I can't find a 5.3 anywhere.

17 The Chairman. No, that is not in the document. That
18 is already pending on the Senate floor, but maybe if you
19 will identify those articles, Sheila.

20 Senator Moynihan. I guess that first line --
21 reconciliation of spending reductions previously agreed to?

22 The Chairman. Right.

23 Ms. Burke. That is correct, Senator Moynihan.

24 Senator Heinz. Before Sheila starts, just one
25 parliamentary question. This is going to be a part of a

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1 reconciliation package, is it not?

2 The Chairman. We hope so.

3 Senator Heinz. Now, the parliamentary rules under
4 which reconciliation is considered means that, for all
5 intents and purposes, amendments will not be in order really
6 any place except in this committee.

7 The Chairman. We hope so.

8 Senator Heinz. Isn't that --

9 Mr. DeArment. No. Germaine amendments are permitted.

10 The Chairman. Yes, germaine.

11 Mr. DeArment. So that anything can be struck out of the
12 bill, any numbers can be added, any limitations can be added.

13 The Chairman. If you strike out something, what do you
14 do on the other side? If you reduce spending by \$2 billion,
15 and you knock that out, do you have to --

16 Mr. DeArment. No, there is no requirement on that --

17 The Chairman. That you balance it?

18 Mr. DeArment. No, that you balance it.

19 Senator Heinz. We all recognize, however, that as a
20 practical matter amendments are going to pass -- if you are
21 going to have change any spending numbers, you will have to,
22 as a practical matter, replace either with additional revenue
23 or additional spending savings.

24 The Chairman. That is right.

25 Senator Heinz. The point I want to make is that, once

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1 we work our will on this bill, it is for practical purposes
2 going to be nearly impossible to amend it on the floor. As
3 you say yourself, you hope so.

4 The Chairman. I mean, there may be certain exceptions.
5 You may be talking about one of them now.

6 Senator Heinz. Perhaps. If you will recall, Senator
7 Armstrong waxed eloquent about this process about five or
8 six months ago and explained how this really forfeits for
9 the rest of the Senate their rights to offer amendments and
10 to make meaningful changes, every time we attempt to write
11 a far-reaching budget reconciliation package, inasmuch as
12 there as some very intricate and perhaps far-reaching
13 proposals before us. And I am not just talking on the
14 spending side. I am talking on the tax side. Many proposals
15 on which we have not held hearings. There is a set of
16 proposals labeled "Accounting Abuses," some of which may
17 just be accounting practices that the Administration doesn't
18 like. I think we should be very careful, Mr. Chairman, about
19 what we are doing, given the reality that there is not a
20 second chance once you get out of committee. Any mistakes
21 we make are going to be visited on the Senate as a whole.

22 The Chairman. That is why I suggested earlier this
23 morning that we agree to those that we can agree on, and
24 where we have a difference, that they be set aside because
25 everything we have done so far is tentative, and obviously

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1 we are going to be here all this week and all next week. So,
2 there is still plenty of opportunity to reopen anything that
3 may have been done.

4 Senator Heinz. Thank you, Mr. Chairman.

5 Senator Bradley. Mr. Chairman, I am not sure any of
6 us is exactly clear on where we are in the budget process.
7 Are we saying that what we are proposing here will be added
8 to the reconciliation of last year? If that is the case,
9 what are we going to do with respect to the new budget?
10 Under the procedures we will be forced to write a letter
11 in the near future outlining what we intend to do with
12 respect to both taxes and spending. So, I guess this goes
13 back to one of my basic concerns. It may be that this is
14 the appropriate way to act, but we do have a whole new
15 budget process beginning to take place. Almost
16 simultaneously at the same time, we are saying we are going
17 to make certain spending and tax changes with respect to
18 last year's reconciliation. I just wonder what the chairman's
19 proposal is with respect to the new budget.

20 The Chairman. What I hope we might do if we can find
21 agreement is just to write the Budget Committee, Senator
22 Long and myself, and say we have already agreed to do the
23 following, and they can insert that in their budget
24 resolution. We have another factor involved, and that is
25 that last November 18 the committee asked us to come back

1 with some options which would save \$150 billion. That now
2 has shrunk to about \$100 billion, and we also have a portion
3 of that already reported to the Senate floor. But it seems
4 to me that we shouldn't wait on the record budget process.
5 We will be here until July if we do that. By own view is
6 that we have demonstrated -- last week -- that this committee
7 is willing to take the lead in putting together a package
8 of spending restraints and tax changes and hopefully other
9 committees will follow suit. And I might add that one reason
10 we need to move quickly is to save the \$7 billion that your
11 committee reported, you know, in the Cola changes last year.

12 As I understand it, if we don't do something by the
13 1st of April, we lose that \$7 billion in savings reduction.

14 Senator Roth. And that, of course, is already reported
15 to the floor and can be added upon.

16 The Chairman. Right.

17 Senator Roth. If I understand what the chairman is
18 saying, in a sense what we are doing now, both with respect
19 to spending and taxes, it would be what we would report for
20 the new budget. So, we would not be facing a new --

21 The Chairman. My view is we pass out this tax bill
22 with all the additions that I am certain will be offered,
23 and that will be enough for this year.

24 Senator Roth. Thank you, Mr. Chairman.

25 The Chairman. And I note that the governors have been

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1 town again and are saying we ought to reduce deficits, but
2 I haven't noticed any of the governors coming before this
3 committee saying we ought to reduce the matching in any of
4 their programs. That is one thing that is hanging up child
5 support enforcement. They insist on 70 percent, so I would
6 hope when they scold us for the deficit that they might be
7 willing to absorb a little more of some of the programs.

8 Senator Bradley. Mr. Chairman, do you intend to make
9 child support enforcement a part of any package that we move
10 out of the committee?

11 The Chairman. We would like to.

12 Senator Moynihan. Yes, sure.

13 The Chairman. Everything but the kitchen sink, and
14 maybe the kitchen sink. Now, Sheila, did you answer Senator
15 Baucus? He asked for a breakdown of which was Medicaid and
16 Medicare in that first \$5.2 billion.

17 Ms. Burke. In the proposals that were agreed to by
18 the committee last fall, approximately \$2.8 billion were
19 the result of changes in the Medicare program. Approximately
20 \$2--excuse me. Approximately \$500 million in the AFDC
21 program. Approximately \$43 million in the SSI program.
22 There was an increase of \$161 million in the maternal and
23 child health program, and \$136 million with respect to the
24 Medicaid program. And that is over a --

25 Senator Bradley. And that is a cut?

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1 Ms. Burke.. That is correct. In Medicaid, there was
2 a reduction of \$136 million.

3 Senator Bradley. Thank you. And maternal child health
4 was increased?

5 Senator Baucus. Thank you.

6 Ms. Burke. That is correct.

7 The Chairman. Okay. Now, if you want to recap very
8 quickly what we did last week, and then move into what we
9 will do very quickly this morning. Very quickly.

10 Ms. Burke. Mr. Chairman, before the committee is a copy
11 of the document distributed last week, dated February 23,
12 the Down Payment Budget Plan. On the second page of that
13 document is the beginning of the spending reduction items.
14 I will quickly run down those items which were agreed to
15 last year--last week. I might also note that the savings
16 that are reflected next to each proposal are additional
17 savings to those achieved in S. 2062.

18 Item number one under Medicare, we have --

19 Senator Roth. You say savings? What is the baseline
20 that we are using?

21 Ms. Burke. Current law. These savings are in addition
22 to those savings achieved in S. 2062.

23 Senator Roth. Current law plus the changes made?

24 Ms. Burke. Yes, sir.

25 Senator Roth. Thank you.

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1 Ms. Burke. Item number one under beneficiary options,
2 the committee agreed to increase the Part B premium. This
3 is a proposal that was supported by the Administration and
4 is a modification of a proposal in S. 2062. Item number two
5 was an Administration proposal, and was agreed to last week.
6 Item number three was supported by the Administration and
7 was agreed to last week. Item number four --

8 Senator Long. Might I know what those options are -- I
9 mean, what those items are?

10 Ms. Burke. Yes, sir. Item number two is the delay in
11 the initial eligibility.

12 Senator Long. Okay.

13 Ms. Burke. Item number three was a modification of
14 the working age of provision. Turning to page --

15 Senator Bradley. If you could, Sheila, item number one,
16 the Part B premium -- that raised over a five-year period
17 almost \$10 billion. Is that it? Or over current law it
18 raised \$11 billion? Is that right?

19 Ms. Burke. No, sir. Over a four-year period of time,
20 it was \$3.1 in addition to the \$359 million assumed in S.
21 2062, so it is approximately \$3.4.

22 Senator Bradley. What is the current law proposal
23 then? What does that mean? It says current law on the first
24 line, and the second line says proposal.

25 Ms. Burke. I am sorry, Mr. Bradley. I am not aware of

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1 the document you are referring to. I am following the
2 document provided to the committee last week, and it should
3 be before you. It is dated February 23.

4 Senator Bradley. On the explanation of that in the
5 same document, it has listed for each year for the next five
6 years current law and then what the proposal number is.

7 Ms. Burke. Yes, sir.

8 Senator Bradley. And my question to you was does that
9 mean by 1988 that this will have achieved a reduction of
10 approximately \$11 billion \$300 million?

11 Ms. Burke. No, sir. The numbers that you are referring
12 to reflect the monthly premiums paid by the individual.

13 Senator Bradley. Oh, I see. Thanks.

14 Senator Heinz. Mr. Chairman, on that. Sheila, under
15 that proposal, the premium increases consistently all the
16 way up to 1990. How much will the premium be in 1990 for
17 a retired couple versus what it is under current law?

18 Ms. Burke. Under current law, the average retired
19 couple would spend approximately \$41.60 per month for
20 premiums.

21 Senator Heinz. In what year?

22 Ms. Burke. In 1990.

23 Senator Heinz. And under this proposal, how much would
24 it amount to?

25 Ms. Burke. I am just double checking. We had had

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1 numbers through 1988.

2 The Chairman. Maybe we can furnish those numbers.
3 Let's try to move on if we can. It is now 10:40, and we
4 haven't done anything.

5 Senator Heinz. Mr. Chairman, I would like those numbers
6 because I want to check my own. According to the figures I
7 have, the monthly premium for a couple will rise under
8 current law, as Sheila said, to \$41.60. Under the changed
9 proposal, it will rise to \$84.60 per month, or \$43.00 per
10 month increase, or about a \$516.00 per year increase in
11 this one element, by 1990.

12 Ms. Burke. I will have to double check those.

13 The Chairman. Let's check those figures. And be
14 certain to get them to Senator Heinz.

15 Ms. Burke. Yes, sir. As I indicated under item two
16 on the description, this was an Administration proposal
17 and was agreed to last week. Item number three --

18 Senator Chafee. Sheila, I want to spend a little time
19 further on that.

20 Ms. Burke. Yes, sir. And in fact, the Administration
21 has provided to us today some suggestions which we will
22 examine in terms of options for coverage. Item number three
23 was a proposal supported by the Administration and that was
24 to modify the coverage of the working ages. Item number
25 four was an Administration proposal that was modified. It is

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1 also a modification of S. 2062 and that had to do with
2 coverage with respect to physicians' fees. That item was
3 agreed to.

4 Senator Grassley. Mr. Chairman, at this point, could
5 I raise a question? It is my understanding that the
6 Administration proposal would have had a \$600 million savings
7 in fiscal year 1985, with a five-year savings of \$4.5 billion
8 and now we are going with a savings that only adds up to
9 \$1.7 billion for the four years. Is that --

10 Ms. Burke. Mr. Grassley, the proposal that was made
11 by the Administration had a four-year savings of approximately
12 \$2.5 billion. The proposal before you and agreed to by the
13 committee is in addition to those savings achieved in S.
14 2062 and the total of that would be the \$1.7 billion
15 achieved in addition to approximately \$1.6 billion.

16 Senator Grassley. Okay. So, what we have on the page
17 in front of us is savings in addition to what the President
18 had --

19 Ms. Burke. That is correct. In addition to what --

20 The number that you see before you is in addition to
21 the savings achieved in S. 2062, and is greater than the
22 Administration's proposal. The Administration's proposal
23 over a four-year period of time achieves \$2.5 billion. This
24 proposal would achieve approximately \$3.4 billion.

25 The Chairman. All right.

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1 Ms. Burke. The first item under hospital options was
2 one that was set aside by the committee last week. The
3 second item dealing with the lab fees was supported by the
4 Administration and is the modification of a proposal in S.
5 2062 and was agreed to. The first under Medicaid dealing
6 with the extension of the Federal reduction was an
7 Administration proposal modified and was agreed to, and the
8 second item -- the assignment of rights -- was also an
9 Administration proposal and was agreed to.

10 Senator Bentsen. Sheila, let me ask you a question
11 on one of the fees, and that is on the physicians' options.
12 Doesn't the provision that we are looking at here give a
13 further option to physicians than what was found in the House
14 proposal?

15 Ms. Burke. That is correct.

16 Senator Bentsen. Doesn't that proposal mandate their
17 participation?

18 Ms. Burke. Yes, sir. With respect to in-patient
19 services, it would require assignment. This proposal does
20 not require assignment.

21 Senator Bentsen. But if you don't take it, then you
22 have the other situation of a two-year freeze.

23 Ms. Burke. That is correct.

24 The Chairman. What we are trying to do -- and I know
25 the AMA has objected to what we did -- what we are trying to

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1 do is to avoid cost-shifting. You freeze it, and then they
2 just shift the cost to the patient. So, what we have tried
3 to do is back away and look at it, and we came up with what
4 we thought would be a better method to the patient and not
5 be a mandatory assignment program.

6 Senator Bentsen. As compared to the House actually, it
7 gives further options.

8 The Chairman. That is right. But we don't think it is
9 unreasonable. I guess the AMA does, and I intend to meet
10 later with Mr. Sammonds.

11 Senator Grassley. Mr. Chairman, could I ask the staff,
12 in their view, how would mandatory assignment shift the cost?

13 The Chairman. Mandatory assignment would not shift the
14 cost.

15 Ms. Burke. That is correct. Mandatory assignment
16 would require physicians to accept what Medicaid paid.

17 The Chairman. If we just froze it without anything,
18 there is a question of shifting costs.

19 Senator Grassley. Yes. I understand. I thought Senator
20 Bentsen asked the question how was this bill different than
21 the House, and essentially, as I heard the answer, the House
22 said mandatory assignment and we said let's try to provide
23 some incentives to avoid that without making it mandatory.

24 Ms. Burke. Yes, sir. That is correct.

25 Senator Bradley. Mr. Chairman, I asked for an

1 explanation, which I got, between the Administration's
2 proposal and what we ended up doing. Could I ask staff to
3 tell me then what is the difference in savings between what
4 we agreed to in this committee and what the AMA is suggesting?

5 Ms. Burke. As we understand it, Senator Grassley, the
6 American Medical Association has requested of their members
7 and of all physicians to voluntarily freeze their fees for
8 one year, this period of time. They do not have an
9 addition to that -- any suggestion with respect to
10 incentives for assignment, but the effect of their suggestion
11 is hopefully to discourage physicians from passing on any
12 additional costs and to hold their rates down.

13 Senator Grassley. Okay, but my question is ours versus
14 theirs -- which one saves the most money?

15 The Chairman. Ours.

16 Ms. Burke. Ours.

17 Senator Grassley. Okay. By how much?

18 The Chairman. Double.

19 Ms. Burke. Approximately double. Ours is in excess of
20 two years of freeze.

21 The Chairman. But we are trying to work out any
22 problems they may have. I might say, in some of these areas,
23 I think Sheila was telling me yesterday, that as high as
24 90 percent of the physicians agreed to the voluntary freeze.
25 In other words, they have agreed not to pass on the costs,

1 not to raise fees. In fact, I think if that is an indication
2 of their willingness to cooperate, we don't want to make it
3 more complicated for them. Senator Pryor?

4 Senator Pryor. It is my understanding also, Sheila, if
5 I am not incorrect, that the association not only requested
6 not to increase fees on Medicare issues but also across the
7 board.

8 Ms. Burke. Yes, sir. That is correct.

9 Senator Pryor. These for a period of 12 months?

10 Ms. Burke. Yes, sir.

11 The Chairman. Now, let's move on to the new material.
12 Then, maybe tomorrow we can have all this in writing, so
13 we don't have to go back over this again.

14 Ms. Burke. Mr. Chairman, the committee has before it
15 a new piece of paper that describes an alternative with
16 respect to hospital reimbursement, entitled "Limit Increase
17 in Hospital Costs per Case." It is a single sheet.

18 The Chairman. That is this sheet?

19 Ms. Burke. Yes, sir. A single sheet identified as
20 "Limit Increase in Hospital Costs per Case." If the committee
21 will recall, the description last week very briefly, Medicare
22 provides for an increase in hospital costs on a case basis
23 by a market basket which is about 6 percent per year plus
24 1 percent. The 1 percent is applied to the portion of the
25 hospital's costs under the old system which is the cost base

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1 system and 1 percent on the new DRG system. Again, if the
2 committee will recall, there is a three-year blending that
3 takes place to move us towards a single payment system under
4 DRGs over a three-year period of time. During that time,
5 each piece of the hospital's reimbursement is updated
6 annually to reflect changes in prices. The proposal that
7 the committee had before it last week would have removed
8 that 1 percent and would have simply provided for an increased
9 base solely on the market basket, that is the cost of goods
10 and services that institutions purchase.

11 The alternative proposal which is before you today -- and
12 both proposals are actually described -- the first would
13 simply be to remove the 1 percent entirely from hospital
14 costs. That would have a four-year savings of \$2.3 billion.
15 The alternative proposal would be to remove that 1 percent
16 inflation factor from only that portion of the hospital's
17 costs that are under the old system. That is, under the
18 cost base system. That is, as you recall, phased out over
19 three years. That savings over a four-year period of time
20 is \$1.1 billion.

21 The Chairman. Then, you have another idea how to pick
22 up about half of that. Is that correct?

23 Ms. Burke. There was another proposal that we were
24 asked to examine, and that is one that has been recommended
25 by the Congressional Budget Office, having to do with

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1 disallowing the revaluation of hospital assets when they
2 are purchased. This is based on a recommendation from CBO
3 based in part on work done by the General Accounting Office,
4 and it has to do with the purchase of institutions between
5 institutions and what happens with the reevaluation of that
6 asset for purposes of Medicare's reimbursement. We are
7 talking with the Department in OMB about the specifics of
8 that proposal. The cost savings that we have attributed to
9 it are \$330 million over a four-year period of time.

10 The Chairman. Is there any objection to the first
11 proposal? As I understand, the concern was that we shouldn't
12 start meddling with the DRG system.

13 Ms. Burke. Yes, sir.

14 The Chairman. When it only started in October, and we
15 tell these people in one breath we are market basket plus
16 one -- let's make it work -- and then we change the rules
17 six months later. So, what we have done is to modify that,
18 as I understand it, to eliminate that problem.

19 Ms. Burke. That is correct, Senator. This would only
20 affect the portion of the hospital's cost under the old
21 system -- not the DRG.

22 The Chairman. What was the justification for that
23 market basket plus one as far as those costs were concerned?

24 Ms. Burke. Traditionally, Medicare has paid market
25 basket plus an inflation factor to reflect those changes in

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1 technology that are not necessarily represented in the market
2 basket itself. In fact, it is a fudge factor in terms of
3 the costs that hospitals have to face.

4 The Chairman. But inflation is down, isn't it?

5 Ms. Burke. Inflation is down. The market basket is
6 projected to be about 6 percent, which is lower than it has
7 been in the past.

8 Senator Bentsen. Mr. Chairman, could I get the
9 Administration's position on this modified proposal?

10 The Chairman. Who is here from HHS? Has the
11 Administration has a chance to look at this modified proposal?

12 Ms. Kelly. Yes, Senator, we have. We have reviewed it,
13 and we do not oppose it at this time. We are concerned about,
14 as I indicated before, the amount of money we would be taking
15 out of the hospitals in this proposal, but in the spirit of
16 the budget reconciliation and the budget reduction that this
17 committee is trying to do, we do not oppose this proposal.

18 Senator Bentsen. You do not oppose it. Do you support
19 it?

20 Ms. Kelly. No, Senator, we don't support it. We are
21 not opposing it.

22 The Chairman. I wonder if you would identify yourselves
23 for the record?

24 Ms. Kelly. My name is Carol Kelly. I am Director of
25 the Office of Legislation and Policy with the Health Care

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1 Financing Administration.

2 Mr. Schieber. I am George Schieber, the Director of
3 the Office of Policy and Analysis in the Health Care
4 Financing Administration.

5 The Chairman. Is there a distinction between
6 nonopposition and the support? I don't want to complicate
7 your life, but we need to save --

8 Ms. Kelly. What I am saying, Senator, is that if the
9 committee chooses to adopt this proposal, certainly the
10 Administration is not in opposition to it, but we are not
11 supporting it.

