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MARK-UP OF DEFICIT REDUCTION PROPOSALS

THURSDAY, MARCH 1, 1984

U.S. Senate
Committee on Finance
Washington, D.C.

The committee met, pursuant to recess, at 10:26 a.m. in room SD-215, Dirksen Senate Office Building, Senator Robert J. Dole (chairman) presiding.

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

Also present: Commissioner Roscoe Eggar, Internal Revenue Service; Mr. Ronald Pearlman, Treasury Department; Mr. Bill Gainer, General Accounting Office.

Also present: Mr. Roderick DeArment; Mr. Michael Stern; Mr. Richard Belas; Mr. James Wetzler; Mr. Donald Susswein; Mr. Stewart Dorsey; and Mr. Stewart Dorsey.

1 The Chairman. While we are waiting for other members
2 to appear, Senator Heinz says he has discovered some fine
3 print in one of the proposals.

4 Senator Heinz. About 200 pages worth.

5 The Chairman. Right.

6 Senator Heinz. Mr. Chairman, this problem has been
7 discussed with the extremely knowledgeable Finance Committee
8 staff by Ms. Raffaelli. The problem has to do with the
9 receipt of extraordinary dividends by corporations. As
10 described in the Finance Committee handout, I had absolutely
11 no problems with what we were doing, and I still don't.
12 But it turns out that on the very end of the Treasury
13 description, in the very last paragraph, the third
14 subparagraph nonindented says:

15 "3. There is othersise a substantial dimunition of
16 the taxpayers risk of loss from holding the stock by reason
17 of his holding one or more other positions."

18 I will be quite honest with you. I still can't figure
19 out what that means, and I don't know if any of the rest
20 of you do, but what it apparently means in practical terms
21 is that a stock issue that is now being contemplated which
22 has been largely committed to by a major corporation in my
23 State, at least as they understand this language, I would
24 ask the staff to discuss it further.

25 Mr. Wetzler. Senator Heinz, the issue here is under

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1 present law to get the dividends received deduction, a
 2 corporation has to hold a stock for at least 15 days, and
 3 as a special rule, 90 days or certain kinds of preferred
 4 stock, and what the bill does is set up a special one-year
 5 holding period for so-called extraordinary dividends.

6 Under present law, there are some rules that deal with
 7 the question of -- let's say I have bought a stock and I
 8 have sold short substantially identical stock. The law
 9 today says I can't count that period when I sold short -- I
 10 can't count that period as part of my 15-day holding period.

11 What has happened is that, since those rules were
 12 written many years ago, there have been all sorts of new
 13 products -- listed options, futures contract, and what not,
 14 and Treasury's recommendation is that you should not have
 15 your holding period run during any period in which you
 16 entered into some other position which substantially
 17 diminishes your risk of loss. It is a concept similar to
 18 the straddle concept that was dealt with here in 1981.

19 Now, there has been some concern within the securities
 20 industry about two areas. One is the Treasury proposes an
 21 exception for so-called-- It says that you should not get
 22 a holding period when you own the stock and you have written
 23 a so-called in the money cupboard call. The securities
 24 industry would like that exception to only apply to exception
 25 for covered calls that are deep in the money. It is a similar

1 concept to the covered call amendment that was agreed to in
2 this committee last December. I don't believe Treasury has
3 an objection to that.

4 Now, there has also been expressed some other concern
5 about how this provision would apply to securities traders,
6 and I think, if you don't mind, we would like to try to work
7 up something that we think would be a compromise between
8 what Treasury wants and what the concerns expressed by the
9 securities industry.

10 Senator Heinz. Let me ask you this. Does the catch-all
11 risk apply only when the corporate taxpayer does dispose of
12 the stock?

13 Mr. Wetzler. The issue is: If I am a corporate
14 taxpayer who owns stock and suppose I have written a call
15 option which is so-called deep in the money. Now, the
16 practical effect of that is that I am almost certain to
17 sell the stock pursuant to the call option that I have
18 written. And therefore, for all intents and purposes, I
19 really don't own the stock anymore, or at least I have very
20 little risk from owning the stock since I am almost
21 guaranteed--I am virtually certain to have locked in my
22 selling price.

23 And I think with respect to deep-in-the-money covered
24 calls, I don't really think there is any objection to the
25 Treasury's suggestion. I think there is an objection when

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1 the covered call is not deep in the money, and I think that
2 can be worked out without a problem.