12 Mr. Brockway. Mr. Chairman, isn't the difference
13 fingerprints?

14 The Chairman. I guess. It would be ours instead of
15 theirs.

16 Senator Chafee. Mr. Chairman?

17 The Chairman. Senator Chafee?

18 Senator Chafee. Mr. Chairman, I am not sure that I
19 am sympathetic with this proposal. I take it that what you
20 are suggesting -- or what is being suggested here -- is that
21 we drop to the so-called revised proposal. Is that it?
22 That produces 1.1 instead of 2.3. Is that correct?

23 The Chairman. That is correct.

24 Senator Chafee. Why are we doing that? We are freezing
25 the physicians, we are increasing the Part B premium for the

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1 retirees for the insured, and yet we are easing up on the
2 hospitals.

3 The Chairman. I am willing to vote either way. What
4 I want to do is cut spending. But we did implement the DRG
5 system. It became effective October 1, and there is a
6 feeling that we shouldn't revisit that in February of 1984.

7 Senator Chafee. If the theme is have some kind of
8 consistency here, instead of changing the ground rules
9 constantly, I can see that also. But in the spirit of--
10 We are hitting a whole series of people here, and I am not
11 sure that we should ease up necessarily on the providers
12 -- the hospitals. Sheila, could you address that?

13 Ms. Burke. Senator Chafee, the suggestion made by the
14 chairman is, in fact, the one reflected by the hospital
15 industry, and that is a concern with the interference in
16 the new payment system which has already, of course, reduced
17 hospital expenditures by approximately \$13 billion over a
18 period--excuse me-- approximately \$10 billion over a period
19 of time. The concern is that this is one more change in a
20 new set of rules that people are already having to learn
21 to adjust to. Their hope is that we will not interfere with
22 that while they are trying to work out those problems. They
23 understand the concern with respect to the budget, but would
24 prefer that we deal with that portion of the institution's
25 cost that is historical rather than the new system.

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1 Again, to avoid interference with the new payment model.
2 That is, in fact, the argument that they propose.

3 Senator Chafee. What do you think of the argument?

4 The Chairman. Yes. Give us the facts now, Sheila.

5 Give us the truth.

6 (Laughter)

7 Ms. Burke. There is legitimacy to their concern about
8 interference with the new payment system. There is a
9 tremendous amount of concern and I think a lot of disagreement
10 over the impact on different kinds of institutions. And I
11 think the hospitals feel that they negotiated in good faith
12 with the Congress to move to a new payment system and I
13 think they honestly feel that that should not be interfered
14 with, given the number of difficulties already with respect
15 to payment, including urban, rural, and all the other issues
16 that have been brought before the committee. So, I think
17 there is indeed some legitimacy to their argument, but,
18 alternatively, I think in the spirit of budget, they should
19 also feel the same kind of difficulties that individuals
20 will feel, as you have suggested, with the premium changes
21 and so forth.

22 The Chairman. Is there any objection to the modification
23 modification?

24 Senator Heinz. Mr. Chairman, may I just pursue Senator
25 Chafee's line of questioning, because I think it is helpful?

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1 The Chairman. Yes.

2 Senator Heinz. Sheila, you used a \$10 billion number
3 of savings. What was that related to?

4 Ms. Burke. Those were the approximate estimates of the
5 TEFRA changes, Senator Heinz.

6 Senator Heinz. Over what period of time?

7 Ms. Burke. I believe that was over approximately a
8 three-year period of time.

9 Senator Heinz. Do we know how much money we have saved
10 so far?

11 Ms. Burke. I would have to look back at what the
12 TEFRA numbers were because that would have been 1982-1983
13 in addition to the year we are in. I would have to check,
14 but I can do that and give you the information.

15 Senator Heinz. Because we just implemented the DRG
16 system partially on October 1 of this last year.

17 Ms. Burke. Yes, sir, but we are under budget
18 neutrality, as you recall. We are still working under
19 the TEFRA limits. So, we in fact put limits on two years
20 prior to that and are moving into a new system, but we are
21 not exceeding those limits that were previously established.

22 Senator Heinz. Now. Thank you. On the question of
23 good faith, does that mean that where we had been mistakenly
24 or horrendously overreimbursing for a procedure -- and I
25 have some in mind -- that even though we can document that

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1 we have been paying too much for the past 10 years, that we
2 would somehow be breaking faith with the American Hospital
3 Association if we corrected a grievously large
4 overreimbursement that the health Care Financing
5 Administration, for whatever reason, hadn't been able to
6 cope with up until now? Does good faith mean we have
7 grandfathered in all the mistakes of the last 10 or 15
8 years?

9 Ms. Burke. No, sir. I don't believe so.

10 Senator Chafee. When anybody tries to make a change in
11 the reimbursement portion that is still left to hospital
12 specifics, we are told that this is breaking faith with the
13 agreement. We are told that this is changing the rules in
14 the middle of the game.

15 The Chairman. Well, the game hasn't started yet.

16 Ms. Burke. No. I think my reference was specifically
17 with respect to the inflator. I think the reference that you
18 are making is to the catherization of individuals into
19 groupings -- diagnostic groupings. And the concern that
20 has been raised in that context is that all of the DRGs,
21 the relative weights of those DRGs, and the portions of those
22 DRGs that were established under, in fact, the New Jersey
23 system and modified is one that will, in fact, be examined
24 as we look at reweighting, as we look at reclassification.
25 I would certainly agree that changes will, in fact, have to

1 be made as we look at changes in technology that have, in
2 fact, changed, as you have suggested correctly, with respect
3 to pacemakers and other areas -- changed the relative value
4 of a procedure versus another procedure.

5 Senator Heinz. Last question. What would be the
6 argument against reducing the pacemaker procedure
7 reimbursement under Part A by 25 percent? What would be the
8 argument against that, particularly since some hospitals
9 have voluntarily reduced their reimbursement by saying we
10 are not going to take the \$7,000.00 or \$8,000.00 you offer
11 us?

12 Ms. Burke. I think the concern, and the Administration
13 has to address this also-- I think the concern was pulling
14 out one particular aspect of a DRG in the context of
15 reweighting of all of the DRGs and how much information we
16 actually had available to us to be able to do that
17 correctly. Again, I might ask Mr. Schieber, or Dr. Schieber,
18 to comment on that because of the construction of the DRGs
19 and what we know about those weights. My understanding is
20 that it is an informational issue as much as anything else,
21 but I may be incorrect.

22 Ms. Kelly. Senator, I think that within the perspective
23 payment system that certainly the implementation of the
24 system has encouraged hospitals to be prudent purchasers
25 of devices such as pacemakers. We in HCFA are keeping

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1 careful track of that information, and we can use it in the
2 context of recalibration in 1986 to make sure that we are
3 paying an appropriate amount of money for pacemakers.

4 So, I think that we are accommodating your concerns.

5 Senator Heinz. That is two and a half years away
6 though -- 1986. What is the reason for us -- if we know
7 that we are overreimbursing by a very significant amount
8 -- what is the reason for our not doing something about it
9 today as opposed to waiting for two and a half years for
10 maybe something to be done?

11 Ms. Kelly. The perspective payment system, Senator,
12 is based on the relative weights of one DRG in relation to
13 another, and as Sheila indicated, they are carefully
14 constructed, and we don't wish to put the system out of
15 whack to a certain extent that we should be paying out a
16 lower amount of money for the pacemaker DRGs.

17 Senator Heinz. But if we decided to reduce the
18 reimbursement for pacemakers under Part A by 25 percent,
19 what would you do about it? Nothing? Or would you have
20 to run it through a computer for a few minutes?

21 I really don't understand your answer. Your answer
22 says, well, it is going to cause us some kind of informational
23 problem, and I suppose anything we do causes informational
24 problems. Is that a reason not to do anything?

25 Ms. Kelly. In the context of budget neutrality, we are

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1 supposed to dedicate a certain amount of money to the
2 perspective payment system in a year. Now, if we are to
3 back it out of several particular DRGs, I don't know how
4 it is that you expect us to put that into others and pay
5 that into the system.

6 Senator Heinz. Oh, now I see what you are saying. You
7 are saying that, under the concept of budget neutrality,
8 that is not just a ceiling, it is a floor, and we are not
9 allowed to lower the floor even if we have -- or the
10 ceiling -- even if we have a good reason to do it. Now,
11 suppose we just said we are going to be consistent? We are
12 going to reduce pacemaker reimbursement, and we are going
13 to reduce the budget numbers by that much so that it is,
14 in a sense, budget neutral. We will just change the numbers.
15 What would be wrong with that?

16 The Chairman. Are we on pacemakers?

17 Senator Heinz. We are on the general principle, Mr.
18 Chairman, because I think there are some-- I need to
19 understand why we can't do anything to fix things that
20 are broke.

21 The Chairman. I might be willing to help you fix the
22 broken pacemakers.

23 Senator Heinz. Yeah, well, that is another issue.
24 Maybe we ought to register them.

25 The Chairman. That is an issue between you and Senator

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1 Durenberger.

2 Senator Heinz. I think Senator Durenberger has a
3 heightened sense of interest in this subject. I hope. But
4 this is a different issue that we are talking about. I just
5 don't understand why when we are overreimbursing for
6 something, we can't do anything about it.

7 Dr. Schieber. I think Sheila basically responded.
8 This is basically a new system, Senator. I think there are
9 a lot of things going on in there. There may be other
10 procedures that are overreimbursed. There are a lot of
11 concerns about technology changing rapidly in this area,
12 and I think, given the rather substantial effect this system
13 is going to have in this country over the next three years,
14 that our feeling is that we would like to let that play out
15 and try to adjust and redress that as well as whatever other
16 imbalances there are when we get to 1986 and recalibrate
17 the rates.

18 Senator Heinz. Mr. Chairman, I think that is an
19 interesting answer, and I won't comment on it further except
20 that it makes no sense.

21 Senator Bentsen. Sheila, when you talk about this
22 limitation on DRGs as to the market basket rate -- the
23 further limitation -- what types of hospitals would find
24 this the most burdensome?

25 Ms. Burke. Senator Bentsen. We don't think there is a

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1 differential difference between institutions. We think it
2 will play out evenly across all institutions. At least, that
3 is the information that we have from the Administration
4 -- that it will not differentially affect one institution.

5 Senator Bentsen. You don't see as far as hospitals or
6 -- treatment or --

7 Ms. Burke. I think logic would suggest that, though
8 that may be on the average, I think that logic would suggest
9 that those institutions that are more intensive and have a
10 higher percentage of technology might, in fact, be
11 disadvantaged more than institutions that are community-based
12 and not as intensive, but one also has to look at the doubling
13 of the teaching adjustment which is contained in the provision
14 currently in current law, which accommodates some of the
15 teaching institutions concerned.

16 Senator Bentsen. That is a good point. Now, how about
17 rural hospitals that have a very substantial dependence on
18 Medicare payments -- 70 percent or more?

19 Ms. Burke. Certainly any change in that aspect -- if
20 they are, in fact, 70 percent Medicare -- any single change
21 could make a lot of difference to them. This is a 1 percent
22 reduction in what they would otherwise receive on average,
23 so, yes, it certainly could to the extent that they are a
24 large Medicare.

25 Senator Bentsen. Thank you very much.

1 The Chairman. I wonder if we might go ahead and
2 approve B, unless somebody wants to vote on A. We are doing
3 all this on a tentative basis, in any event. If there is
4 some other way we can modify this to save more revenue
5 without infringing on the program, we should do it. Is
6 there any objection to adoption of B?

7 Senator Heinz. Mr. Chairman, would it be in order to
8 offer an amendment to what we have here that would be
9 revenue-neutral? Or do you want to do that another time?

10 The Chairman. I think if it deals with DRG --

11 Senator Heinz. It would affect many of the things we
12 have talked about so far.

13 The Chairman. Why don't we go ahead and adopt this if
14 we can, and then you can offer the amendment. What I would
15 like to do is go through the others we have pending that we
16 want to suggest, and then come back to committee members.

17 Senator Heinz. If my feeling about the adoption of
18 this package is premised on how we are going to amend it,
19 I don't know that that procedure is terribly --

20 The Chairman. If it deals with this specific issue,
21 then it probably should be offered now.

22 Senator Heinz. All right. Let me-- Sheila, did you
23 have a chance to work out that number on the Part B premium
24 yet?

25 Ms. Burke. Yes, sir. Your estimates are correct.

1 Senator Heinz. So, the Part B premium will --

2 Ms. Burke. Would double.

3 Senator Heinz. Would double. It would be \$43.00 a
4 month higher than current law in 1990?

5 Ms. Burke. That is correct.

6 Senator Heinz. \$43.00 a month.

7 Ms. Burke. For a couple. That is correct.

8 Senator Heinz. For a couple. Senator Durenberger
9 asked what does it have to do with hospital-based DRGs.
10 Mr. Chairman, here is what it has to do with it. What I
11 would like to do, in order to be revenue-neutral, is offer
12 an amendment that kind of cuts across several of these
13 provisions. What we would do is we would limit reimbursement
14 under Part B of Medicare for pacemaker services, that we
15 would reduce that by 25 percent. We would reduce
16 reimbursement for clinical labs, both in-hospital and free
17 standing, from 62 to 60 percent. And we would limit Medicare
18 reimbursement for revaluation of hospital assets under
19 Medicare -- the CBO proposal. As I add those proposal
20 items up, they come to \$1.4 billion in savings over four
21 years, and I would propose that we reduce the premium
22 increase under Part B that is scheduled by that amount,
23 so that we reduce the amount of premium increase -- we are
24 still going to have some above the current law -- but we
25 would hold back on costs and the amendment would be

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1 revenue-neutral.

2 The Chairman. I would rule that that doesn't deal with
3 this amendment. Let's go ahead and vote on this amendment.
4 If you want to reopen Part B premium, we can do that after
5 we have gone through all the other things.

6 Senator Heinz. All right.

7 The Chairman. Anybody want to vote on this, or are
8 we willing to accept B, without objection?

9 Senator Durenberger. I am going to object to it. Oh,
10 you are on B -- I am sorry.

11 The Chairman. Yes.

12 Senator Durenberger. I may enrich it for you a little
13 later on, I hope.

14 The Chairman. We would like to because I think that
15 would help Senator Heinz's problem. I think some of these
16 things we may want to revisit. All right. Then, let's
17 move onto the rum. Are we ready for rum?

18 Senator Baucus. Mr. Chairman, before we get to rum,
19 I think it is important for us to understand where we are,
20 at least as I see it. As I understand it, our efforts are
21 basically to cut deficits by \$100 billion. And there are
22 many of us who feel that it should be cut by more -- say,
23 \$200 billion over the three-year period. Medicare constitutes
24 7.4 percent of outlays. That was this year, and it will
25 probably rise to close to 8 percent of outlays by 1987,

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1 the third year of this three-year period. We have already
2 cut last week \$7.4 billion from Medicare which would amount
3 to Medicare's proportional share, assuming a \$200 billion
4 deficit reduction. If we assume a \$100 billion deficit
5 reduction, then we have already cut -- last week -- Medicare
6 by twice as much as Medicare's proportionate share, if we
7 want to go that way. If you add in reconciliation -- last
8 year 2.8 -- plus Part B of the two options, hospital DRG
9 reductions, that means we will be cutting Medicare \$11.4
10 billion, which would be about 50 percent above Medicare's
11 proportionate reduction, assuming a \$200 billion deficit
12 reduction, then it would be two or three times Medicare's
13 proportionate reduction, assuming a \$100 billion deficit
14 reduction. So, I suggest that, frankly, we are cutting
15 Medicare way beyond its fair share compared with other
16 programs. The defense budget is about 28 percent of outlays.
17 We should therefore cut defense \$28 billion, assuming a
18 \$200 billion total deficit.

19 The Chairman. I think it ought to be cut more than
20 that.

21 Senator Baucus. All I am saying is that what we are
22 doing thus far is way beyond Medicare's proportionate share.
23 So, I suggest that a lot of this can be modified when we
24 get to that perhaps a little later on today or in the next
25 couple of days. Perhaps the \$1.1 billion reduction with

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1 respect to hospitals can be taken out of or can replace some
2 other beneficiary cut that we made last week. Perhaps the
3 increase in the Part B premium. It can be reduced in some
4 way, so that Medicare is paying its share but no more than
5 its proportionate share. So, I just think all of us should
6 be aware that we are going way beyond Medicare's
7 proportionate share, and it really isn't fair to beneficiaries
8 because we are taking it out of the beneficiaries' hides
9 much more than we are others.

10 I just think basically, before we go too far down that
11 road, we should realize what we are doing because I suggest
12 that probably we are not going to do it when push comes to
13 shove later on, if the other programs aren't taking their
14 fair share, too.

15 The Chairman. Right. I will be willing to take any
16 other amendments you have to cut spending. You know, if
17 you have got some amendments --

18 Senator Baucus. I will have amendments later on.

19 The Chairman. Well, you can't have it both ways. You
20 can't make those great speeches about deficit reductions,
21 and then say we don't want to cut anything.

22 Senator Baucus. But I am saying that-- Remember last
23 year, Mr. Chairman, one of the hallmarks -- and you said it
24 many times yourself -- is evenhandedness, fairness. Every
25 program take its fair share. I am following up on that.

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1 I am just saying so far, right now, one program is
2 taking way, way more than its fair share, and I wonder if
3 that is fair.

4 The Chairman. Except that we are looking at the
5 hospitals. We have gotten over \$3 billion from physicians
6 who have the freeze. This is about \$1.1 billion in the
7 hospital area. There is more coming, and about \$3 billion
8 in beneficiaries. So, we have tried to look at all three
9 of the problems in Medicare, plus, I think, we have suggested
10 that that money go into the HI trust fund. Correct?

11 Ms. Burke. That is correct.

12 The Chairman. Obviously, if we can find another spending
13 reduction and ease the pain some other place, it is fine
14 with me, but I hope we do more instead of less.

15 Senator Baucus. I understand, Mr. Chairman, but I
16 cannot support a program that cuts Medicare say two or
17 three times beyond its fair share when other programs
18 aren't being cut.

19 Senator Durenberger. Then, you have got to get into
20 what is fair share, and you have really got to go with
21 growth and reduction in growth, and this committee over the
22 last three years has put about 51 or 52 percent of the
23 reductions in Medicare on hospital and about 15 percent on
24 doctors and we are going to up that in this process. Only
25 about 20 percent has been shared by beneficiaries in a

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1 system that isn't in any way based on need. So, I think you
2 have to put what we are doing this year in perspective of
3 what we have done over the last four years. And I would
4 suggest that we have been fairly evenhanded.

5 Senator Baucus. There are two questions here. One
6 question is what should Medicare as a total, including
7 doctors, hospitals and beneficiaries, be cut? That is one
8 separate matter. How much should Medicare be cut compared
9 with other programs? That is one question. The second
10 question is within the Medicare cut, what should the
11 appropriate allocation be among hospitals, physicians,
12 and beneficiaries?

13 Senator Durenberger. And we have moved a whole lot
14 more into Medicare over the last four years than we moved
15 into AFDC and a whole lot of other needs-based systems in
16 this committee.

17 The Chairman. And I think it might be helpful to
18 address that -- just maybe sort of put together a memo on
19 the last three years where we have had reductions, where
20 they have fallen within Medicare. Let's move on to the one
21 that I had hoped we might approve. I hoped we might approve
22 the next item, and have HHS look at it after we have
23 approved it. That is the \$330 million. I think we need to
24 address that.

25 Ms. Burke. The revaluation of assets? That was also a

1 portion of Senator Heinz' amendment, as I understand it.
2 That is, to look at the CBO proposal with respect to
3 revaluation of assets, hospital assets, during purchase.
4 And that would, in effect, alter the way Medicare reimburses
5 institutions. There is a description, which we will prepare
6 for you, in talking with the Department about the way
7 Medicare currently pays for assets, through their depreciation
8 payments. Medicare, of course, does not follow ACRS, but
9 uses a straight-line schedule, and it has been suggested
10 by CBO that institutions when they change hands, up their
11 assets -- their asset value -- and in fact, Medicare pays
12 a higher amount on depreciation and interest than perhaps
13 it might otherwise need to.

14 The Chairman. Has the Department had a chance to look
15 at that?

16 Ms. Kelly. The CBO report, you mean, Senator?

17 The Chairman. Yes.

18 Ms. Kelly. Yes. I believe that this committee has a
19 hearing in a few weeks on capital as does the Ways and Means
20 Committee, near the end of March. We have not taken a formal
21 position on this particular amendment. We are studying,
22 however, capital in the context of the perspective payment
23 system and have a report due to the Congress in October.

24 The Chairman. October?

25 Ms. Kelly. Yes.

1 The Chairman. This is February.

2 Ms. Kelly. Yes, Senator, you are right.

3 The Chairman. We may not need a report. Maybe we will
4 act on it. Anyway, let's get that put together so we can
5 look at it tomorrow. And let's move to the rum section.
6 Who is in charge of rum?

7 Mr. Belas. Mr. Chairman, the primary impetus which has
8 caused the introduction of bills both on the Senate side by
9 Senator Long and on the House side is a process called
10 redistillation, where distillers are --

11 The Chairman. We have been over all of that. Let's get
12 down to the nitty gritty.

13 Mr. Belas. The staff suggests looking at a redefinition
14 of the products -- the alcoholic products -- that would
15 qualify for the so-called cover-over, the rebase, of the
16 excise tax to include rum only and therefore deny the cover
17 over for the redistilled spirits, the grain spirits, that
18 have been coming from the United States, and also for
19 cane neutral spirits which are indistinguishable from grain
20 neutral spirits -- vodka, use in vodka, and cordial markets
21 -- that are also produced in the United States. And if
22 allowed to continue without the restriction would probably
23 take the place of the redistilled spirits as a vehicle for
24 the cover-over to --

25 The Chairman. Now, what is the issue? I don't

1 understand all that stuff, but what is the problem?

2 Mr. Belas. The problem is that the amounts -- the
3 costs -- of the distilled spirits is a small fraction, about
4 one-tenth, of the amounts of the excise tax, and so it
5 therefore pays the Virgin Islands and Puerto Rico to
6 subsidize the production of these distilled spirits to get
7 the excise tax rebate. The suggestion would be to stop the
8 redistilled spirits and the use of the rebate for cane
9 neutral spirits at the end of June 1984.

10 Senator Long. Could I just ask one question? How much
11 does it cost to redistill this alcohol? How much does that
12 cost?

13 Mr. Belas. The marginal cost is next to nothing. The
14 transportation cost is about \$1.50 to \$2.00, and the actual
15 cost of the redistillation is a small fraction of that.
16 What we have been told --

17 Senator Long. Can you give us an idea of what the
18 actual cost -- now, you are talking about redistilling --
19 it has already been distilled, right? It is ready to be
20 consumed the way it is, and you bring it down there, and
21 then you redistill it. Now, what does it cost to redistill
22 the stuff?

23 Mr. Belas. We are told that it is approximately 30
24 cents per gallon.

25 Senator Long. All right. So, it is about 30 cents.

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1 Now, what is the transportation cost to haul it down
2 to Puerto Rico and back?

3 Mr. Belas. We are told that it is about 81 cents, or
4 about 80 cents, 85 cents.

5 Senator Long. 85 cents? So, you have got this
6 situation. My understanding is that it costs about 88 cents
7 to make a gallon of this beverage. Right?

8 Mr. Belas. Yes.

9 Senator Long. All right. So, 88 cents is the cost
10 of manufacture. Now, the tax is \$10.50. Is that right?

11 Mr. Belas. That is correct.

12 Senator Long. All right. That is a Federal tax of
13 \$10.50. Now, if you take the 30 cents, which you assume
14 to be the cost of the redistillation, that is really a
15 service -- 30 cents. All right? 85 cents transportation.
16 All right? So, that is a total of \$1.15 and for that
17 somebody makes \$10.50 out of our Treasury. So, that is
18 saying a profit of \$9.35 at Uncle Sam's expense for carrying
19 out a totally unnecessary operation, which costs \$1.15.
20 Right?

21 Mr. Belas. Even the Puerto Rican Government would say
22 that the net gain is about \$8.50 to \$9.00 per gallon.

23 Senator Long. Now, if we are going to continue, I want
24 in that business. Here you are providing a totally
25 unnecessary service for \$1.15, and your net profit is \$9.35.

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1 So you provide an unnecessary service for \$1.15 and your
2 profit is \$9.35. Now, how much are the people being paid
3 who participate in this -- let's say the distillers or
4 redistillers, or whatever -- the people who do the
5 redistilling and the rest of it?

6 Mr. Belas. We understand that in Puerto Rico the
7 Government provides an incentive payment of about 50 cents
8 to the Puerto Rican distillery, and that of course is shared
9 between the Puerto Rican distillery and the American shipper
10 distiller.

11 Senator Long. All right, there is a 50 cents profit in
12 there for them. Now, mind you, that doesn't sound like much
13 when you compare that to what Uncle Sam is losing, but
14 people tell me in this business it is a very competitive
15 business, with a cost of about 88 cents a gallon. I have
16 been told by Louisiana people who are in the business of
17 manufacturing alcoholic beverages that there is a small
18 profit in there, and if they have got to compete with
19 somebody who is being subsidized 50 cents a gallon, the
20 overall cost is 88 cents, that they can't compete. They
21 can't stay alive for a year trying to compete with somebody
22 who is being subsidized 50 cents a gallon for doing this
23 when their cost is 88 cents, and I assume that would be the
24 case of all American distillers. Is it not?

25 Mr. Belas. Certainly.

1 Senator Long. This is a very competitive business.
2 So, nobody up here can compete with that. And the Government
3 takes a tremendous loss in all this. For every gallon that
4 you move back and forth into Puerto Rico that way, the
5 Government loses \$10.50. So, the Government down there can
6 make \$9.00 every time they move a gallon in and out.

7 Mr. Belas. The Puerto Rican Government has budgeted
8 \$130 million from the redistillation process for their
9 fiscal year ending this June 30, and are estimating that
10 they will budget for next year \$214 million.

11 Senator Long. If this is to be permitted, why shouldn't
12 they do all of it? Just provide us all of our spirits here
13 in the United States by this process. Who in the hell could
14 compete with it? Hold on just a minute, I want to ask this.
15 What is the potential loss to the Treasury if you let them
16 do it all that way?

17 Mr. Belas. I am not sure, Senator. We would have to
18 check with --

19 Senator Long. Who knows here for Treasury?

20 Mr. Brockway. There is approximately \$4 billion a year
21 in distilled spirits taxes made.

22 Senator Long. So, it is a potential loss of \$4 billion
23 to the U.S. Treasury if you let them do it all that way.

24 The Chairman. Senator Moynihan.

25 Senator Moynihan. Mr. Chairman, thank you. You were

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1 courteous enough to ask Governor Merrill and, of course,
2 Representative Carada to come up and be with us as they are
3 and we welcome them to the committee. Mr. Chairman, I can't
4 speak for them, but I can make a general proposal, and Mr.
5 Chapoton and I have talked about this. There are two things
6 that I think that the committee would want to know.

7 The first is that the Government of Puerto Rico, finding
8 itself very much impacted by the reduction in programs such
9 as CETA and foods stamps, I mean, they have had a very hard
10 time in the last three years -- are looking for new sources
11 of revenue and employment. They asked the Treasury Department
12 -- I think Mr. Chapoton will confirm -- whether this would
13 be an acceptable practice and received from the Treasury
14 Department, in writing, a statement that yes it would.
15 And they proceeded to get it under way. Now, they come here,
16 Mr. Chairman, to say that if this is something that the
17 committee doesn't think is possible, acceptable -- and
18 Treasury has had second thoughts about -- they are willing
19 to put an end to the practice. What they would like to do,
20 however, is what you would expect them to do. They are not
21 here saying we have our letter. This is our right. They
22 are saying that if the committee feels it should be changed,
23 we can stop it, not for cane spirits but for imported spirits.
24 They would ask this: their fiscal year begins July 1, as
25 ours used to do. So, their budget is already put together.

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1 And the revenues -- I believe \$214 million -- represent 10
2 percent of their budget. Now, what they would like to ask
3 Mr. Chairman is can they continue the practice for fiscal
4 year 1985, which begins in July, and then phase it out over
5 the next five years and be done. At 20 percent for five
6 years, or would it be four years? I guess it would be.

7 The Chairman. I didn't know about the phase-out.

8 Senator Moynihan. 80, 60, 40, 20. 0. Four years.
9 In effect, this would be five years in the program. The
10 first year would be 100 percent -- that starts in July.
11 Then 80, 60, 40, 20 and gone.

12 The Chairman. I don't want to do that, but I will
13 listen to Treasury.

14 Mr. Chapoton. Mr. Chairman, I think that the one that
15 we ought to focus on is limiting this problem for the future,
16 and as the staff has already suggested, it ought to be
17 limited to run for the future. We ought to get around this
18 problem where we encourage this type of very noneconomical
19 conduct.

20 Senator Moynihan. Mr. Secretary, would you mind if I
21 interrupted? The proposal would be to cut down from the 1985
22 level as a cap, not to let it float up and have 80 percent.

23 Mr. Chapoton. But Senator Moynihan is perfectly
24 correct. The Government of Puerto Rico applied for a ruling
25 to the Bureau of Alcohol, Tobacco, and Firearms. It

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1 disclosed what they were intending to do, got a favorable
2 ruling, and then set about doing it. The revenues, I think,
3 have exceeded their original projections. If we take care
4 of the problem for the future, I think the only question is
5 what we do about the revenues now. We think we should leave
6 in place for the remainder of this fiscal year of Puerto
7 Rico which ends on June 30 and then through next year, we
8 would not -- if the committee wants to think it through, all
9 of 1985 for Puerto Rico -- but Senator Moynihan, we could
10 not support going beyond late 1985. And you might-- We
11 could not support going beyond 1985.

12 Senator Long. Let me just ask this question now. Why
13 were not we on this committee advised about this? Now, here
14 is something that could cost the Government \$4 billion a
15 year. Now, when somebody gave a letter down there saying
16 that this thing was all right -- okay, here is a letter
17 signed by Government officials -- this Government -- saying
18 they could do it. Were you advised about that Mr. Chapoton?

19 Mr. Chapoton. No, sir, I was not. It was primarily a
20 technical amendment, whether this was a redistillation
21 process within the meaning of the cover-over provisions of
22 the law.

23 Senator Long. Now, you know, we were not advised.

24 Mr. Chapoton. Yes, you were not advised, but we were
25 not either.

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1 Senator Long. At the time that letter was given, did
2 the person who signed that letter advise any responsible
3 person who was his superior what the potential loss to the
4 U.S. Treasury was by permitting this scheme to go forward?

5 Mr. Chapoton. They did not, as far as I know, advise
6 anyone. I frankly think, Senator, they didn't recognize
7 what was involved.

8 The Chairman. Somebody indicated to me it was \$5
9 million.

10 Mr. Belas. It was five million gallons, I believe.
11 They were under the impression that it would be a \$50 million
12 program, not a \$200 million program, but that, of course,
13 still doesn't excuse the \$50 million.

14 Senator Long. Frankly, in my judgment, anybody who did
15 that should be moved out of Government. That type thing
16 could bankrupt our Government, and when we find out about it,
17 I think we should terminate it as quick as we know how.
18 Now, to say because they did this thing that you are going
19 to let them do it for five years, in my judgment that is
20 patently ridiculous. That is taking unfair advantage of
21 something we did, which was a wonderful deal for Puerto Rico.
22 The Federal taxes that are collected down there -- let them
23 keep the money down there. Then, they take the money and
24 use that to subsidize the operation, which can put all our
25 people out of business up here. But further than that, it is

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1 an enormous rate on our Treasury -- something that we did
2 not intend at all.

3 Senator Moynihan. Would the Senator yield for a remark?
4 And he knows that I am saying this with the great affection
5 in which I hold him. The people of Puerto Rico are our
6 people, too. They are American citizens.

7 Senator Long. Well, of course they are. Have I said
8 anything different than that? All I am saying is that it is
9 a tremendous burden on us. No other State--no State in the
10 Union gets that break. We can keep all the Federal taxes
11 in our own State, so we are not in a position to parlay that
12 and subsidize it to make a further gain out of it.

13 But it would seem to me that when we find out about it
14 on this end, it is our duty to terminate the thing. Now, it
15 is all right with me to let this thing continue -- how long
16 would it be to the end of this fiscal year?

17 The Chairman. The end of June.

18 Mr. Belas. It is the end of June.

19 Senator Long. To the end of June. I don't see any
20 reason why we should go beyond that.

21 Mr. Chapoton. Senator, I think we just have to recognize
22 there has been a budget. This is a significant amount of
23 money in the budget for Puerto Rico's next fiscal year.
24 And I think we ought to concentrate on -- we shouldn't design
25 the law that encourages this type of thing -- both here and

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1 in the Virgin Islands. I think the main thing is to make
2 sure we correct the law in that regard. We feel that we
3 have, I think incorrectly -- I agree with the Senator --
4 issued a ruling that they quite aboveboard acted on the
5 ruling, and established their plans for next year, and I
6 understand there will be severe hardship by the loss of those
7 funds. However, we may not have given those funds if my
8 office, for example, had --

9 Senator Long. How long have they had the funds? How
10 long has this been going on?

11 Senator Moynihan. It has been going on for a year. May
12 I say, sir, that this just started, and it started in
13 response to cuts that we had made in programs going down
14 there. And remember, that the American citizens in Puerto
15 Rico are singular in that we have statutes all over the
16 books and particularly from this committee that say an
17 American citizen is entitled to X benefits under welfare,
18 or Y benefits under education, but if you are an American
19 citizen of Puerto Rico, you are entitled to X minus Y.
20 Can't we just help them smooth out their budget? You will
21 never hear about this subject again.

22 Senator Long. It is all right with me to let them
23 continue to the end of this fiscal year, and it is all right
24 with me if you want to do some of it next year, but I don't
25 think that it should go any further. But even this year, if

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1 we are going to do that, something should be done to see
2 that this subsidy is not used to put Americans up here out
3 of business who can't compete with that subsidy. Some of
4 them tell me that they won't last the year out, up against
5 that kind of competition.

6 Mr. Belas. We have heard the same from certain
7 distillers in this country..

8 The Chairman. I thought the question was, when we
9 came in this morning, whether the effective date would be
10 the date of enactment or the date of introduction of the
11 bill -- February 1 -- or the end of the fiscal year. And
12 I was prepared to suggest we go to the end of the fiscal
13 year. I am not prepared -- unless Treasury has some strong
14 feeling that we ought to continue it -- if there is a need
15 for a direct subsidy to Puerto Rico, maybe they can do that
16 in the Appropriations Committee.

17 Mr. Chapoton. Mr. Chairman, I think I have made the
18 point. We feel that we have presented Puerto Rico with a
19 method of doing something. They acted on it, and the sole
20 question is a judgment call. The question is their plans
21 are made for next year, and it will be a hardship --

22 The Chairman. Well, they haven't made their plans for
23 next year.

24 Senator Moynihan. Yes, they have.

25 Mr. Chapoton. Their budget for next year.

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1 Mr. Belas. Mr. Chairman, we understand that they have
2 made a preliminary budget for FY 1985 -- their 1985. But
3 the budget will not be finalized until next month. Correct
4 me if I am wrong.

5 Senator Moynihan. Neither will ours. Mr. Chairman, I
6 wonder if I could put a simple proposition? Treasury
7 suggests that they be allowed to continue this year and
8 one more fiscal year -- their fiscal year which starts in
9 July. Could we agree to that? And then the subject is
10 over, done, and ended.

11 The Chairman. I wouldn't agree to that. No.

12 Senator Moynihan. Would we have a vote on it, Mr.
13 Chairman?

14 Mr. Brockway. Mr. Chairman, on that, if you extend it
15 for some period, I think it would be advisable to put, in
16 any event, a dollar cap. If you just extend it for a period
17 of time, then you could run through a lot of alcohol and
18 run it up.

19 The Chairman. They are talking about going back to the
20 higher figure, aren't they, instead of --

21 Mr. Brockway. Because their budget estimates are lower
22 than we are estimating what is going through and what their
23 current revenue loss is.

24 Senator Moynihan. Their budget estimate is \$214 -- the
25 Government.

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1 Senator Bentsen. Mr. Chairman, why don't you compromise
2 this and say for fiscal year 1985 -- their budget year.
3 Instead of the \$220 or something like that, we put a cap
4 of \$115, \$110, something like that, and go through the end
5 of June and then put a cap on it for fiscal year 1985, their
6 budget. Would that work or not? Let's give it some thought.

7 Mr. Brockway. You could do that. You could certainly
8 put a cap on it like that. You would also want to put a cap
9 on for fiscal year 1984 at the current level, which would
10 be something like -- they are budgeting \$130 this year, and
11 you use that as the cap. And then, you just set whatever
12 level you wanted for the later year.

13 The Chairman. I don't have any quarrel with doing
14 anything. But when you find a boondoggle, why do you let
15 it continue? No wonder we have got a big deficit. All
16 the governors were in town yesterday castigating the Congress
17 for not reducing the deficit, and here we are just throwing
18 money away.

19 Senator Bradley. Mr. Chairman, what is the Treasury's
20 recommendation?

21 Mr. Chapoton. We would recommend that you put a cap
22 -- if you want to get into that -- put a cap for the remainder
23 of this fiscal year at the current rate, so we don't have
24 an increase in the level. And then, provide it into fiscal
25 1985, but I agree subject to a cap. We have not recommended

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1 the dollar cap, but you certainly would have some --

2 Senator Bradley. So, Treasury did not recommend a
3 dollar cap. Senator Bentsen said he thought there should
4 be a dollar cap, so that that brings it down from what
5 Treasury had recommended.

6 Senator Bentsen. What I am suggesting is that we put a
7 cap at the current level through the balance of this--until
8 the start of their fiscal budget of 1985, and then we put
9 a cap on for half of the preceding one to give them a
10 phase-out of this process.

11 Mr. Chapoton. That would make sense.

12 The Chairman. Let's vote first on ending at the end
13 of this fiscal year. And then, if that fails --

14 Senator Moynihan. Could we, Mr. Chairman, have three
15 votes -- ending it this fiscal year, having a vote on
16 allowing it to continue with a cap at the budgeted estimate
17 for 1985, and then --

18 Mr. Chafee. What are the revenue figures on this? I
19 can't find this page. Suppose we-- What does it mean to
20 the U.S. Treasury? Suppose we ended it completely.

21 Mr. Brockway. If you ended it completely, we are
22 estimating that in fiscal 1984 you would pick up \$119, in
23 fiscal 1985, \$260, in fiscal 1986 --

24 Senator Chafee. What page is that on?

25 Mr. Brockway. This is not on that sheet. Roughly, if

1 you ended it right now over that four-year period, you would
2 pick up about a billion dollars of savings. If you put a
3 cap on it, for example, for the rest of this year, you would
4 lose from that roughly \$50 million for the remainder of this
5 year.

6 Mr. DeArment. Senator Chafee, on the document that is
7 entitled "Down Payment Budget Plan" -- with all the numbers
8 -- if you will look on page 3 of that, that number -- there
9 is a line called rebate and that is the savings.

10 Senator Chafee. Hold it. I don't see that.

11 Mr. DeArment. Midway down the page there is hospital,
12 labs, Medicaid, assignment of rights, and right under
13 assignment of rights, rebate. And that line across there
14 is the estimated savings from the full proposal.

15 Senator Chafee. Now, the first column where it says
16 zero -- that is fiscal 1984 anyway.

17 Mr. DeArment. No, there is no zero, Senator. The first
18 number should -- right across from rebates -- be .1, then
19 .3, then .3, for a total of \$1 billion.

20 Senator Chafee. Now, that is \$100 million. How much is
21 this to the Treasury? Is this 10 percent to the Treasury
22 of the Commonwealth of Puerto Rico?

23 Senator Moynihan. Then it would be for one year.

24 The Chairman. Well, you are talking about two years now.
25 The rest of this year and all of next year.

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Senator Moynihan. For another 16 months.

Senator Long. Now, let me just read a little from this letter -- a line or two from this. Now, here is a letter where this acting director suggested this to the asistant director for enforcement operations.

(continued on next page)

1 Senator Long. I suppose we could lie for them and
2 say this is all okay. At that point, he is estimating that
3 this would apply to 5 million gallons annually. All right,
4 that's \$52 million and \$50.00 that he's talking about. Now
5 right now this thing is costing us how much?

6 So a year later it is costing three times what it is
7 estimated. Now none of this was told to us. If this had
8 been told to us, how long would we have authorized this to
9 go on.

10 So as a practical matter, the Congress wouldn't have
11 approved this for a moment. So here they start this scheme
12 and now it is costing us \$135 million a year. And it could
13 go up to \$4 billion a year. And it is our duty to stop it.

14 We should have stopped it the first time we heard about
15 it. Now listen to this paragraph. "The nominal nature of
16 the treatment, coupled with the government subsidies" -- now
17 that means the government subsidy by Puerto Rico to subsidize
18 this operation by those who do it -- "leads us to believe
19 that the proposed activity is no more than a plan to divert
20 tax revenues, which rightfully belong to the U.S. Treasury."

21 Now when they start these things and we find out about
22 it, we are in the process of acting, and we ought to do this.
23 But how long should we reward Puerto Rico for doing it? How
24 long should we reward them for doing it?