3 Now, the Treasury proposal is-- Some concern has been
4 expressed that the language is vague. What do you mean by
5 a substantial diminution of the risk of loss? If I own one
6 utility stock, and I have sold short a different utility
7 stock, does that mean I have substantially diminished my
8 risk of loss? And I think we are going to have to work out
9 some rules that clarify just what the Treasury had in mind
10 in order to make the proposal less controversial.

11 But you are right. There has been some objection
12 expressed as to the way they have done it.

13 Senator Heinz. Jim, I think that would be a good idea,
14 and with the chairman's concurrence, I would ask that my
15 staff, Treasury, and Jim try and work out the specifics on
16 this so that we don't avoid--excuse me, so we do avoid any
17 unintended --

18 Mr. Wetzler. I think it would be helpful if we could
19 talk to your people to find out just exactly what their
20 problem is. It might be something that we haven't thought
21 of yet.

22 Senator Heinz. All right. Thank you.

23 The Chairman. Now, as I understand it, I have a sheet
24 here called "Additional Revenue Raising Measures--
25 Possibilities." Let's pass each one of those out. Now, we

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1 are not limited. If somebody doesn't like any of these,
2 maybe they have something they can substitute for it.

3 But before we go into the revenue side, and again, I
4 would indicate for those who may have other business, I don't
5 think we will get to any additional items -- whether it is
6 insurance or whatever it is -- today. I think we are going
7 to be--we are not operating in a closed session, so it takes
8 us a bit longer to put together this package. But the House
9 hopes to complete action on their \$50 billion package today.
10 They started at 9:30 and they ought to be finished by shortly
11 after lunch.

12 But in the sunshine here, it takes a little longer.
13 We may have to resort to a caucus later on, sort of an open
14 caucus with no one permitted but members, to reach final
15 agreement on some of these items. But I don't think we will
16 be taking any add-ons today.

17 What we would like to start with today -- we have
18 narrowed down the Grace Commission list -- eliminated some
19 that were flawed or objectionable, or highly objectionable,
20 and we think we have a smaller list. Are those available?

21 Maybe while we are finding those, I can ask Treasury
22 a question. Mr. Perlman, I would like the record to address
23 just a couple of questions. Some have suggested that an
24 appropriate Section 483 interest rate would be 80 percent
25 rather than 120 percent of the T-bill rate for equivalent

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1 blank securities. Have you given us any thought as to this,
2 or has this been brought to your attention?

3 Mr. Perlman. Yes, Mr. Chairman, it has. And we have
4 given it some thought. In our package, when we suggested
5 a rate, and the rate that is proposed in the Administration
6 proposal is 120 percent of the T-bill rate for equivalent
7 blank securities, we attempted to establish a rate that would
8 be the best rate -- the most favorable rate -- that would
9 be extended to a credit on an arm's length basis, that is,
10 the lowest interest rate that someone could expect to get
11 in the market.

12 We thought that was the fairest way to arrive at a
13 rate for purpose of the OID rules. People don't borrow at
14 80 percent of the T-bill rate. That is just not a realistic
15 borrowing rate, and we think what we need to do here is use
16 what is viewed as a realistic borrowing rate.

17 Now, that doesn't mean to suggest that there is any
18 particular magic to 120 percent. It could have been 130 or
19 125 or 118, but we think that a rate in excess of the T-bill
20 rate is a fair approximation of what people would--what the
21 most solid credit risk could borrow for in the market and
22 that 80 percent is such a departure from that that it would
23 really introduce some rather significant distortion into
24 the OID rules.

25 So, I don't think we could support an 80 percent

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1 approach.

2 Mr. Wetzler. Mr. Chairman, in the House in the spread
3 sheet that was handed out yesterday, staffs are suggesting
4 110 percent, instead of 120 percent on the theory that there
5 are high quality corporations that can borrow it at as low
6 as 110 percent of the Treasury rate. So, you might consider
7 dropping the Treasury's 120 percent down to 110, and their
8 130 down to 120.

9 That suggestion is being considered over in the House.

10 The Chairman. Would the Treasury object to that?

11 Mr. Pearlman. No. I think if the committee believed
12 that were more appropriate, we can live with that.

13 The Chairman. Why don't we, when we have a working
14 quorum, that might ease some of the pain, particularly where
15 it is probably going to be done in the House side, I would
16 assume.

17 Then, the second question. Some have also suggested
18 that it might be appropriate to have an exclusion from the
19 OID rules if the deferral involved is less than five years.
20 Have you considered such an exception?