25 Here is something where, for all understanding, maybe

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1 they can keep all the money in their own state. That's all
2 right. I have no complaint about that.

3 If they want to use it to subsidize their own
4 producers to produce more to consumers down there in Puerto
5 Rico, I have no complaint about that. But when they are
6 using this to put our own people out of business up here in
7 the United States, and as a raid on our Treasury -- it
8 could potentially be a \$4 billion raid on the U.S. Treasury.
9 Well, how long do we want to reward that type of activity?

10 It seems to me that we ought to just say, well, if we
11 let them get away with it the rest of this year -- I think
12 that's generous enough. By rights, they weren't entitled to
13 five cents out of this scheme. And it turns out they are
14 going to get, what, about \$150 million or some such thing.
15 Why should we continue it into next year?

16 The Chairman. Why don't we have a vote on this? Ending
17 it this fiscal year, and if that fails --

18 Senator Moynihan. Let's have the vote, Mr. Chairman,
19 on ending it this fiscal year and Senator Bentsen's proposal.

20 The Chairman. Okay. Why don't we just say June 30 of
21 this year?

22 Senator Chafee. What is Senator Bentsen's proposal?
23 That they end it with --

24 Senator Bentsen. That we cut it in half for the next
25 fiscal year. That we put a cap on it now until June of this

1 year.

2 Senator Moynihan. Well, we have to be --

3 The Chairman. As I see it, the only thing that will
4 make sense if you are going to extend it a year is to go
5 back to this Treasury letter and say it's 5 million gallons
6 and \$50 million. I mean that's all they ever hoped to get
7 in the first place. Now we want to double or triple that.

8 Senator Bradley. What's the difference in revenues
9 between the two proposals that we are voting on?

10 Senator Moynihan. It would be about -- if we had it
11 capped at half the rate, the difference would be about \$105
12 million for one year.

13 Mr. Brockway. If you allowed \$105 million for the second
14 year, that would be what the difference was.

15 Senator Moynihan. One time; not to be repeated then.

16 Senator Chafee. What's the date of the letter?

17 The Chairman. June of 1982.

18 Senator Chafee. Mr. Chairman, I think you have got a
19 proposal here that makes some sense. Suppose we capped for
20 the -- let it continue for this fiscal year; then go to
21 what the letter talks about for the second fiscal year; and
22 then end it.

23 In other words, it isn't as though they are geared up
24 for many years in this. I understand the date of this letter
25 is what, 1982?

1 Senator Moynihan. No.

2 Senator Chafee. What's the date of the letter?

3 The Chairman. June of 1982.

4 Senator Chafee. Okay. So they are not entrenched with
5 this into their system.

6 Senator Moynihan. Nor are they asking that it be.
7 They say, all right, if you want to change the rule on us,
8 but give us a fiscal year. That's all.

9 Senator Chafee. Well, we are not inclined to do that.
10 At least I'm not. So I have got a suggestion. You give
11 them exactly what they anticipated they were going to get
12 when the letter was written only a little over a year ago.
13 And it seems to me that is a pretty fair deal.

14 The Chairman. They are going to pick up \$50 million.

15 Senator Matsunaga. Mr. Chairman, I think the proposal
16 of letting them continue as is until the end of this fiscal
17 year, their fiscal year, and capping it at 50 percent is a
18 fair proposal. I think we should do it.

19 The Chairman. I don't make any difference. It seems
20 to me we are getting into very sensitive areas -- Medicaid,
21 Medicare, all these things that are very sensitive. And here
22 is a clear boondoggle and we want to continue it. I don't
23 want to. I want to be on the record voting to end it this
24 fiscal year. If we lose, we lose.

25 Call the roll.

1 Mr. DeArment. Mr. Packwood?
2 Senator Packwood. Aye.
3 Mr. DeArment. Mr. Roth?
4 Senator Roth. Aye.
5 Mr. DeArment. Mr. Danforth?
6 Senator Danforth. Aye.
7 Mr. DeArment. Mr. Chafee?
8 Senator Chafee. No.
9 Mr. DeArment. Mr. Heinz?
10 Senator Heinz. Aye.
11 Mr. DeArment. Mr. Wallop?
12 (No response)
13 Mr. DeArment. Mr. Durenberger?
14 Senator Durenberger. Aye.
15 Mr. DeArment. Mr. Armstrong?
16 Senator Armstrong. Aye.
17 Mr. DeArment. Mr. Symms?
18 (No response)
19 Mr. DeArment. Mr. Grassley?
20 Senator Grassley. Aye.
21 Mr. DeArment. Mr. Long?
22 Senator Long. Aye.
23 Mr. DeArment. Mr. Bentsen?
24 Senator Bentsen. No.
25 Mr. DeArment. Mr. Matsunaga?

1 Senator Matsunaga. No.

2 Mr. DeArment. Mr. Moynihan?

3 Senator Moynihan. No.

4 Mr. DeArment. Mr. Baucus?

5 Senator Baucus. Aye.

6 Mr. DeArment. Mr. Boren?

7 Senator Boren. Aye.

8 Mr. DeArment. Mr. Bradley?

9 Senator Bradley. No.

10 Mr. DeArment. Mr. Mitchell?

11 (No response)

12 Mr. DeArment. Mr. Pryor?

13 Senator Pryor. Aye.

14 Mr. DeArment. Mr. Chairman.

15 The Chairman. Aye.

16 On this vote the yeas are 12, and the nays are 5.

17 And it's terminated as of June 30 of this year.

18 Senator Long. Now, Mr. Chairman, I believe the staff
19 has an amendment to prevent the islands from using this
20 subsidy to take an unfair advantage of our competitors here
21 in the United States who are threatened with being put out
22 of business in some cases. Do you have such an amendment?

23 Mr. Belas. Mr. Long, the concern would be that the
24 islands, Virgin Islands and Puerto Rico, would have excess
25 capacity which they could use to produce cane neutral spirits

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1 which would be the same thing as grain neutral spirits used
2 in cordials and vodka and gin. And with the rebates, the
3 cover over, would be able to compete unfairly with the
4 grain neutral spirits produced in the mainland United States.

5 The proposal would be to --

6 Senator Moynihan. What is being said here? What is
7 the word "unfair?" I mean they are trying to make a living
8 down there. They have got 25 percent unemployment. We cut
9 them every time we turn around. They are American citizens.
10 The only place they get treated equally is when they are
11 drafted.

12 This is not unfair.

13 Senator Long. We are talking about a \$.50 a
14 gallon subsidy on something that costs \$.88 to produce.
15 That's what we are talking about. And nobody in the United
16 States can compete with that. I don't know whether you have
17 any distillers up there in New York State or not. But we
18 have some in Louisiana and other states have people who are
19 in that business.

20 And they can't compete with that. I assume their
21 profit might be, what, \$.07 or \$.08 a gallon, and they
22 can't compete with somebody that is being subsidized \$.50
23 a gallon.

24 Senator Bradley. Well, I would like, if we could, to
25 take a little different slant on this issue. We are dealing

1 with an administration proposal to give \$10 billion in
2 assistance to Central America. And here we have a proposal
3 that amounts to something under \$50 million for a territory
4 of the United States, commonwealth. And it seems to me that
5 we have to try to keep this thing in perspective.

6 I understand that some states are adversely affected
7 by this; there are some people who have industries in their
8 states who are affected. But I think there is a larger issue
9 here.

10 And I don't think we can pull the rug out from under our
11 people in a critical area of the world, and at the same time
12 argue that we are threatened in Central America and have to
13 spend \$10 billion in economic assistance.

14 Senator Long. Now we are not talking here about anything
15 for the Puerto Rican government. At this point all we are
16 talking about the extent to which they are permitted to
17 subsidize their producers to compete with the U.S. producers.

18 Mr. Belas. Senator Long, as you know, the only two
19 areas that benefit from this are the Virgin Islands and
20 Puerto Rico. The Virgin Islands have almost no cane neutral
21 spirit production. It's between zero and 1 percent. It's
22 negligible. And, therefore, this will not have any impact on
23 them other than a marketing opportunity in the future.

24 For the Puerto Rican government, they are receiving
25 \$30 million according to the budget for this year in rebate

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1 cover over for the cane neutral spirits. And this would
2 have that impact on the \$30 million.

3 But the concern would be that they have this excess
4 capacity which they are currently using for the Reed
5 distilling program, and that could easily be turned over
6 to distilling molasses into a cane neutral spirit which
7 would compete with the grain neutral spirits in this country.

8 Senator Long. Could we have Mr. Hardee on that?

9 Mr. Hardee. What Senator Long's concern is that we do
10 not subsidize -- the Puerto Rican government does not pay
11 money over to these companies that they can use to compete
12 with domestic brands, domestic distillery. What he wants
13 to do is try to let Puerto Rico keep more of the money
14 rather than rebating some of that in the form of a profit
15 to the distillers in Puerto Rico.

16 And we have a staff amendment that would basically say
17 that Puerto Rico would keep the money and not pass on anything
18 other than direct costs that are incurred in shipping the
19 redistilled spirits to and from Puerto Rico.

20 Senator Bradley. Could we clarify the point? There is
21 no revenue that this means to the government of Puerto Rico?
22 This means no revenue to the government of Puerto Rico? I
23 don't think that's correct.

24 Mr. DeArment. When you say "this" --

25 Senator Bradley. This provision. In other words we

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1 have acted to cut them off in June of this year. Now that
2 means the following year they would have how much less
3 revenue in the general treasury of the government of Puerto
4 Rico?

5 Mr. DeArment. They were anticipating that we would --
6 they were anticipating \$214 million which would be rebated
7 to them.

8 Senator Bradley. Two hundred and fourteen million to
9 the government of Puerto Rico? I mean is that what this
10 committee really wants to do? I mean they are not asking
11 for this to continue. They are saying help us cope with what
12 you have already done in the Congress, which has in the last
13 few years slashed considerably the amount of money that is
14 appropriated. And I agree with you, Mr. Chairman, that's the
15 better way to do it.

16 The Chairman. Well, I don't want to get into --

17 Senator Bradley. It's an abrupt change to say we are
18 going to cut this off in June of this year and in the same
19 breath in the same Congress say we are going to send \$10
20 billion worth of assistance to other countries in Central
21 America.

22 The Chairman. I don't know if that would be a good
23 analogy or not. I'm a strong supporter of the Puerto Rican
24 interest, and food stamps, Medicare, Medicaid, the Caribbean
25 Basin. It just seems to me that we can't even close a

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1 gaping loophole like that and we are never going to reach
2 \$200 billion.

3 If somebody thinks Puerto Rico ought to have an
4 appropriation, I will vote for it. But let's don't take it
5 out of -- somebody made a stupid mistake in BATF. And I
6 thought the only issue this morning was whether we are
7 going to end it February 1st or June 30. And I didn't even
8 want to go to June 30, as my staff will recall. But I
9 said okay. I don't want to interfere with the budget they
10 are already working with, so let's go to June 30.

11 Mr. Belas. Mr. Chairman, maybe it would be useful to
12 clarify what the revenue protection elements that Senator
13 Long was bringing up. It is two-fold. One the question is
14 have you really plugged the loophole if, in fact, the
15 production can continue in another form? And the second
16 one is do you allow the cover over, the rebate, to be allowed
17 to Puerto Rico or the Virgin Islands if, in fact, part of
18 that cover over is then paid back to the American distiller
19 as an incentive for him to bring the grain spirits in the
20 short interim period, five month period, that it would
21 continue or not?

22 And it was the second part that I think was unclear that
23 Senator Long was trying to get at. Do you allow the cover
24 over if, in fact, a portion of the 10/50 proof gallon is
25 rebated to the American distiller?

1 Senator Moynihan. Mr. Chairman, may I suggest that
2 we are not really prepared to deal with this second issue
3 today. The Treasury ought to have a view on it. I'm not
4 sure they have a view. Do you have a view, Mr. Secretary?

5 Secretary Chapoton. I'm not really sure how this
6 works. This would be the idea of preventing a rebate to
7 the producer. I guess the effect of that would be the
8 producer would leave Puerto Rico immediately. I'm not sure.

9 Mr. Belas. Mr. Chairman, the amendment -- the potential
10 amendment would be to limit the amount of the payment from
11 the Puerto Rican government to the Puerto Rican distillery
12 to an amount that would cover the cost of the transportation
13 from the United States to Puerto Rico and back, but no
14 additional amount would be on that.

15 Senator Moynihan. May I suggest, sir, that we ought
16 to give the Treasury a chance to look at that.

17 The Chairman. I think that's a good idea. If Senator
18 Long has no objections. Would you look at the amendment? I
19 think David Hardee has the amendment prepared. Is that
20 correct?

21 Mr. Hardee. Yes.

22 Senator Moynihan. Well, I haven't seen that amendment,
23 and I really think we are dealing in a very high-handed manner
24 with a group of American citizens. This is their economic
25 development policy. Do we go into North Dakota and say you

1 have a policy of taxing this land at a lower rate than that
2 land and you had better stop it right away?

3 Senator Long. We are talking about a subsidy.

4 Senator Moynihan. Or severance taxes for this but not
5 for something else?

6 Senator Long. We are talking about a subsidy here, a
7 very large subsidy, when you compare it to the cost of
8 manufacture. We are talking about a very large subsidy and
9 we have producers who are prepared to come testify that they
10 can't compete with this. They will be broke.

11 Senator Moynihan. Let them come testify. We will have
12 a hearing.

13 Senator Long. Well, fine. Do you want to hold the
14 hearing? We will just bring people up to testify. They
15 can't compete against a \$.50 subsidy on something that costs
16 \$.88 to manufacture. And all we are saying is, well,
17 now -- some of them say -- but for all we know some people
18 might not last the six months trying to compete with this
19 type of thing. Don't we have indications from producers that
20 they are in difficulty trying to compete with this, Mr.
21 Hardee?

22 Mr. Hardee. Yes, Senator Long. The staff amendment is
23 only two-fold, and this has been worked out by Mr. Belas and
24 myself. One is just to say that cost may be reimbursed for
25 a company shipping spirits to and from Puerto Rico, and the

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1 cost for redistilling in Puerto Rico, but they can't have
2 any more than that. So they can't subsidize and have an
3 unfair competitive advantage vis-a-vis the domestic
4 distillers.

5 And in the second part of the proposal, that is just to
6 clarify that vodka based white distilled spirits, whether
7 it's produced out of grain or out of cane, is the same, and
8 treat that as the same as redistilled spirits.

9 Senator Bradley. Mr. Chairman, I must say I don't
10 understand what Mr. Hardee is saying.

11 The Chairman. I think what we might do is have Treasury
12 get together with staff and with Senator Moynihan and
13 Senator Long and see if there is some resolution. If not,
14 we will just have to bring it up and vote on it.

15 Now if we can move onto the so-called tax reform areas.

16 (Pause)

17 The Chairman. As I understand the Treasury package
18 of so-called tax reform areas, there were questions raised
19 by a certain Senator with reference to certain areas of
20 that package. What we had hoped to do was to go through and
21 tentatively approve those where there are no questions, and
22 then set aside -- I think Senator Boren had a question in
23 one area; Senator Heinz had a question in one area; there
24 may be others who have questions. If we can't resolve the
25 problem, then we will have to vote later today or this

1 evening. So maybe we could just start. Buck, do you want
2 to go through Treasury's?

3 Secretary Chapoton. I will just give a rather brief
4 description of each of the proposals, and then if there are
5 any questions about it, we can deal with it.

6 The first set of proposals relates to partnership
7 allocations. We are making four changes in those rules. The
8 first would prohibit an allocation of either gross or net
9 income that has the affect of making an expense that would
10 otherwise would be a capital expense deductible by treating
11 it as an income allocation rather than a capital expenditure.
12 We would not make any change in the rules that an item
13 allocation, if it otherwise -- that is, an item of allocation
14 of a specific deduction -- if it otherwise has substantial
15 economic effect which is the current law rule -- that would
16 not be changed.

17 The Chairman. Anybody raise objection to that area?

18 Secretary Chapoton. Not that I'm aware of.

19 The Chairman. If not, we will tentatively approve that
20 provision.

21 Senator Symms. Where are you in the book?

22 The Chairman. Page 1.

23 Secretary Chapoton. Well, the one I just described in
24 that is on Page 1. That is little two ii, limitation on
25 partnership allocation and recharacterization of certain

1 partnership distributions.

2 Then I will move back to the first one -- retroactive
3 partnership allocations. This is simply a change to give
4 affect to a change that we thought was clearly adopted in
5 1976. That is, we would prevent avoiding the rule that says
6 you cannot allocate to a new partner losses before the day
7 he entered the partnership. I'm not aware of any
8 controversy on that.

9 Then the third one on that page would be a rule to
10 prevent shifting of income and loss relating to contributed
11 property. For example, if you have property that has
12 depreciated or appreciated. Attempts have been made to
13 use partnerships, the partnership mechanism, to transfer that
14 to another partner by the carryover basis. When you transfer
15 the property of the partnership, it has a carryover basis.
16 And then the new partner would have an interest in that
17 property. And could take advantage, for example, of a
18 built-in loss on that property through the partnership
19 allocation mechanism.

20 This would simply say that built-in losses on
21 contributed assets would retain their character. First of
22 all, the built-in gain or loss would have to be allocated to
23 the partner who makes the contribution so you couldn't shift
24 it to another partner.

25 Secondly, if you contribute inventory, property or

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1 property of that type, it would keep its character as
2 inventory property for five years from the date of the
3 contribution so you couldn't use the partnership to turn
4 that property into capital gain property, for example.

5 I'm not aware of any objection to that, Mr. Chairman.

6 Senator Danforth. Back to your 1(a)(3) now.

7 Secretary Chapoton. 1(a)(3), right.

8 Senator Danforth. And you have just described 1(a),
9 all of 1(a)?

10 Secretary Chapoton. Completed 1(a) now.

11 Senator Danforth. All right. If there is no objection,
12 then we will agree to those tentatively.

13 Secretary Chapoton. Okay.

14 Then on top of Page 2, (b) is charitable contributions.
15 The proposal is a Treasury proposal that would have -- two
16 favorable proposals. The first is increase the current
17 50 percent of AGI limit on charitable gifts to public
18 charities. Increase that from 50 to 60 percent. The second
19 favorable proposal to charitable giving would be to increase
20 the present five year carryover period on excess gifts,
21 gifts that exceed whatever limit the law provides, the 50
22 percent AGI limit now, increase that from 5 to 15 years.

23 And then the third proposal would be to prevent
24 property that has -- to limit the deduction for property
25 contributed to a charity to its cost basis if the

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1 contribution is made within three years after the property
2 was acquired. That we have proposed to prevent the gemstone
3 type of abuse where a property is acquired by a taxpayer and
4 then as soon as the one year period is over, makes a gift
5 to a charity and claims a very large increase in the value of
6 the property, and takes a large charitable deduction.

7 Now there is, as you know, Senator Danforth, a concern
8 about the third step in that proposal.

9 Senator Durenberger. Mr. Chairman, I have done a lot
10 of work on this section with that problem. And we have
11 presented an alternative which I think in the long run
12 overcomes this baby with the bath water problem that I think
13 we get into if we try to get at gemstones with this three
14 year provision. It's got a whole series of toughening up
15 appraisal requirements and so forth. And I think Treasury
16 is now in the process of looking at that alternative.

17 Secretary Chapoton. Let us look at that, Senator
18 Durenberger.

19 The problem is it is correct. If you knew appraisals
20 were sound, this problem would disappear. But, frankly, the
21 appraisal problem just doesn't seem to disappear no matter
22 what we do. And so we thought there ought to be a pretty
23 straightforward approach here, and this would be.

24 Now it would have some impact on charitable giving
25 outside of the appraisal problem, but we do not think it would

1 have any significant adverse impact.

2 Should I --

3 The Chairman. Without objection.

4 Secretary Chapoton. Senator Dole, we approved the
5 l(a) on the first page. And passing over (b), as I understand
6 it on the second page. And then we go to number (c).

7 We are proposing two changes in the like kind exchange
8 rules. The first would simply say that if your change is a
9 partnership, interests are not within the like kind of change
10 rules. It has not been altogether clear historically
11 whether partnership interests are intended to be within
12 the like kind exchange rules or not. Stock, interest in
13 trusts and other similar interests are not and we think that a
14 partnership should not be included. Indeed, it is claimed
15 as a method of getting out of burned out tax shelters at
16 a lower tax incident. And so we think that ought to be
17 precluded altogether.

18 The Chairman. Have you given the revenue implications
19 as you have gone along?

20 Secretary Chapoton. No, sir, I haven't. We do have a
21 sheet.

22 The Chairman. I think it might be helpful to some.

23 Secretary Chapoton. The like kind exchange provision
24 would --

25 The Chairman. If you just Xerox that.

1 Secretary Chapoton. That's what he is going to do.

2 The like kind exchange provision would pick up \$1.5
3 billion over the period 1985 through 1987.

4 The second element of the like kind exchange provision
5 would prevent deferred like kind exchanges. The rule under
6 a case decided by, I believe, the 9th Circuit some years
7 ago allowed one party to make an exchange of property and
8 then have a period of time up to five years in that case to
9 designate like kind property that would be purchased by his
10 assignee, and then conveyed back to him.

11 When you have that situation, there is really no reason
12 for a tax incident to not fall. The parties have agreed on
13 the value, obviously, and the party selling the property has
14 a very much like right to demand cash payment at any time.

15 So our point would be that like kind exchanges should
16 qualify, but you should make the exchange at or about the
17 same time. And we are proposing that it has to be completed
18 within 90 days after the taxpayer transfers his property.
19 That he has to get the other property back within 90 days
20 for it to be a like kind exchange.

21 Senator Matsunaga. Mr. Chairman, I brought this
22 question up at our last meeting, but the language will be
23 such as to exclude those transactions which have already
24 been entered into although the full exchange will not have
25 been completed within 90 days.

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1 Secretary Chapoton. That is correct. This would be
2 effective for exchanges.

3 Senator Matsunaga. For contractual arrangements
4 entered only after the --

5 Secretary Chapoton. Right. One leg has been completed
6 before the date of enactment of this legislation, then the
7 new rule would not apply to that transaction.

8 Senator Matsunaga. Oh.

9 The Chairman. Does that satisfy you?

10 Senator Matsunaga. Yeah. If the language is clear on
11 that. Maybe it could be clarified in the report.

12 Secretary Chapoton. The staff on the committee has
13 suggested extend the 90 day period to the lesser of six
14 months of the date the return is filed. We wouldn't have
15 any objection to an extension like that.

16 The Chairman. The staff raised a concern.

17 Mr. DeArment. That was one of the member's concerns
18 that the Treasury could accommodate.

19 The Chairman. Without objection.

20 Secretary Chapoton. Okay.

21 The Chairman. Which members so the record will
22 indicate that?

23 Mr. DeArment. Senator Bentsen, we believe.

24 The Chairman. All right.

25 Secretary Chapoton. Okay. Item (d) on Page 2,

1 market discount on bonds would simply be treated as
2 ordinary income. Market discount when a purchaser
3 purchases a bond in the secondary market. He looks at the
4 market discount as an interest return on his purchase. There
5 is no reason not to treat that as ordinary income, and we
6 would propose that it be so treated.

7 That would have a negligible affect on revenues because
8 it would apply to obligations issued after the date of
9 enactment.

10 The Chairman. Without objection.

11 Secretary Chapoton. Then turning to category two,
12 accounting abuses on page two. Item (a), the original
13 issue discount rules would be extended to cover the sales
14 of property and we would, in effect, provide that to
15 prevent mismatching of income and deductions that with the
16 exceptions specified and the exceptions for sales of farms
17 and of principal residences and transactions under
18 \$250,000.00. But for those transactions, exchanges of
19 property for a note on a discount basis, discount note, be
20 the discount element would be treated as interest and it
21 would be subject to the rules of present law requiring
22 inclusion of income over the life of the obligation on the
23 recipient's side, on the holder of the obligation, and the
24 deductions on the other side would be treated in a
25 consistent manner.

1 This does prevent the mismatching that we have been
2 concerned about. That is a major tax shelter device today.

3 In addition, the imputed interest rules would be
4 strengthened. Under current law, under Section 483, interest,
5 if interest is unstated on a transaction, or is stated at
6 below 9 percent simple interest, then the law imputes
7 interest at a higher rate. Specified in the regulations
8 currently as 10 percent. But there are several shortcomings
9 in that present provision.

10 The first of which is the test rate is simple interest;
11 not compounded interest. So it dramatically understates the
12 true interest in the transactions.

13 And, secondly, the interest is deemed paid not on an
14 economic basis but a pro rata or according to the payment
15 which has been given rise to what we call the two payment
16 device where a payment is made in an early year, and the
17 second payment made 25 or 30 years in the future, and a
18 large amount of the interest is attributed to the first
19 payment. So the purchaser then can treat a large portion of
20 the first payment as interest and deductible even though
21 he is purchasing a capital asset that would certainly not
22 economically be deductible.

23 Also by understanding the interest in the transaction
24 you overstate the principal and, therefore, the purchaser
25 can increase ITC and accelerated cost recovery deductions.

1 The Chairman. Was that the Supreme Court case on
2 that?

3 Secretary Chapoton. No. The Supreme Court case was
4 on the interest free loan transaction. I don't think there
5 was a Supreme Court case on this recently.

6 We are proposing that the deemed rate be a compound
7 rate. That it be a rate established at 6 month intervals
8 by regulations. That it be 2 percent, two points above
9 the Treasury rate on obligations of like maturity. And
10 that it be -- I guess that would be the sum of those
11 proposals.

12 We are proposing generally an effective date on the
13 date of January 1, 1985 on these changes, except for what I
14 described as two payment transaction, which we think should
15 be effective on the date of committee action because that is
16 clearly an abuse.

17 Deferred payment rules would pick up \$3 billion over
18 this period so this is a significant item.

19 The Chairman. Without objection. I think the next
20 item, the prepayment expenses, there has been some questions
21 raised, even in addition to Senator Boren. I have a
22 question on it. So maybe we can either pass that again or --

23 Senator Boren. I hope maybe we could pass it, Mr.
24 Chairman. I have provided staff with some suggestions in
25 terms of trying to get at the abuse without having a

1 devastating affect both in agriculture and in the independent
2 producing sector in terms of raising capital. So I would
3 hope that they would look at the alternatives.

4 Senator Moynihan. Mr. Chairman, can we hear from the
5 Treasury?

6 The Chairman. Sure.

7 Senator Moynihan. This is an important sum of money.

8 The Chairman. It's on 2(b).

9 Secretary Chapoton. Oh, I'm sorry. You have moved up.

10 The Chairman. Right.

11 Secretary Chapoton. Senator, prepaid expenses is -- we
12 are proposing that it not affect people, a businessman, in
13 the business in making a prepayment in connection with his
14 business.

15 But where the expense is a prepayment by an investor and
16 an economic performance will occur later, we have just seen
17 again and again that that is simply a device to shelter
18 income and it is simply, I think -- I frankly think that
19 many of the legitimate operators in the oil business and
20 in other businesses will welcome this change because it has
21 put tremendous pressure on them to try to go through the
22 charade of saying there is a business purpose for making the
23 prepayment. And, indeed, in many, many of the cases -- in
24 most of the cases, frankly -- there is no business purpose.

25 The Chairman. As I understand, it encourages investments

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1 in December. Right?

2 Secretary Chapoton. It definitely encourages payments
3 to be made in December, even though activity is deferred
4 sometimes many, many months after the end of December.

5 Senator Moynihan. And these people are avoiding
6 taxes.

7 Secretary Chapoton. They are clearly avoiding taxes.
8 They roll the taxes into the next year by this process, and
9 then the next year they face the same problem and they go
10 through the same exercise all over again.

11 Senator Moynihan. It's comparable in ways to the
12 straddle problem.

13 Secretary Chapoton. It is a straddle deferral. That
14 is correct.

15 Senator Moynihan. They have lost an awful lot of skin
16 in getting ride of the straddle a couple of years ago. I
17 don't know -- so did the Chairman. We haven't go any more
18 to lose on that subject.

19 Senator Pryor. Mr. Chairman, I would like to just say
20 that there are instances, I think, with agriculture interests,
21 farmers, who do make very legitimate use of this area. And
22 I know that we did discuss last year or last fall an
23 amendment to this that would exempt them or would at least
24 treat them differently.

25 Secretary Chapoton. That's correct.

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1 Senator Pryor. I would like your comments on that.

2 Secretary Chapoton. We are providing that for a
3 taxpayer in the business that the rule would simply not
4 apply. But if it's a doctor or lawyer investing in a
5 prepaid feed operation, for example, then he would be caught
6 under this proposal.

7 Senator Moynihan. Could I hear that again? If someone
8 is in the oil business and does something like this, then that
9 is presumed to have some economic reason because that is his
10 economic activity, but when the person with income that he
11 would not like to pay taxes on just does this in December
12 and then does it again in December,-- you can do it
13 indefinitely, I guess, can't you?

14 Senator Boren. Mr. Chairman, I would ask the Senator
15 from New York, for example, if you were a farmer and you
16 could stock up on, let's say, fertilizer or seed or something
17 that you know you are going to utilize during the next year
18 and the price happened to be lower at a certain period of
19 time, and you were going to build up your inventory and go
20 ahead and pay for it out of pocket right there and have to
21 use it within the next year -- that's what I propose -- do
22 you think that you wouldn't be able to take advantage of
23 fluctuations in the market? Or if you are in the oil
24 business and pipe happens to be at a low price in November
25 and it is going to be higher later in the year that just

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1 because you are not a corporation -- you see, most farmers
2 are not incorporated. You've got a lot of family
3 partnerships. They have got a rule here -- I don't disagree
4 with the target that they are aiming at, but I think that
5 they are hitting a lot of innocent people with the way they
6 are shooting at this target. I would like to see us -- and
7 I propose to him that we put in a proposal that the
8 expenditure must be an actual out of pocket payment,
9 irretrievably made that couldn't be refunded, that the
10 expenditure must have a legitimate non-tax business purpose,
11 and that performance of the contract must occur within one
12 year. To me, that would get rid of the abuses. But I
13 think it would be wrong to come in here and say that just
14 because they are not a corporation that they are operating
15 under a partnership -- in the oil business right now in my
16 state we had over 900 drilling rigs drilling 18 months
17 ago. We dropped all the way to 238. We are at about 340 now.
18 A lot of that has to do with the fact that we had a bank
19 collapse. We had an over-reaction in terms of attracting
20 capital.

21 Now most oil investments are put together not in a
22 corporate set up, but they will come around and I'm going to
23 be the operator or you are going to be the operator, you
24 try to get a dozen other people to put in \$5,000.00 or
25 \$10,000.00 -- very often that adds up to more than 35 percent

1 of it is by investors who are not the operator.

2 You have a very similar situation with a family farm
3 where you may have had an inheritance and you may have a
4 lot of children involved, brothers and sisters and others
5 who are not operating it, and to come in here and say that
6 they can't operate legitimately as a business -- I think if
7 it doesn't have a business purpose, yes. But if it has a
8 legitimate business purpose, why penalize an oil or an
9 agriculture or some other venture just because it is
10 operated as a partnership. I don't think that's fair.

11 And when you already have a great shortage of capital
12 and a tremendous depression in these sectors, because they
13 are cash starved right now, we ought to be encouraging
14 more investment and not less.

15 Secretary Chapoton. Senator, the case as you describe,
16 of course, would not be covered by this proposal when you
17 talk about the farmer or the oil man. If he is in the oil
18 business he would not be affected by this proposal.

19 Senator Boren. Oh, yes, he would be affected because
20 you say that in any case you don't say either/or. For
21 example, you say either instead of and. Look, number three
22 of your proposal is where the principal purpose of the
23 enterprise is avoidance or evasion of tax. Now I agree with
24 that if the principal purpose of the action is avoidance or
25 evasion of tax then they shouldn't get the deduction.

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1 But then, you say "or." You don't say "and." You
2 say "or" an enterprise where 35 percent or more of the losses
3 are allocable to limited partners. Well, you know, that's
4 true and you may have more than a 35 percent participation.
5 I would say that would be true in 90 percent of the
6 independent. Not the major companies but the independent.
7 The independent producers or operations. They may raise
8 that 35 percent of their money.

9 If you said "and," maybe that would be different.
10 But why do you just pick on something that has more than
11 35 percent outside investors or a farm, if the other
12 brothers and sisters have 40 percent of it as opposed to
13 30 percent it of -- they can't stock up on their seed or
14 fertilizer.

15 Secretary Chapoton. Of course, the problem is that
16 we are talking about people that are outside of the business.
17 And if it's more than 35 percent outside of the business,
18 that's the problem.

19 Senator Boren. Well, where are you going to get your
20 money for the independent producer sector? They are not
21 Gulf or Mobile or Exxon. That's where they get their money.
22 They have to go out here and sell participations.

23 Secretary Chapoton. They will get their money as they
24 do now. Most of them are not particularly concerned about
25 trying to speed up cash receipt at the year end for drilling

1 for the following summer.

2 Well, have you asked the sector, particularly those who
3 represent the independent sector like the IPAA and others,
4 if they feel that they -- do they agree with your statement
5 that this would have minimal impact and that most independent
6 producers feel this would have minimal impact on their
7 ability to raise capital? Do they agree with that statement?

8 Secretary Chapoton. I have not asked them. And we have
9 not heard from this, I must say, which is some sort of test.
10 But this proposal has been out there for some time.

11 The problem is, Senator, if we don't address this type
12 of problem then there is nothing we can do about the shelters
13 that involve these three to one, four to one write-offs.
14 In the rules you stated, they must be economic, I believe
15 you said, there must be a business purpose. There has to be
16 a legitimate business purpose.

17 Senator Boren. There has to be a legitimate business
18 purpose. That would codify what the existing law is
19 supposed to be.

20 Secretary Chapoton. That's current law.

21 Senator Boren. And that there would have to be an
22 out of pocket expenditure, irretrievably out of pocket.
23 You couldn't just go get a line of credit and say we are
24 going to use it or something else.

25 Secretary Chapoton. That is clearly current law.

1 Senator Boren. And that there should be performance
2 within one year.

3 Secretary Chapoton. The one year rule is, I think,
4 more or less a rule of thumb. Indeed, I think most revenue
5 agents would think it would have to be much shorter than a
6 one year. So you might even be expanding --

7 Senator Boren. Well, I would hope, Mr. Chairman, that
8 before we act on this -- I don't know why they have not
9 contacted Treasury. But I can assure you my phone has rung
10 off the wall. I've had the general counsel of the
11 Independent Producers in to talk to me. They've been doing
12 a survey among their members. That sector is in a depression
13 in my state.

14 When you have 600 rigs at a cost of \$3 to \$4 million
15 each idled and many of them not paid for with interest, when
16 you have had a major bank collapse with a \$2 billion loss,
17 and a freeze up of credit in that whole sector, and you add
18 to that kind of pressure an additional uncertainty as to the
19 means of raising -- I mean that sector is starved for
20 investment capital. We want to get those rigs working again.
21 And I am told by people in the industry that they think it
22 would have a devastating affect.

23 Now they are ready to live with something reasonable
24 that gets at the abuse of this. And I've also been
25 contacted by the cattlemen and agricultural people who are

1 not in what I would call flush circumstances at this time.
2 And I am just concerned that we not throw the baby out with
3 the bath water. I think we have all heard of these people
4 that didn't put up any cash, they weren't even at risk,
5 that there have been a lot of headlines about it, some of
6 it even involving outgoing high-ranking government
7 officials. Now I am not at all aiming at preserving that
8 kind of thing. I don't have any interest in that.

9 But I am concerned if we are to cut off another several
10 hundred million dollars of investment. And anything you do
11 in these areas affects the competitive attractiveness of
12 one kind of investment versus another. And all I can say is
13 that agriculture and energy -- two sectors I certainly know
14 about in our state. We are in a depression in those two
15 sectors, and we cannot afford another element of uncertainty.
16 And I have been contacted by people expressing grave concern
17 about this.

18 Secretary Chapoton. Senator, let me correct my earlier
19 statement. I'm advised that the IPAA has contacted us. They
20 have objected to the proposal, but has not responded when we
21 ask them for some description of the impact of the proposal.

22 We simply think that when you are dealing with year
23 end items that are trying to move deductions from the next
24 year into this year, that you are not going to have any
25 significant impact on an industry.

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1 The Chairman. Could I suggest that -- I think there
2 is no abuse because it's legal to use the system as it
3 presently is, but obviously there are a lot of cases that
4 use last minute shelters. There ought to be some way, Buck,
5 to modify this in some way. So why don't we just pass over
6 it for now. It's one of those controversial areas that we
7 will have to come back and vote on.

8 We have checked with some of our independent oil people.
9 Obviously, I think they do use this in December for drilling
10 later into the next year. A lot of people are looking for
11 ways to reduce their income tax at the end of the year.
12 Maybe you could cut it off in October or something. But in
13 any event, let's take a look at it.

14 Senator Long. Well, I'm concerned myself about this
15 matter. And I think that we ought to at least let those who
16 feel that they would be adversely affected have an
17 opportunity to testify.

18 Now I'm only looking at the type of situation in which
19 people, it seems to me, should have a right to. And
20 assuming that they could get a claim of a deduction of as
21 much as 70 percent of what you invest, and you are in a
22 50 percent bracket -- that's the top bracket -- that would
23 amount to about \$.35 tax savings on every dollar invested
24 in a drilling venture. Now my impression is that that is
25 about par for the course. Is that about the way you see it?

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1 Secretary Chapoton. I'd say that's right. About
2 70 and 75 percent of the cost.

3 Senator Long. Now that certainly wouldn't be any
4 two for one or three for one tax advantage, it would seem
5 to me.

6 Secretary Chapoton. No. But this is not limited to
7 the oil business by any means, Senator.

8 Senator Long. Well, I'm just concerned, Mr. Chairman,
9 about the fact that we have got half those rigs shut down.
10 And somebody ought to be doing something to try to get those
11 rigs working again because if we don't this nation is going
12 to be in severe trouble down the line. Now this
13 administration has been very fortunate. When the President
14 came in, the very day he came in, the Yatola Khomenia
15 turned those hostages loose. And the price of energy has
16 been going down. We have got a surplus of oil. But who
17 knows how long that is going to continue. And at such point
18 if trouble brews or breaks out again over there -- we are
19 told it could happen any day in this situation between
20 Iran and Iraq -- we would be short on energy all over again.

21 So I just don't think that we ought to cut off the
22 funds. In fact, I think we ought to try to do something
23 to help get some funds into drilling.

24 Secretary Chapoton. Senator, we would not be making
25 this proposal if we thought it would have any substantial

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1 impact on drilling activities. It is an across the board
2 device for sheltering income, for moving income from one year
3 to the next. And we are talking about it just for people
4 that are not in the business of the particular activity
5 involved.

6 The Chairman. Let's take a look at it. I don't
7 quarrel with Treasury's objective.

8 Now we have taken care of the first section there.

9 Senator Moynihan. Mr. Chairman, are we going to pass
10 this along?

11 The Chairman. As the precedent set by passing over
12 the Puerto Rican matter last week, we thought we would pass
13 this over.

14 Senator Moynihan. Well, sir, we are in a mark-up now.

15 The Chairman. Well, we were in a mark-up then. We
16 will get back to it, hopefully, this afternoon.

17 Senator Moynihan. But we will get back to it?

18 The Chairman. Oh, yes. We are not dropping it out.

19 Now we have concluded the first section. We are down
20 to three payments. What about any questions on interest
21 free loan section, related party, life hold, premature
22 accrual -- Senator Symms wants to be present when that is
23 discussed.

24 Mr. DeArment. Senator Wallop also has a conflicting
25 committee meeting, and is concerned about the premature

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1 accrual.

2 The Chairman. Estimated payments on individual
3 alternative minimum tax. Anybody raise any objection to
4 that?

5 (No response)

6 The Chairman. If not, why don't we approve those
7 sections except for premature accrual.

8 Senator Pryor. Mr. Chairman, I would like some
9 comment on the transactions in Section D there, if you
10 don't mind. Or maybe we could postpone that discussion a
11 little bit.

12 I think we are going to see in the transition rule
13 adoption that we could find a problem with some of our
14 export markets, if we adopt this rule without a great deal
15 of study.

16 The Chairman. Which one is that, Dave?

17 Senator Pryor. That would be Section D, Mr. Chairman,
18 on Page 3. That's the related party transaction.

19 The Chairman. All right. Let's just hold that one
20 off then.

21 Senator Pryor. All right.

22 The Chairman. If there is no objection, we will start
23 on related party transactions when we come back at 2:30. And
24 then premature accrual. Then the prepayments. That will be
25 three out of that group that we have not had final

1 determination. The others, without objection, will be
2 agreed to.

3 Senator Moynihan. Mr. Chairman, I have a proposal from
4 a bill I have introduced on tax shelters which I believe
5 my colleagues know about. And that is to disallow interest
6 deductions on certain short-term obligations under certain
7 circumstances.

8 Under current law, taxpayers do not pay tax on interest
9 earned on many short-term securities until they sell or cash
10 them in. If the same taxpayer has borrowed the funds to
11 purchase these securities, he can deduct his interest
12 payment as he owns them. And together the transactions
13 create a straddle. Another one of those straddle situations.
14 You deduct in one year and pick it up in the next.

15 And I would have thought this would go very well under
16 the section 1(d), the market discount on bonds treated as
17 ordinary income.