21 Mr. Pearlman. Yes, we did consider a variety of
22 exceptions, ranging from shorter deferral periods to as
23 much as five years. Again, Mr. Chairman, our concern is
24 that, particularly with interest rates in the range they
25 are at now, and even more seriously if they go higher -- which

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1 we all hope they will not -- a five-year exception can create
2 a material amount of distortion in the transaction. I don't
3 have any data with me, so I can't give you any specifics,
4 but we think a five-year exception would be a substantial
5 weakening and, indeed, an inappropriate weakening of the
6 deferred payment rules.

7 The Chairman. Jim, have you considered this?

8 Mr. Wetzler. We have looked at it, and I think we
9 agree with the Treasury. I can't speak to what the committee
10 will end up doing, but I think it would clearly weaken the
11 provision quite a bit to allow a five-year exception.

12 The Chairman. Okay. I wanted that to be expressed
13 publicly, because I have had inquiries. In fact, I met with
14 someone who asked me to raise the question. We will make
15 that change if there is not objection when an additional
16 member arrives.

17 Now, could we go back? Who wants to discuss the
18 modified Grace Commission list?

19 We have eliminated, I think, the most controversial
20 portions. I know that Mr. Eggar is violently--not
21 violently--but strongly opposed to number one, so we made
22 that effective in fiscal year 1986, to give IRS time to
23 figure out a way to do it. I think if we made it effective
24 in January of 1985, he would have a real problem. Now, who
25 is going to discuss these -- Don or Stu?

1 Mr. Dorsey. The only item on the list that we had not
2 discussed--excuse me--

3 The new item on the list -- let's see -- it is the
4 acceleration of --

5 The Chairman. Let's go over all of them. We have got
6 a different list here.

7 Mr. Dorsey. Okay. The first item is offsetting
8 delinquent debts against tax refunds. And this would allow
9 the IRS--or it would give the IRS the ability to offset
10 nontaxed delinquent debts against IRS tax refunds.

11 The Chairman. Is there any objection to our making
12 that effective -- we changed the effective date. Is that
13 correct?

14 Mr. Susswein. That is correct.

15 Senator Heinz. Just so I understand this. These
16 nontaxed debts would include what kinds of things?

17 Mr. DeArment. Student loans, SBA loans.

18 Senator Heinz. Now, an SBA loan to a corporation
19 would be offset against a corporation's individual tax,
20 or an individual --

21 Mr. Susswein. Senator, the corporation's corporate
22 tax. In other words, where there is a debtor that can be
23 identified, and that debtor is getting a refund, this is
24 a collection thing of last resort.

25 Senator Heinz. But after what level of adjudication of

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1 the general debts claimed to the United States.

2 Senator, the proposal of the Grace Commission was
3 that the legislation include appropriate safeguards to
4 ensure that the agency contacts the debtor to ensure that
5 it is a valid debt. And the recommendation before the
6 committee today would essentially say that procedures
7 similar to those used by the IRS in notifying taxpayers of
8 tax debts -- that is to say, the four notices that are
9 required -- would be required by any agency before they
10 passed the debt onto the IRS. This is essentially similar
11 to the current law procedures whereby the IRS can offset
12 one tax debt against another tax debt.

13 Senator Heinz. It is similar, but I want to be sure
14 it is the same, because different agencies have very
15 different collection procedures, as I understand it. I am
16 not an expert in the area, but I just want to be sure, for
17 example, that when the Social Security Administration has
18 made an erroneous payment, and that it is at least what
19 they think is an erroneous payment, that they will not be
20 empowered, for example, to go to the IRS and simply deduct
21 that erroneous payment from someone's tax refund.

22 Now, will this empower them to do that?

23 Mr. Susswein. The proposal would not. The proposal
24 would require that the agency adopt procedures to notify
25 the allegedly delinquent debtor and give him an opportunity

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1 to contest with the agency.

2 Senator Heinz. Now, the Social Security Administration
3 says that they will not do that. They refuse to do that.
4 Now, they say that that would be very prejudicial to them
5 to adopt a notification process where they notify people
6 of an erroneous payment because, if they notify people,
7 they claim that people will take the money and run, even
8 though the IRS may be in error. And so, what the IRS does
9 is they go into people's bank accounts and just take the
10 money.

11 Now, technically, they say we don't do that. We just
12 tell the bank to do that for us, and the banks do, and they
13 give the money to the IRS because the banks have no choice
14 in the matter, so it amounts to the same thing.

15 Now, we are going to allow -- in addition to that -- we
16 are going to allow the IRS to be another mechanism here for
17 going -- not even into people's bank accounts -- the money
18 is just going to disappear out of their refunds.