18 The Chairman. Are you aware of that proposal, Buck?

19 Secretary Chapoton. Yes, I am. It's not among our
20 proposals, but we have examined it since we have sent ours
21 forward, and we would support that proposal. It is a
22 straddle type operation.

23 Senator Moynihan. A short transition period for it,
24 but it's just another one of those things where you just avoid
25 taxes, that's all.

1 The Chairman. Any revenue estimate?

2 Secretary Chapoton. Yes.

3 Senator Moynihan. You follow the proposition?

4 Mr. Wetzler. Senator Moynihan, we are still working
5 on a revenue aspect on the --

6 Senator Moynihan. Would you like to wait until you
7 have a revenue estimate?

8 The Chairman. With no objection, let's adopt it.

9 Senator Moynihan. I mean we are not going to lose any
10 money on it.

11 Secretary Chapoton. Let us come back to you. It
12 picks up a little. It's not substantial. None of these are
13 too substantial. Let us come back to you with a number on
14 that.

15 Senator Moynihan. Can we move the measure, Mr. Chairman?

16 Mr. Wetzler. Senator Moynihan, there is sort of a
17 third proposal that is related to these which is not in your
18 bill but which we have working on with Treasury which deals
19 with leverage purchases of market discount bonds.

20 Senator Moynihan. Yeah.

21 Mr. Wetzler. And that's really -- it's another way of
22 deferring income. And if you just close up one and not
23 close up the other, you are probably not going to raise very
24 much revenue. So you might want to include that.

25 Senator Moynihan. Do we want to ask the staff and

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1 Treasury if they could combine these measures?

2 The Chairman. I think that would be a good suggestion.

3 Secretary Chapoton. I think we can combine these
4 measures. And I think it does make sense. When we give you
5 the revenue estimate, let us make a recommendation on that
6 as well.

7 Senator Moynihan. Fine. And I withdraw the measure.

8 The Chairman. Then they can prepare the combination.

9 Senator Moynihan. Right.

10 The Chairman. All right. Then at 2:30 we will come
11 back. And we will assume that we have agreed to the first
12 grouping. In the second grouping there are still three areas
13 that we need to discuss. And then if we can finish this
14 package this afternoon, we would meet again tomorrow at
15 10:00. Come back at 2:30.

16 (Whereupon, at 12:34 p.m., the mark-up session was
17 recessed.)
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25

AFTERNOON SESSION

(2:37 p.m.)

1
2
3 The Chairman. Mr. Chapoton, when we left at about
4 12:30, we had completed the second group, except there were
5 notations on prepayments, related party transactions, and
6 premature accrual.

7 As I understand the related party transactions,
8 Senator Heinz has a question there on low income housing,
9 and I'm wondering -- that's just a portion of that package --
10 if there is no objection to the balance, if we could go ahead
11 and approve that except for that one. Senator Heinz cannot
12 be here; he is on the floor on the Export Control Act. Am
13 I correct?

14 Mr. Chapoton. That is correct. There is a lot more
15 to it than low income housing. I think that would be fine.
16 We have been talking to Senator Heinz about the low income
17 housing portion, but there is no objection to the rest of it,
18 as I understand.

19 The Chairman. All right. Then, without objection, we
20 will make that exception.

21 Then, premature accrual -- Senator Symms wanted to be
22 heard on that, and Senator Symms is here.

23 Senator Symms. Mr. Chairman, maybe if I could ask Buck
24 a question, he could explain to the committee just exactly
25 what it is, briefly, that the Treasury is proposing to do,

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1 and then maybe I would have a question from that.

2 Mr. Chapoton. All right.

3 The proposal relates to the problem not by any means
4 limited to the mining or reclamation costs but any number
5 of costs that will not be incurred for several years, but it
6 can be two or more years after the end of the taxable year
7 under current law, if the all-events test has been complied
8 with.

9 Senator Symms. The law of what?

10 Mr. Chapoton. All events. All events have occurred
11 prior to the end of the taxable year, from which one can
12 determine both the amount of the liability, the amount of the
13 cost or the expense, and the fact that the liability for that
14 expense has occurred by year end. Then, under the general
15 rule now, it is deductible.

16 What we are now seeing are a lot of expenses that
17 arguably meet the all-events test but will not be paid and
18 no economic performance will take place and no payment will
19 take place until several years after the event.

20 A major one we saw is nuclear decommissioning costs for
21 a nuclear facility, and the costs can be estimated now with
22 some degree of accuracy, clearly are liable to incur those
23 costs later but they won't be paid until 25 or 30 years
24 later; but the taxpayer, nevertheless, if it is going to cost
25 \$10 million to decommission the plant 30 years, would claim

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1 a \$10 million deduction right now.

2 I think anybody who looks at the problem reasonably
3 understands that \$10 million due 30 years from now is not
4 the same as a \$10 million deduction now. In other words, a
5 deduction of far less than \$10 million would be correct to
6 justify that \$10 million expense incurred 30 years later.

7 So, the question is whether you have overstated the
8 value of the deduction. A conceptually sound basis would be
9 to discount that \$10 million back by 30 years. And we looked
10 at the possibility of discounting the deduction, but we
11 run into very difficult administrative problems in doing so.

12 So our proposal has been that no deduction occurs until
13 economic performance takes place. And example would be 30
14 years later. We think that reaches the proper economic
15 result, but conceptually I will say again that one could
16 construct a sound basis for a discounted deduction currently
17 for an expense to be paid later.

18 Senator Symms. This isn't going to set any kind of,
19 or does this in any way set any kind of or establish a new
20 concept of the way we interpret law like on charging people
21 taxes before they have earned the money? That is what I'm
22 getting at.

23 Mr. Chapoton. No. It would add a new element, a new
24 factor, to the all-events test. That factor would be that
25 economic performance would have to occur. But I think I would

1 be correct in stating that under general accounting
2 principles that economic performance would be a factor under
3 those principles now.

4 But I don't want to underestimate the impact of this
5 proposal on the decommissioning facility. And I think under
6 mine reclamation expenses the IRS argued that they did not
7 meet the all-events test under prior law; they won some
8 cases. And they would be deferred their deduction until the
9 reclamation took place.

10 Senator Matsunaga. Mr. Chairman?

11 The Chairman. Senator Matsunaga.

12 Senator Matsunaga. Under the existing law you may
13 carry back three years.

14 Mr. Chapoton. Correct.

15 Senator Matsunaga. Under your proposal, this proposal,
16 how far could you go back?

17 Mr. Chapoton. For these types of expenses, you could
18 carry back 10 years.

19 Senator Matsunaga. Ten years. Despite the fact that
20 you allow a carryback of 10 years, you would still have --
21 let's see -- a 1.9 gain over the next three years?

22 Mr. Chapoton. Yes. Of course the carryback, the revenue
23 impact of the carryback wouldn't show up on these sheets
24 until the economic performance had occurred in the future
25 year.

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1 Senator Matsunaga. Well, will this mean that after
2 the third year we will suffer loss in revenue?

3 Mr. Chapoton. No. The effect of this is deferring
4 deductions. We want to make sure the deductions are fully
5 available when they are claimed, but it means that the
6 deduction is in later years.

7 No, it would not be a loss, but it would shift the
8 year of the deduction.

9 Senator Matsunaga. And how will you define "economic
10 performance"?

11 Mr. Chapoton. Well, we mentioned in our general
12 explanation examples of that, but I think we would do it by
13 regulation and by committee report. But generally, if you
14 are talking about workmen's compensation, it is when the
15 workmen compensation claim is paid. If you are talking about
16 mine reclamation expense, it is when the mine is in fact
17 reclaimed. It is when the work is done for which you are
18 paying.

19 Senator Matsunaga. All right. Thank you.

20 The Chairman. Are there any further questions on this
21 section?

22 (No response)

23 The Chairman. Without objection, then, we will agree
24 to that.

25 That will leave prepayment, which we are still working

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1 on in that one area in related-party transactions.

2 Let's move on to the next group.

3 Mr. Chapoton. Is that the corporate reform?

4 The Chairman. Right. As I understand -- what is the
5 one area there that may be difficult?

6 Mr. Chapoton. The one area is the ordinary distribution
7 of appreciated property. I believe that is the area we
8 heard some concern expressed about.

9 The Chairman. Is there any question on the leveraged
10 dividends? As far as I know there was no question raised on
11 that.

12 Mr. Chapoton. No, I do not know of any concern. Well,
13 I do not want to overstate that, Mr. Chairman; I am not
14 sure any members have raised a concern about that. We wanted
15 to make it clear that this provision would disallow the
16 interest deduction if a debt is incurred directly connected
17 with the purchase of stock. Then the interest deduction is
18 disallowed to the extent that the corporate owner of that
19 stock receives 85 percent dividends-received deduction. In
20 other words, he will not get both the dividends-received
21 deduction and the interest deduction.

22 We have been careful to make it clear that the cases we
23 are covering are only there where there is a direct
24 relationship between the borrowing and the purchase of stock.
25 We are not talking about an allocation rule where you simply

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1 other debt and also purchase stock.

2 The Chairman. Without objection.

3 What about the next one, short sales?

4 Mr. Chapoton. That is designed simply to make it clear
5 that you would have to hold the short sale open for 16
6 days, or the payments in lieu of dividends would not be
7 deductible. The point is to have some economic risk in the
8 short sale transaction to prevent using short sale
9 transactions from getting ordinary deductions on one side
10 and capital on the other.

11 The Chairman. As far as I know, there is no objection
12 to that.

13 Mr. Chapoton. I have not heard any.

14 The Chairman. Without objection.

15 Would the Moynihan Amendment fit in at this point?
16 Maybe we will finish these and come back to the Moynihan
17 Amendment. Are you prepared, Jim, on that one?

18 Mr. Wetzler. Well, we've got the revenue estimate on
19 Senator Moynihan's suggestion.

20 The Chairman. Well, why don't we do that now.

21 Mr. Wetzler. And on both the leveraged purchases of
22 Treasury Bills and leveraged purchases of market-discount
23 bonds, that would be about .6 over the three-year period --
24 600 million.

25 Senator Moynihan. That's the one we did this morning.

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1 Mr. Wetzler. Yes.

2 Senator Moynihan. I think the Chairman is talking about
3 the alternative minimum tax.

4 The Chairman. No, I think they were going to combine
5 your idea plus Mr. Wetzler said if we didn't do the other
6 we might escape.

7 Senator Moynihan. So then we have combined them?

8 Mr. Wetzler. Yes. This is the market discount and the
9 Treasury bills.

10 Senator Moynihan. Right. Well, I would move we accept
11 that, Mr. Chairman, if the Treasury approves it.

12 The Chairman. Does the Treasury have any problem with
13 that?

14 Mr. Chapoton. No, but maybe we should discuss whether
15 there is any transitional problem there.

16 Senator Moynihan. Mr. Chairman, there have been persons,
17 as in the case of the commodity tax straddles, that asked
18 if there could be a period of transition, because as it
19 frequently turns out there has been a lot of this going on,
20 and a lot of taxes would suddenly be owed. Could we have a
21 two-year transition or something like that?

22 Mr. Wetzler. Senator Moynihan, we were thinking of the
23 same five-year rule that was done in 1981 for commodities
24 tax.

25 Senator Moynihan. What about the same five-year rule,

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1 then we will have a certain uniformity and predictability?

2 Mr. Chapoton. That would be fine with us.

3 The Chairman. That is satisfactory to the Treasury?

4 Mr. Chapoton. Yes, sir.

5 The Chairman. All right, then.

6 Senator Matsunaga. What item are we talking about now?

7 The Chairman. It was an item we discussed this morning
8 that is not on the list. It is one that Senator Moynihan
9 had suggested earlier and the Joint Committee suggested that
10 there were probably two facets to it. I don't know how you
11 describe it. If you wanted to write it in there, how would
12 you describe it, Jim?

13 Mr. Brockway. Market discount and T-Bill straddles.

14 Mr. Chapoton. It is a straddle transaction involving
15 those two aspects.

16 The Chairman. All right. Let us go on to extraordinary
17 dividends.

18 Mr. Chapoton. All right. That number C, Mr. Chairman,
19 that is simply dealing with the problem where a corporate
20 shareholder will buy stock before an extraordinary dividend
21 and not report any gain on the dividend but create a loss in
22 his stock as a result of the dividend and claim a loss.

23 This says that if you don't hold the stock for at least
24 a year on which the dividend is paid, then the basis in the
25 stock is adjusted downward so you don't get to report a loss

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1 on the sale of the stock.

2 The dividend is what made the value of the stock drop,
3 and we are just saying that the basis would be adjusted
4 downwards. So you wouldn't get the loss on the sale of the
5 stock.

6 The Chairman. Without objection.

7 Mr. Chapoton. All right.

8 Now, the number 2 there on page 4 is the one that some
9 question has been raised about, the ordinary non-liquidating
10 distribution of appreciated property. That is the case where,
11 under existing law, a corporation has appreciated property
12 and uses that property to redeem its stock. Then the
13 corporation, unless it falls within one of the exceptions,
14 recognizes gain on the transaction.

15 We are proposing that that same treatment be accorded
16 where the property is not used to redeem the corporation
17 stock but is simply an ordinary dividend distribution to its
18 stockholders.

19 The corporate tax applies if the corporation sold the
20 asset, and we are saying the corporate tax ought to apply if
21 it is a nonliquidating distribution and it distributes this
22 property to shareholders.

23 Senator Bentsen. Mr. Chairman, I would like to speak
24 on this one, because I have some concern about this. I really
25 don't know why it is in the package; it's a revenue loser, and

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1 we are trying to raise revenue. What you are going to do is
2 trap appreciated property within a corporation.

3 The other point I would like to make is, when you get
4 into some of these instances where you have someone trying
5 to force that kind of a distribution, and we have seen a
6 number recently, I think it serves a rather useful purpose
7 in reminding some of these corporate presidents who really
8 owns the company, that it's the shareholders that own that
9 company.

10 Now, this is a very complicated situation that we are
11 talking about doing here, and raise no revenue by it.
12 Actually, you are going to lose revenue. And I think in the
13 long run you will lose more than the estimates that you
14 are talking about.

15 Let me refer to what Secretary of the Treasury Ronald
16 Perlman said when he was talking about this type of thing
17 in October of 1983, when he said, "We wish to emphasize, the
18 scope of these proposals is enormous. They would make
19 fundamental changes to the rules that govern the most basic
20 as well as the most intricate corporate transactions, some
21 of which have been in the law since 1918. The proposal
22 would affect to some degree every corporation and every
23 shareholder.

24 "Accordingly, we strongly believe that adoption of
25 these proposals should come only after they have been

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1 translated into specific statutory provisions subjected
2 to deliberate and detailed, technical and policy analysis
3 by all interested parties."

4 I think that is true. I think you are getting almost
5 in the sling of the stepped-up basis fight that we went
6 through on estate taxes.

7 So I would frankly think that this provision, which
8 brings in no revenue, which loses revenue, that we ought
9 to defer that. We have a corporate reform study going on
10 now, and I would like to see hearings on this and a deferral
11 until that period of time.

12 We are fighting like the devil to raise money here, and
13 to come in with one that loses money, that hasn't had that
14 kind of attention and the kind of hearings I think it should
15 have, I really think is a mistake.

16 Mr. Chapoton. Well, Senator Bentsen, we, of course,
17 estimate that it does raise money. We have heard the
18 argument from some on the other side that they don't think
19 it will have that impact.

20 But let me back up just a minute. Mr. Pearlman's
21 statement, by the way, was talking about the proposal that
22 was being considered by the committee staff and others on a
23 very broad revision of the corporate taxation, and in
24 particular the overruling of the so-called "general utilities
25 doctrine" that would cause any asset that comes out of

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1 corporate solution, whether by liquidation or otherwise,
2 to be taxed at the corporate level.

3 Now, we reviewed that and decided not to go forward with
4 that. This is a very targeted proposal which simply says,
5 "If you are doing business in corporate form and you are
6 going to continue to do business in corporate form, then
7 an attempt to remove part of the assets of an ongoing
8 business from the corporate solution will not escape the
9 corporate tax.

10 Senator Bentsen. You backed away from the other because
11 you saw too much broadbased opposition, and you thought if
12 you came in in a more narrow scope that it might not arouse
13 that concern.

14 I still think it's a serious mistake, and I can't
15 believe that you will not have anything but a loss of
16 revenue, because people are just not going to make the
17 distributions under that kind of a basis.

18 I would strongly urge that we defer it until we do
19 have hearings on this particular one.

20 Mr. Symms. Would the Senator yield on a question?

21 If I could just ask a further question, Senator Bentsen,
22 what you are talking about is, if a corporation has assets
23 and wants to, say, set up a royalty trust, for example, then
24 the management would be more accountable to the stockholders
25 and to the country, and it would really allow for a more

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1 efficient operation.

2 Senator Bentsen. Well, I am not going to argue that
3 point, frankly, Senator, because I don't think it ought to
4 be just royalty trusts; I think that that ought to apply
5 across the board. They are just not going to take the steps.

6 And the other thing that you have, when you get into
7 some of the large corporations you get management that
8 really often is not responsive as it should be to
9 stockholders. And I think you ought to be in a position where
10 those concerns can be brought to their attention, and this
11 avenue allows some of it.

12 Senator Symms. Well, I agree with you, but let me ask
13 the question the other way. Let's say somebody has a
14 packing house and a production like an orchard, and they
15 want to take the orchard and put it into different
16 ownership. This would disallow this, if I understand it
17 correctly.

18 Mr. Chapoton. Take the orchard and put it into -- ?

19 Senator Symms. Say they want to put the orchard --

20 Mr. Chapoton. If they sell the orchard they pay tax.

21 Senator Symms. What if they want to have the
22 stockholders own the orchard separately and lease it back
23 to the parent company?

24 Mr. Chapoton. That would be a similar situation, or
25 the royalty trust would be a similar situation; that is, they

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1 are trying to remove this asset from corporate solution
2 but frankly still have the benefits of using it in the
3 corporate solution, and avoid the tax at the corporate
4 level.

5 Senator Symms. Well, no. What we are talking about is,
6 let's say for example that you have a company that is
7 integrated, that has basic production and processing.

8 Mr. Chapoton. Right.

9 Senator Symms. And I don't care what the product is.
10 And the people, some of the stockholders, would like to own
11 the land that let's say the potatoes or the apples or
12 whatever is produced comes from. This would disallow this,
13 if I understand it correctly.

14 Mr. Chapoton. Well, let's back up.

15 If they want to liquidate the corporation, they --

16 Senator Symms. They don't want to liquidate it; they
17 want to put the value out there and have a partnership own
18 the land, or something.

19 Mr. Chapoton. Well, that's correct. We have a
20 corporate tax. They cannot do that, for example, Senator
21 Symms, by redemption of stock. We have a corporate tax
22 system, whether we all agree whether it is a sound tax or
23 not. We now have one. If you say that by having a dividend
24 of property out that you can remove inventory, for example,
25 from the corporate tax system, then you can obviously reduce

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1 the corporate taxes in that method.

2 It is income -- the point is, it is income that was
3 earned by appreciation or by changes in value while it was
4 owned by the corporation.

5 Senator Symms. What you want to do is tax the transfer,
6 though.

7 Mr. Chapoton. That's correct.

8 Senator Symms. Of the assets.

9 Mr. Chapoton. That is correct.

10 Senator Symms. So then, what you are doing is building
11 in intransigent management maybe of a giant corporation,
12 where the stockholders really can't run the corporation.
13 That is the point the Senator is making.

14 Mr. Chapoton. Well, it's true that an attempt to
15 dividend out property would be subjected to a corporate tax.
16 You would not have that route to avoid corporate tax on
17 the appreciation that had occured while the asset was in the
18 corporation.

19 I would like to say in response to one thing
20 Senator Bentsen said: We never did, Senator, endorse the
21 broader proposal. It wasn't in response to any criticism.

22 Senator Bentsen. There were a number of them that
23 tried to propose.

24 Mr. Chapoton. There were other proposals out, and we
25 didn't like some of the other proposals. We did like this

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1 one, because it does seem to us to be a hole in the
2 corporate tax system.

3 The Chairman. Let us at least defer it for now, along
4 with the other things we have deferred. If there is no
5 way to resolve it, we will just have to vote on it.

6 Mr. Chapoton. All right.

7 Number 3, Mr. Chairman, is a very technical provision
8 that simply says that the present law treatment, with respect
9 to transfers of partnership interests where they recapture
10 assets or the like in the partnership, that those rules
11 cannot be avoided if the partnership interest is held in a
12 corporation. And I don't think there is any criticism of
13 this at all. A lot of people thought this was current law.

14 The Chairman. Is there any objection to that?

15 (No response)

16 The Chairman. If not, agreed to.

17 Senator Mitchell had a question on one we had gone
18 over.

19 Senator Bentsen. Well, I think that last one is a
20 clear loophole and it has to be plugged.

21 Mr. Chapoton. Yes, sir.

22 Senator Mitchell. Thank you, Mr. Chairman.

23 I apologize for not having been here earlier, but I
24 wanted to go back to item F on the previous page, "premature
25 accruals," and ask Mr. Chapoton whether there was any

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1 discussion of the peculiar problem that nuclear power
2 plants would face in terms of the decommissioning costs.

3 Mr. Chapoton. Yes. There has been a good deal of
4 discussion on that on the House side, Senator, and they are
5 attempting on the House side to work out a system for a
6 discounted deduction in the early years, trying to arrive
7 at a present value of the future cost and then spreading
8 that deduction over the life of the nuclear facility.

9 Senator Mitchell. I think it is important that we do
10 something here as well, Mr. Chairman; as a part of a broader
11 public policy we are seeking to encourage nuclear plants to
12 make a provision for decommissioning. And of course most of
13 the States which have them, as mine does, and the public
14 utility commissions in those States are attempting to
15 devise plans to do that.

16 Were we to adopt a provision such as this without
17 taking that into account, I think we would be defeating what
18 is very much in the national interest in a much broader
19 sense than which we are dealing here.

20 Mr. Chapoton. Well, when the details of that are
21 worked out, and I think they are very nearly worked out, we
22 would have no objection to that.

23 Senator Mitchell. Thank you, Mr. Chairman.

24 The Chairman. All right.

25 Next is the investment companies.

1 Mr. Chapoton. Mr. Chairman, this is simply a rule
2 that says you do not avoid the accumulated-earnings tax
3 simply because the company is widely held. If the principal
4 purpose for failure to pay a dividend is avoidance of tax,
5 then the accumulated-earnings tax rules would apply.

6 The Chairman. Without objection it will be agreed to.

7 Mr. Chapoton. The 4-B, the capital gains dividends for
8 mutual funds: The present law, 30-day rule, would be
9 expanded to six months. It is another rule requiring
10 economic risk before the tax benefits resulting from a
11 capital gain dividend may be achieved.

12 The capital gain dividend otherwise would give a tax
13 benefit for a very short holding period.

14 The Chairman. Without objection, it will be agreed to.
15 Collapsible corporations?

16 Mr. Chapoton. Number 5 deals with the taxation of
17 assets to foreign corporations. The purpose of this
18 proposal is to clarify what the rules will be when a U.S.
19 company transfers assets abroad, to make the rules clear
20 enough so that rulings do not have to be obtained on very
21 case. And in addition, to apply a rule, a clear rule, for
22 taxing of transfers of intangible assets abroad. That would
23 be a tougher rule than existing law; so that if a company
24 develops a patent, for example, in this country and takes
25 deductions in the development of the patent, and then

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1 transfers that patent abroad, this rule says that if the
2 company does not want to pay tax on the transfer at the then
3 fair market value of the patent, then it has to agree to a
4 deemed royalty payment from abroad back to the U.S., so that
5 the income would not escape entirely the U.S. tax. A
6 portion of the income would be taxed here.

7 The Chairman. What is the revenue impact of that?

8 Mr. Chapoton. The revenue impact is below \$50 million
9 a year. I understand from the Joint Committee that the
10 revenue estimate is being revised and that there is going
11 to be a more positive revenue estimate on their standpoint.

12 There has been a lot of drafting on this proposal in
13 the last several days.

14 The Chairman. Well, on a tentative basis if there is
15 no objection, we will approve that provision.

16 Senator Chafee. What is the revenue impact? I didn't
17 get that.

18 The Chairman. Fifty million, but they are now revising
19 that.

20 Mr. Chapoton. Less than \$50 million a year now, but
21 there is thinking -- it is a problem we have been worried
22 about, Senator, for some time. That is, where an intangible
23 is developed here, expenses are taken against U.S. income, and
24 then it is transferred to a low-tax country so that the income
25 from the patent or know-how is not later taxed. And we

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1 think this is finally a clean-up to that problem. And we
2 do not show significant revenue. The Joint Committee
3 advises me that they are showing more revenue than we are
4 on this.

5 The Chairman. All right.

6 Mr. Chapoton. A related foreign corporation matter is
7 dealing with the so-called "McDermott Case."

8 The Chairman. Which one is this?

9 Mr. Chapoton. This is number 6 on page 5.

10 The Chairman. What is it on this sheet?

11 Mr. Chapoton. It is the last item, "Decontrol of
12 Controlled Foreign Corporations."

13 It was simply an attempt by a U.S. company to transfer
14 ownership of the U.S. company to a foreign subsidiary, so
15 it became the subsidiary rather than the parent. And if it
16 resulted in it being a foreign company, the Controlled
17 Foreign Corporation, the subpart F rules didn't apply. And
18 this is an attempt to deal with that, to say that transaction
19 at least when it is entered into would result in tax
20 liability to the U.S. company. They simply found a way
21 that people didn't realize they could avoid that tax.

22 The Chairman. That has a revenue impact, but a minimal
23 impact.

24 Mr. Chapoton. That has a minimal impact.

25 The Chairman. The last one, Decontrol of CFC's.

1 Mr. Chapoton. And that completes our package.

2 The Chairman. If there is no objection, in that
3 particular group, then, we have deferred action on ordinary
4 distribution of appreciated property; we have tentatively
5 agreed to the other provisions. Obviously, if somebody
6 who was not present wants to raise a question, that is
7 certainly appropriate.

8 On the accounting abuse group, the related-party
9 transactions, there is still one provision in that -- Senator
10 Heinz, with reference to low-income housing.

11 Prepayments? I understand there is an effort to work
12 out some resolution of the problem raised by Senator Boren
13 and others.

14 And then in the first group -- wait a minute; there
15 is also the premature accrual. I think Senator Mitchell
16 and Senator Wallcp still have outstanding reservations.

17 The first group, being contributions of property, let's
18 see. I wasn't here when that was objected to.

19 Mr. Chapoton. I don't think there was an objection.

20 The Chairman. I guess Senator Durenberger is on the --

21 Mr. Chapoton. Oh, on the charitable problem, the
22 three-year rule for gifts to charities.

23 Senator Moynihan. That was involved with the
24 President's Commission on the Arts.

25 The Chairman. Has that been resolved, Senator

1 Durenberger?

2 Senator Durenberger. I think it has been resolved in
3 this committee. We were just giving Treasury a chance to
4 add, if they would, to the proposal we had made. I think
5 the votes are here if we want to approve my proposal.

6 Mr. Chapoton. We have not had a chance to consider the
7 impact. As I understand it, the proposal, Senator
8 Durenberger, would strengthen the potential penalties on
9 appraisals.

10 Senator Durenberger. It sets up an appraisal process
11 that is very clear, and it provides a substantial enough
12 penalty so as to discourage people from not using the
13 appraisal process.

14 The Chairman. Why don't we give Treasury some time to
15 look at that.

16 Senator Moynihan. Mr. Chairman, I think we have a nice
17 combination of things. We are going to encourage giving and
18 discourage fraud, but giving. And we will be back
19 tomorrow?

20 The Chairman. I'm afraid so.

21 Senator Moynihan. All right. Let's not let that
22 pass by.

23 The Chairman. It may not be quite that way, but
24 hopefully it will be.

25 Now, did we approve the item in the first group,

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1 straddles? Was that discussed this morning? I had to leave
2 the room temporarily.

3 Mr. DeArment. As I understand it, that is a duplication
4 of what we have in 2062.

5 The Chairman. Oh, that is the same provision?

6 Mr. DeArment. That's right.

7 The Chairman. Does that include the language that I
8 recommended be included at that time?

9 Mr. DeArment. No. As I understand it, Buck, you have
10 straddles listed here under your tax shelter proposals. As
11 I understand it, those are the stock option straddle rules
12 that we included in 2062.

13 Mr. Chapoton. That is correct, but I think we have a
14 few different proposals. Let me get this in my mind.

15 (Pause)

16 Mr. Chapoton. I think the major difference we have
17 in our proposal from 2062 is dealing with options, market
18 makers. We are proposing that professional market makers
19 on both the securities and commodity options would be
20 required to use the market-to-market system, but with not a
21 60-40 rate, but with a full tax rate. And I am not certain,
22 Rod, how you handled market makers in 2062.

23 Senator Moynihan. We would like to talk about that,
24 Mr. Chairman.

25 Mr. Chapoton. Market makers were not dealt with in

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1 2062, and we are proposing that market makers be dealt with.

2 Senator Moynihan. Let's see. There have been two
3 questions raised about, first, the idea of a level playing
4 field for options which have an underlying equity basis;
5 and then the question of what do you do with the market
6 makers.

7 Mr. Chapoton. I think we are talking about that whole
8 area now.

9 Senator Moynihan. Mr. Chairman -- and please correct
10 me, any and all -- I believe that, and Senator Bradley and
11 I are concerned here, the first is the question that options
12 with respect to underlying equities indexes be taxed
13 equally.

14 I believe somewhere in our bill as reported there is a
15 provision that gives the 32-percent rate to such options
16 on the futures markets but leaves it at 50 percent for such
17 options on the regular markets. And I think it is our
18 proposal on the level-playing-field principle that it should
19 be 50 percent for either. It could be 32 percent, but I
20 don't think the Treasury would find that agreeable. Is
21 that right?

22 Mr. Chapoton. Senator Moynihan, you are talking about
23 options on commodity futures and options on stock?

24 Senator Moynihan. On stock futures, the indexing.

25 Mr. Chapoton. Oh, options on stock indices?

1 Senator Moynihan. Yes, sir.

2 Mr. Chapoton. I think your proposal or the industry
3 proposal would go market-to-market at a 60-to-40 rate. Is
4 that your proposal?

5 Senator Moynihan. I believe our proposal is that it
6 should be market-to-market and a 50 percent rate in all
7 exchanges.

8 Is that correct, Senator Bradley?

9 But we don't want a different rate in different
10 exchanges.

11 Mr. Wetzler. Senator Moynihan, the situation is that
12 the committee's bill that reported last Fall treats options
13 on futures contracts like futures contracts. And a concern
14 has been brought up that that leads to two essentially
15 identical products having different tax treatments.

16 Senator Moynihan. That is right.

17 Mr. Wetzler. The Treasury in its budget has proposed
18 resolving this problem by treating options on futures
19 contracts like options, which would put everybody on a
20 so-called "level playing field."

21 A group of industry people have been working with the
22 Ways and Means Committee staff on a somewhat different
23 proposal, which would try to resolve the level-playing-field
24 question by keeping options on futures like futures
25 contracts, and then treating some options, actually a lot of

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1 options, as futures contracts as well, subjecting them to the
2 market-to-market rules.

3 Senator Moynihan. I would like to have Mr. Wetzler's
4 view on this, Mr. Chairman, and of course Mr. Chapoton's;
5 but I will stop just by saying that it seems to me our
6 proposal is simple, understandable, uniform, and in that
7 sense --

8 The Chairman. I think what we might suggest, then, it's
9 another area we ought to flag. There is a difference of
10 opinion. We have had some discussion with some of the option
11 people at the staff level, and I know the Joint Committee
12 has and Treasury has, and both Senator Bradley and
13 Senator Moynihan have. Maybe we can all work together to
14 see if we can resolve this.

15 Senator Bradley. Mr. Chairman, I think that some of
16 the things that were said are in the direction we would like
17 to go, and I think that we could work it out.

18 Mr. Chapoton. I would just say, Mr. Chairman, that I
19 think we should discuss it. Our concern has been moving to
20 a lower rate of tax on another type of security instrument.
21 And we conceded -- we went down that way quite far in 1981
22 when we went to a 32-percent top rate for commodity future
23 transactions. But I think the tendency to bring everything
24 closer to that is something we are not going to be too keen
25 on.

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1 Senator Moynihan. Mr. Secretary, you have heard me say
2 that I agree with you.

3 Mr. Chapoton. But I thought you were talking about a
4 50-50 rate, were you not?

5 Senator Moynihan. A 50-percent rate as the normal
6 rate.

7 Mr. Chapoton. Oh, a 50-percent rate?

8 Senator Moynihan. Yes.

9 Mr. Chapoton. Well, we agree with that very definitely.
10 That would just be the normal rate of tax. That's fine.
11 And then I think if we go that way, that would clear up
12 all sorts of problems.

13 Senator Moynihan. No. Well, options; but options
14 where the underlying product is an equity as against a
15 commodity. Is that clear? Am I making it clear?

16 The Chairman. Well, it may not be.

17 Mr. Chapoton. Well, I think that would be fine, but
18 I think maybe we should discuss how you treat other options --
19 options on T-bills and things like that.

20 Senator Moynihan. All right. But we are pretty close
21 to agreement here, aren't we?

22 Mr. Chapoton. I think so.

23 Senator Moynihan. Fine.

24 The Chairman. Rod?

25 Mr. DeArment. Mr. Chairman, you had talked about or

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1 asked about this language on our report on regulated futures
2 litigation. That's not in 2062, and it would probably be
3 appropriate to put it in along with this other language about
4 options. It basically requires the Secretary of the
5 Treasury to report to this committee and to the Ways and
6 Means Committee with respect to the progress made by the
7 Treasury Department and the IRS in reducing the backlog of
8 cases involving the tax treatment of certain regulated
9 futures contracts.

10 The Chairman. I think that reporting date is July 1.

11 Mr. DeArment. That is correct, July 1, 1984.

12 The Chairman. It may be a little early yet.

13 Mr. Chapoton. July 1 of 1984?

14 The Chairman. Right. It may be a little tight.

15 Mr. Chapoton. A little tight.

16 Mr. DeArment. Well, we could shift that date back to
17 maybe September 1st.

18 The Chairman. October 1 or something.

19 Mr. DeArment. October 1?

20 Mr. Chapoton. That would help.

21 Mr. DeArment. All right.

22 The Chairman. All right. As I understand now, except
23 as I said there may be other matters raised by members who
24 could not be present, we will, hopefully between now and
25 tomorrow or Thursday, negotiate some of these areas with

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1 Senator Boren and Senator Bentsen, Senator Moynihan, and
2 Senator Durenberger. But I think for the most part we
3 probably tentatively agree to about \$11.5 billion over
4 a three year period in the Treasury's tax reform list. Is
5 that about right, Buck?

6 Mr. Chapoton. I think that's right. Let me just check.

7 Senator Bradley. What was that number again,
8 Mr. Chairman?

9 The Chairman. I just guessed about \$11.5 billion.

10 Mr. Chapoton. That's right. The items on which we
11 have reserved are not for the most part significant in money.
12 The only one that might be is the premature accrual. The
13 low-income housing? It is hard to say what that would be in
14 the package. The ordinary distribution of appreciated
15 property is not significant. The charitable contribution
16 is not significant. So I think it would be close to the
17 \$12 billion that we would be seeing.

18 Senator Boren. Mr. Chairman, may I make just a comment?
19 I raised an issue right before we broke for lunch relative to
20 related-parties issue. I don't want to hold the committee
21 up at this time. This relates to a transition rule, and I
22 am just hopeful that we can work with the group here on this.

23 The Chairman. Did you call that to their attention
24 today?

25 Senator Boren. Yes. I think we have had some

1 discussions informally about it during the noon hour.

2 Mr. Chapoton. Yes, I am told that we think we can
3 work that out.

4 Senator Boren. Thank you.

5 Senator Bradley. Mr. Chairman, if I could. I don't
6 want to rain on the parade here, but I think I really should
7 point out that I think all of these things, while they are
8 attempts to close the various loopholes, that the very act of
9 changing the regulation will simply require another set of
10 regulations. And I seriously question whether we are going
11 to have any real net revenue gain after the tax lawyers get
12 a hold of the new set of regulations and devise the new
13 loopholes.

14 My point here is simply to say what I think is
15 obvious to the Chairman and to anyone else, which is:
16 Unless we are going to confront the basic issues, we
17 are going to be nibbling around the edge of tax reform.
18 I mean, you can go down and pick almost at random, you know,
19 "Dividend distributions of appreciated property," and
20 "Noncorporate shareholders" -- unless we are going to deal
21 with basic questions like deferral, capital gains, and a
22 variety of others, we are going to be nibbling around the
23 edges.

24 I hope at some point -- and I look to the Chairman for
25 some help and leadership on this issue -- we might actually

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1 move in the direction of a reform proposal where we will
2 close loopholes as opposed to just shifting regulations and
3 complexity until yet another year when we will be back in
4 here again talking about the same regulations and the
5 same complexity, saying we are going to reform those only
6 to create yet another set.

7 So, I felt that at some point we will probably make
8 this point again in the course of the year, but I think that
9 it is one that the Chairman fully understands and I think
10 is sympathetic with.

11 I think for us to call this "a major tax reform
12 package" is probably not right, given the increasing
13 complexity that it will require.

14 The Chairman. Which would lead us to the proposal that
15 Senator Moynihan had. We thought we might discuss it
16 following this, because it touches on the very point made by
17 Senator Bradley.

18 I am not totally familiar with the proposal, but I
19 understand the Joint Committee is prepared to discuss the
20 Moynihan proposal, which is sort of a broad attack on
21 shelters. It may be controversial, so maybe we should.
22 Do you want to discuss that now, Pat?

23 Senator Moynihan. Well, fine, if that is agreeable.

24 Mr. Chairman, I can say what I have to say very shortly.
25 But I have some information here which we have just put

1 together, which I think should get the attention of this
2 committee:

3 In 1982, there were 269,000 persons who paid the
4 alternative minimum tax -- 269,260. This raised \$855
5 million, or about \$3100 per person. And if you simply
6 figure that \$3100, with 20 percent of the amount of income
7 they declared above \$40,000, you will end up -- simple
8 arithmetic will tell you -- that the marginal rate of
9 taxation for these 269,000 persons was 5.5 percent. That
10 is the marginal rate at which they paid tax.

11 Now, there is just something not working here.

12 The main thing that is not working, as we understand
13 it, and this is going to grow and is growing, is that
14 persons paying this alternative minimum tax, even though
15 they have large incomes above \$40,000, can offset that
16 income against paper losses incurred in tax shelters. And
17 they have every reason to do so, and with obviously some
18 success do so, and these are the people that bring our
19 system into dispute and will soon bring it into disrepair.

20 The proposal that we offer you says, simply, that you
21 cannot offset income losses from a tax shelter entered into
22 solely for the purpose of acquiring tax losses; you cannot
23 offset that against your income for purposes of calculating
24 the alternative minimum tax. It could not be more simple.

25 What it means is, instead of chasing around after the

1 tax shelters, which as I said this morning in the House
2 committee is like betting your kidneys against a brewery --
3 you know, it won't work -- here is the opportunity to say
4 there is no gain from the tax shelter or not as much gain
5 if not no gain.

6 I think Mr. Wetzler is very much of the view that people
7 at that level of income should be paying a 50-percent
8 marginal rate, and we shouldn't be too much congratulating
9 ourselves if we get 20 percent. But to settle for 5.5
10 percent is unseemly.

11 The Chairman. Now the Joint Committee -- Dave, have
12 you gone over this proposal?

13 Mr. Brockway. Yes, Mr. Chairman.

14 Senator Chafee. Is there a proposal before us,
15 Mr. Chairman?

16 The Chairman. Well, it was just outlined.

17 Senator Moynihan. Yes, there is a bill introduced.

18 Mr. Brockway. There is a bill that Senator Moynihan
19 introduced earlier this week.

20 I understand that Senator Danforth is interested in a
21 very similar proposal. Basically what it says, for the
22 alternative minimum tax, which is a structure where you pay
23 that rather than the regular tax, it is a 20-percent rate
24 in excess of your income over \$40,000. So in effect it is
25 a 12 percent tax on the first hundred thousand dollars, and

1 16 percent on the next. So it is a low-level tax that you
2 must pay if you use too many preferences against your
3 regular tax.

4 What Senator Moynihan's proposal is, is basically
5 where you have losses on activities where you don't
6 materially participate in that activity. So it is either
7 a tax shelter, other investment loss, or an investment in a
8 building where you don't participate in the management. You
9 cannot use those losses to shelter your salary income or your
10 active business income or your interest and dividends. You
11 have to hold those losses aside.

12 It is similar to a limitation right now in the
13 alternative minimum tax on interest, which is limited to
14 investment income.

15 Senator Moynihan. Right.

16 Mr. Brockway. It is the same notion, and it is a
17 similar notion to what you have in the regular tax of
18 limiting capital losses to capital income. It is that type
19 of notion, where you have too large an investment or
20 passive loss -- passive business loss.

21 The Chairman. Have you reviewed this proposal, Buck?

22 Mr. Chapoton. No, Mr. Chairman, we have not. I have
23 seen similar proposals, but we would like to have an
24 opportunity to look at this.

25 The Chairman. But you don't have any predisposition one

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1 way or the other?

2 Mr. Chapoton. Well, it is another minimum tax, and
3 minimum taxes are certainly a tempting way to deal with
4 these problems, such as this that we are very worried about.
5 My only concern is that sometimes it is difficult to say
6 the ultimate effect of a minimum tax. You try to see where
7 it falls out, but it is sometimes very difficult to
8 anticipate. Let us look at this.

9 The Chairman. Do you have any figures, revenue figures,
10 from the Joint Committee on this?

11 Mr. Brockway. We are still trying to look at it. It
12 looks like it may be a significant revenue item; but there
13 will be a certain amount of trade-off with whatever you have
14 done so far, whether Senator Bradley is correct that people
15 are going to get around the regular rules, then this will
16 pick up relatively more money if those rules actually work
17 to prevent people from sheltering, then this would pick up
18 relatively less.

19 Senator Bentsen. But as I understand it, though, you
20 run into some practical problems. If you had someone that was
21 just on salary and had real cash losses that wiped out their
22 whole salary, they would still be subject to substantial
23 tax.

24 Mr. Brockway. As the proposal was introduced, if you
25 had salary and then a real cash loss from a passive

1 investment, you would not be able to use that loss against
2 your salary income for the minimum tax purposes.

3 Now, for the regular tax you cannot use that loss
4 against your ordinary income, either, if it is a capital
5 loss. If it is an ordinary loss, you can.

6 What we have suggested here is to make sure that if
7 there is any activity where you are materially participating,
8 you can also deduct that against your regular income.

9 Senator Moynihan. Where there is a real loss, that is
10 a real deduction.

11 Senator Bentsen. That isn't the way I understood it.

12 The Chairman. Senator Danforth?

13 Senator Danforth. Well, Mr. Chairman, I think this is
14 a very important course to pursue. We did this in 1982,
15 I guess, and I think it is a very, very good proposal that
16 Senator Moynihan has made.

17 He and I have been working on parallel tracks in this
18 regard, and I think that Jim Connelly of my staff and
19 Dave Brockway have been talking about also the possibility
20 of adding a couple of new tax preferences, one relating to
21 foreign income excluded under section 911 and the other the
22 ACRS deductions in excess of straight line depreciation.

23 Mr. Brockway. Senator Bentsen, I should also clear
24 up that, as the bill was introduced, if you had a cash loss
25 you would not be able to use it. If I understand

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1 what Senator Moynihan says, as he would have this work out,
2 if you did have a cash out-of-pocket loss even in a passive
3 investment, you would be able to use that --

4 Senator Bentsen. But that isn't the way it was
5 introduced.

6 Mr. Brockway. That is correct.

7 Senator Bentsen. That is the point I am trying to make.
8 I am very sympathetic to his objective; I just want to be
9 sure we fully understand it and have thought it through,
10 because it is a very far-reaching thing that he is proposing.
11 And I want to be sure that we don't wipe out the fellow
12 that is making \$30,000 a year and has a true cash loss, and
13 then tell him he has to pay a 20-percent tax in addition,
14 which gets crazy.

15 So, we have found the one problem, and it is corrected;
16 but let's be sure we have thought through the rest of them.

17 The Chairman. Senator Bradley?

18 Senator Bradley. And as we head in this direction,
19 and I think both of the Senators were kind of heading in the
20 right direction, we might consider sweeping even more into
21 that base and lowering the rate, so that you might get a
22 little something in this process in addition to the good
23 feeling that you are closing a loophole. I mean, you know,
24 that's the way we have tried to do it. I would say that
25 we could go even further and maybe get some rate reduction,

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1 too.

2 The Chairman. Well, I think it is good to have the
3 discussion, it may have a great deal of merit; but I would
4 hope the Treasury would take a close look at it, and we
5 might discuss it in more detail either tomorrow morning or
6 tomorrow afternoon.. Is that all right, Pat, since they
7 haven't had a chance as yet?

8 Senator Moynihan. Yes, sir. But, you know, this
9 could be a large enterprise and an important-one. It would
10 tell the world which way we are heading.

11 The Chairman. Now, I understand, Senator Moynihan, that
12 you have no objection to the amendment that Senator Long
13 proposed.

14 Senator Moynihan. No, Mr. Chairman. May I say it is
15 not a question of my objection. The Government of Puerto
16 Rico has said it is acceptable to it, and I am just here
17 as a voice for people who have no voice here.

18 The Chairman. David, do you have that amendment?

19 Senator Moynihan. Yes, sir, I believe he does.

20 Mr. Hardee. Yes.

21 The Chairman. Is there any discussion of the amendment?
22 It was with reference to the Puerto Rican rum problem.

23 Mr. Belas. Excuse me, Mr. Chairman.

24 The amendment would limit the amount or the use of the
25 cover-over, the rebates, to Puerto Rico of the excise taxes,

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1 to include only the direct costs of transportation to and from
2 Puerto Rico of the redistilled spirits, and not to include
3 any additional incentive to the U.S. participant.

4 The Chairman. It eliminates the subsidy, correct?

5 Mr. Belas. That is correct.

6 Senator Chafee. But in addition to all of that, didn't
7 we vote to end it at the end of --

8 Mr. Belas. That is correct. This is only for the
9 transition period ending June 30th of this year.

10 Senator Moynihan. This is for the next four months.

11 Mr. Belas. And after June 30th, the cover-over, the
12 rebate, would be limited to distilled spirits comprised of
13 92 percent rum originally distilled in either the Virgin
14 Islands or Puerto Rico.

15 Mr. Chapoton. Could I ask, are you saying after June 30
16 that the cover-over would apply to rum only?

17 Mr. Belas. That is correct.

18 Mr. Chapoton. All right. The cane neutral spirits
19 which is a minor activity in Puerto Rico would terminate as
20 of the end of this year, then?

21 Mr. Belas. As of June 30th, the end of the fiscal year.

22 Mr. Chapoton. At the end of this fiscal year. All
23 right. I was somewhat concerned. It is not in the same
24 class, I think, as the redistillation problem, but I think
25 I would certainly favor going to rum only so we avoid the

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1 problem that we discussed this morning recurring again.

2 I would point out that it is going to be considered,
3 I believe considered, a precipitous event by Puerto Rico
4 with respect to the cane neutral spirits, which as I
5 understand to be about 30 million or so a year and has been
6 for some time.

7 Mr. Belas. Mr. Chairman, I understand that this
8 amendment in toto, the committee's original proposal
9 agreed to this morning plus this amendment, has been passed
10 by the representatives of the Government of Puerto Rico, and
11 they understand it and agree with it.

12 The Chairman. It is my understanding the Governor has
13 indicated his agreement.

14 Mr. Chapoton. It is up to them.

15 The Chairman. Now, does the Treasury have any
16 additional proposals?

17 Mr. Chapoton. No, sir, we don't have any. We have
18 none that we are making at this time.

19 Mr. DeArment. One thing, Mr. Chairman, that we felt we
20 might raise relates to the Treasury's section 483 proposal.
21 It is really a transition question. This is where, by
22 manipulating the interest rate, you get an over-valuation
23 for purposes of the Investment Tax Credit in depreciation.

24 We would propose that for sales after the date of
25 committee action but before the effective date of the

1 Treasury proposal, section 483 could not be used to
2 calculate a tax basis which the IRS could show, by clear and
3 convincing evidence, that their current law, section 483,
4 would result in the basis in excess of fair market value.
5 That is to avoid a rush to market deductions far in excess
6 of fair market value.

7 Mr. Chapoton. I would certainly support that, and I
8 wonder if the committee report shouldn't contain a
9 no-inference provision that for prior law 483 was never
10 designed to allow taxpayers to claim an excess value on
11 assets and increased ITC.

12 So we ought to clarify it as of today, and have no
13 inference as to prior law.

14 The Chairman. All right. Without objection we will
15 do that.

1 The Chairman. Well, I think since we have virtually
2 completed the so-called reform package, we might spend a
3 little time, in other words, recess until tomorrow morning
4 at 10:00, but use this next hour if we can with a discussion
5 with Treasury with Senator Boren and other Senators who have
6 specific questions.

7 Is that all right with you, Buck?

8 Mr. Chapoton. Yes, sir. That's a good idea. We can
9 cover a lot.

10 The Chairman. And what we might do in line with the
11 suggestions this morning, if we can have a little summary
12 sheet tomorrow to indicate precisely what we have done on the
13 spending and revenue side. I think that would be very helpful
14 to all of us because we come and go in the committee.

15 And then maybe if somebody could fix up the blackboard
16 and put it on the blackboard. And then what can we start with
17 in the morning.

18 Senator Boren. Mr. Chairman, could we have a mark also
19 on which items are included in the President's budget?

20 The Chairman. Right. Indicate which the President
21 supported, I guess.

22 Senator Boren. Well, which ones, so we kind of know which
23 are net reductions of the deficit below the budget.

24 The Chairman. Oh, I see. Right.

25 Senator Moynihan. I think we start with the Domestic

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1 Energy Tax tomorrow morning, don't we?

2 The Chairman. I didn't have that in mind. But have you
3 got some items?

4 Mr. DeArment. There are some additional tax items. The
5 Tax Benefit Rule, the Telephone Tax, all those items that we
6 have listed below there.

7 The Chairman. All right. We can probably start with
8 those tomorrow. Maybe I can meet with staff to see --

9 Senator Baucus. Mr. Chairman.

10 The Chairman. Senator Baucus.

11 Senator Baucus. Mr. Chairman, I have to have an idea
12 here. We are talking about time value of money lost to the
13 government that is going through all of these reforms.

14 Apparently there is a bill in the other body that
15 addresses the time value of money lost by the government,
16 that is, the government's failure to timely deposit funds that
17 it receives in order to get interest and so forth, the
18 Gilman bill.

19 I wonder if perhaps the Treasury and the joint task
20 committee could look at that. Congressman Gilman estimates
21 that it saves I guess 40-some million dollars a year. It
22 just seems to me that we should look at that as well.

23 Mr. Belas. I tend to doubt it is in the committee's
24 jurisdiction.

25 Senator Baucus. Oh. Well, it's in Ways and Means. That

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1 is why we will supply that.

2 Mr. DeArment. There is self-jurisdiction. Indeed, we
3 have a proposal here derived from the Grace Commission
4 recommendations relating to the electronic transfer of
5 certain taxes, and I think that bears on the same subject
6 that you are raising.

7 Senator Baucus. Well, I have checked with the attorney.
8 It is within the jurisdiction of the committee.

9 Mr. DeArment. All right. Fine.

10 Senator Baucus. I don't know what the Grace Commission
11 proposal is, but it seems to me at least that is something
12 that the joint committee could attempt to look at.

13 Mr. DeArment. Yes.

14 The Chairman. Let's do that.

15 Have we got our \$7 billion yet out of the Grace
16 Commission report?

17 Mr. DeArment. No, Mr. Chairman, we have not.

18 The Chairman. Are we close? And is there \$7 billion in
19 the Grace Commission report?

20 Mr. DeArment. In our committee's jurisdiction, not --

21 The Chairman. Any jurisdiction.

22 Mr. DeArment. In anybody's jurisdiction? Surely in
23 everybody's jurisdiction there is.

24 The Chairman. Well, as I understand the problem, it is
25 that CBO won't give us any savings for some of those

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1 proposals. Is that correct?

2 Mr. DeArment. That's correct.

3 The Chairman. And what is the basis for that? There
4 aren't any savings?

5 Mr. DeArment. Well, they are multiple bases. One is
6 that the federal government operates perfectly right now, so
7 that even though we can find some ways to administer it
8 better, unless we lower appropriations for those agencies
9 they won't score the savings.

10 Senator Bradley. Would you speak a little louder,
11 Mr. DeArment?

12 Mr. DeArment. The point of view of CBO is that --

13 The Chairman. Now as I understand, you have been working
14 with CBO though and they have indicated some areas --

15 Mr. DeArment. We have worked with CBO and OMB. They
16 have differences of opinion.

17 The Chairman. I mean OMB.

18 Mr. DeArment. Yes.

19 The Chairman. Will we be prepared tomorrow to go into
20 some of those areas?

21 Mr. DeArment. There are some that I think both CBO and
22 OMB would find to save money, and we could describe those to
23 the committee.

24 The Chairman. Do you have those now?

25 Mr. DeArment. We could come forward with them. Probably

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1 it would be better tomorrow because I know some of the Agency
2 people are not here.

3 The Chairman. Let's see now. Is the joint committee
4 going to be tied up tomorrow with a mark up on the House side?

5 Mr. Belas. Well, probably some of us will. We will see
6 how it plays out. I am not sure that they are going
7 tomorrow afternoon, but if they are some of us will be here,
8 some there.

9 Mr. Chapoton. We will have to split up too, Mr. Chairman.

10 The Chairman. But you are done, virtually. All right.
11 Let's use this next hour if we can with the Treasury
12 representatives.

13 Senator Bradley. Mr. Chairman, will Treasury be here
14 tomorrow? I would like to ask one question on an item that
15 I might raise.

16 The Chairman. You can ask them now if you want and then
17 they could prepare for it.

18 Senator Bradley. All right.

19 Are you supportive of the Olympic checkoff?

20 Mr. Chapoton. We have not been supporting the Olympic
21 checkoff, no. But that has been the Treasury's initial
22 thinking on it. I can't say that that is the Administration's
23 position. We have been concerned about the effect on the
24 tax return, about the numerous other worthwhile endeavors
25 that we want the same treatment, also want to allow them on

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1 the tax returns. And we have not been in favor of it.

2 Senator Bradley. Mr. Chairman, at some point I will be
3 proposing that to add to this bill, and maybe we can get it
4 done when the Olympic athletes are in town.

5 Senator Chafee. Mr. Chairman.

6 The Chairman. Senator Chafee.

7 Senator Chafee. It seems to me that one thing to bear in
8 mind as we go through the revenue raises and the tax cuts
9 that we have had, is to realize that when that is done we
10 are going to come in here with, I understand, a series of
11 proposals that will go with this legislation that will be
12 revenue losers. Example: The extension of the R&D tax
13 credits. And there are others.

14 Now we have got to allow a little leeway for the money
15 we are going to lose in that if we are shooting for a goal
16 of whatever it is.

17 The Chairman. All right. We think we have done that if
18 everybody will restrain themselves on the other end. But
19 how many suggested add-ons are there? I mean, how many have
20 been suggested?

21 Mr. DeArment. More than a hundred, Mr. Chairman.

22 (Laughter)

23 Senator Chafee. Well, take for example on the insurance
24 bill. Now I don't know whether you are working from the 1969
25 law as a base or you are working from the law that expired at

1 the end of 1983.

2 Mr. DeArment. We would be looking at current law as the
3 base from which to measure, as we do in --

4 Senator Chafee. Well, you mean current law being the
5 1969 law?

6 Mr. DeArment. 1959, the 1959 Act.

7 Senator Chafee. The 1959 law?

8 Mr. DeArment. That is correct.

9 Senator Chafee. Well, if you're doing that you are talking
10 a good chunk of money.

11 Mr. DeArment. That is correct. We are talking a fair
12 amount of money.

13 The Chairman. You mean as far as loss?

14 Senator Chafee. As far as loss goes.

15 The Chairman. Right.

16 Mr. DeArment. That's correct.

17 The Chairman. About \$3 billion.

18 Mr. DeArment. That's the Treasury's estimate.

19 Senator Chafee. I mean, I am not sure whether that is
20 right or wrong. If that is the base you are working from,
21 that is \$3 billion that has to be made up.

22 Mr. DeArment. That's right.

23 But that is the biggest single one. I
24 don't say there is agreement, but we have been working with
25 you, and Senator Bentsen and others trying to compromise some

1 of those differences

2 Senator Chafee. Well all I am saying is that there are
3 some legitimate things there that are going to cost money.
4 So I think for us to come right in on target on your cuts
5 and increases in taxes isn't going to be enough by the time
6 we get through with these --

7 The Chairman. And we have suggested, I think--I don't
8 know what the Administration's position is--but I think there
9 are about \$8 billion in the Administration's budget over the
10 next three years.

11 Mr. Chapoton. That's correct on items such as extension
12 of the R&D credit, and the espousal error, tuition tax
13 credits, education --

14 The Chairman. Maybe even some of those might have to be
15 restrained a bit. I don't know what the reaction would be.

16 Senator Bentsen. Let me ask to be recognized, Mr.
17 Chairman, because Senator Chafee raised a very valid point
18 about whether or not the assumption is that the 1959 law
19 would have continued on insurance or whether you would have
20 added some extension of what expired December 31st.

21 Nobody that I know of thought the 1959 law was going to
22 be in effect now. And that is the fault of the Congress for
23 us not having done something about it.

24 But just so we are comparing apples to apples, the
25 Administration -- is that the same assumption the

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1 Administration is using in their --

2 Mr. Chapoton. Senator Bentsen, we agree with your
3 statement as a practical, technical matter. The current
4 services is what we estimate the receipts on, and current
5 services had an expiration of stopgap of December 31, 1983.
6 And so, by necessity, the industry's tax goes back up at
7 that point. But you are right, we have all assumed that
8 there would be a new system in place at that time. But,
9 mechanically, we can't get away from the fact that, compared
10 with current services from which we operate it would lose
11 money.

12 Senator Bentsen. Well that's the point I am trying to
13 get to.

14 Then we are using the same assumption, that CBO is and
15 the Administration is, the extension of the 1959 law.

16 Mr. Chapoton. That is correct.

17 Senator Bentsen. All right. Thank you.

18 Mr. DeArment. We did assume when we did TEFRA that the
19 stopgap would expire. And that was part of our \$98.3 billion,
20 was the assumption we would collect those higher revenues,
21 from the 1959 Act.

22 Mr. Brockway. Our baseline in the budget assumes the
23 expiration of stopgap. So you have to take out for that.

24 The Chairman. But does it assume you would pick it up?

25 Mr. Brockway. It assumes, for example, the House bill

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1 loses revenue on the insurance piece. It is more than the
2 insurance industry was paying in 1983. And so from that
3 standpoint, the burden is going up. But insofar as the
4 revenue square against the budget, it is somewhat of a
5 revenue loss.

6 The Chairman. Now do we have some procedures for the
7 staff, and the joint committee and Treasury for reviewing
8 these suggested additions to this package if we reach that
9 point?

10 Mr. Chapoton. Well we will, as we followed last fall.
11 The staffs met late last week, and we will be going over
12 each of these individuals items.

13 The Chairman. Yes. It would seem to me if you could go
14 through those where we have either no objection or an
15 agreement, it would be very helpful to consider some of those
16 very quickly. Others I assume would want to be discussed
17 at some length, maybe votes on them.

18 But will you have a package? We probably won't need it
19 this week unless late Thursday. But do you think you have
20 agreement or no objection?

21 Mr. Chapoton. I think that's what we should work for,
22 like we did last fall.

23 Mr. DeArment. We could clearly have that by next week,
24 work through that package.

25 The Chairman. I think Senator Chafee is right. We can't

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1 say, well, we need \$50 billion. Here is \$49.9, and then
2 subtract 8.

3 Senator Danforth. Mr. Chairman, it would strike me that
4 Senators who have proposals to add matters to the bill which
5 would be revenue losers should also make an effort to come
6 forth with offsetting ideas; that that should be a
7 responsibility of individual Senators if they are going to --
8 I certainly will. For example, on the R&D tax credit, I will
9 attempt to make that permanent.

10 Now as far as next year's budget is concerned, the
11 difference between permanency and a three-year extension
12 would be zero. But I do think that it is important for all
13 of us not just to look for our favorite add-ons but also for
14 possible subtractions.

15 The Chairman. I think we have got some ideas on how to
16 make it work if we have the votes.

17 Senator Bentsen. Mr. Chairman, when do you anticipate
18 we will be getting to some of the other items that are on
19 this list?

20 The Chairman. About 10:00 o'clock tomorrow.

21 Senator Bentsen. You will?

22 The Chairman. Right.

23 I thought we would use from 4:00 to 5:00 working with
24 Buck. You have one question on --

25 Mr. Chapoton. Extraordinary dividends.

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1 The Chairman. Extraordinary dividends. And Senator
2 Durenberger, and Senator Wallop.

3 So we will stand in recess then until 10:00 o'clock
4 tomorrow morning.

5 (Whereupon, at 3:56 p.m., the session was concluded.)

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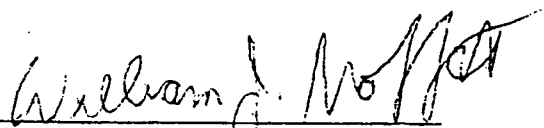
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This is to certify that the foregoing proceedings of an Executive Session of the Senate Finance Committee on the Deficit Reduction, held on February 28, 1984, were reported as herein appears and that this is the original transcript thereof.


WILLIAM J. MOFFITT
Official Reporter

My Commission expires April 14, 1984

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