19 We have got some real problems with the way the
20 Government operates, and it is not quite as benign a
21 Government as we like to think. We held quite a considerable
22 hearing in the Aging Committee on the error rates in the
23 Social Security Administration. The computer system is a
24 disaster -- they admit that -- and their methodology for
25 dealing with people can be a real disaster, and there have

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1 been some fairly spectacular television coverage on 20/20
2 or 60 Minutes and some of those shows. So, Mr. Chairman,
3 I am not against this in principle, but I really wonder
4 about how well the present-- It assumes that the Federal
5 Government, when it makes a claim, is right. And maybe
6 we are not perfect.

7 Mr. Suswein. Senator, the proposal here would permit
8 -- would require -- the agency to give the alleged
9 delinquent debtor an opportunity to respond to the notices
10 from the agency to contest the validity of the debt. The
11 regulations would permit the IRS to offset the refund only
12 in the cases where the debt essentially -- where the agency
13 concluded that the debt was valid after this process.

14 Senator Heinz. Mr. Chairman, as described, I guess
15 I have more of a problem than I think because there is a
16 huge presumption here -- as I hear the safeguard -- the
17 presumption is that the Federal Government, which is right.
18 And I have evidence -- we have evidence -- GAO has evidence
19 that when the Federal Government makes a claim--makes a
20 mistake, it is usually in the favor of the Federal
21 Government, not in the favor of the beneficiary in the
22 case of Social Security checks.

23 And when they make those kinds of mistakes, they may
24 notify people or not, but they just go right ahead and
25 proceed. So, I think we ought to look at this a lot more

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1 carefully than we are.

2 The Chairman. That is another reason we have made it
3 effective in January of 1986, rather than January of 1985.

4 Senator Heinz. But you are still making it effective.

5 The Chairman. Yes. This was, in fact, a recommendation
6 by the GAO initially.

7 Senator Heinz. That may be, Mr. Chairman, but that
8 may have been before the GAO looked at the mess in the
9 Social Security Administration, and maybe this will turn
10 out to be a good proposal, but I want to be on the record
11 at this point that I am opposed to it because I am not
12 confident about the way it is going to work.

13 The Chairman. Do you want a record vote?

14 Senator Heinz. No. I am not asking for a record vote,
15 Mr. Chairman. I am just concerned about it, and I want it
16 to be on the record.

17 Mr. Pearlman. Mr. Chairman, I know you know what our
18 views are. First, I would hope that if you decide to
19 adopt this proposal, that at least you would give us the
20 opportunity to have the Commissioner come back and at least
21 spend a couple of minutes with you. But I do want you to
22 understand that both the Service and the Treasury are deeply
23 concerned about this proposal.

24 We are looking at it from a slightly different viewpoint
25 than Senator Heinz. We are more concerned about its

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1 potential impact on the tax system, but I do want to restate
2 that very deep concern.

3 Senator Heinz. As a matter of fact, I see some people
4 from the Social Security Administration here. Maybe they
5 could tell us if this is going to change their system.

6 Mr. Enoff. Senator, I can't at this time.

7 Senator Heinz. That is what I thought. Mr. Chairman,
8 what I would appreciate the Social Security Administration
9 do is -- in view of the hearing that we had with them on
10 error rates in the Social Security system -- take a look at
11 what the committee is proposing and they say, in short,
12 that the agencies that would be allowed to offset what they
13 believe to be debts to the Federal Government against IRS
14 refunds -- there would be certain safeguards, i.e. required
15 notification.

16 Now, as I recollect, the Social Security Administration
17 has some reservations about required notification across the
18 board. At least, that is what you told us in hearings and
19 privately. So, we have a conflict here, and I would like it
20 to be resolved after the hearing.

21 Mr. DeArment. Senator Heinz, one of the things to
22 look at in terms of the notification is we have this authority
23 now. The IRS does offset debts in the area of child support
24 enforcement. Seventeen States also have similar programs,
25 including the State of Oregon, which the General Accounting

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1 Office has studied, the Oregon program of offsetting refunds
2 and praised it highly. So, with appropriate safeguards, it
3 could work.

4 Senator Heinz. I could support this if we maybe
5 -- based on what I know -- if we excluded the OAS DI program
6 from it. But knowing what I know of the OAS DI system, I
7 think every member here is going to live to regret throwing
8 the Social Security system into this pot, given the terrible
9 problems they have with their information systems -- and
10 they freely admit they have very serious problems with it.

11 Mr. DeArment. They have their own tools, particularly
12 where they are continuing benefits to handle offsets.

13 Senator Heinz. We are giving them an additional power
14 here.

15 Mr. DeArment. No, but they already have their own tools
16 so I am not sure that that would significantly weaken the --

17 Senator Heinz. Let's take them out.

18 Mr. DeArment. Yes.

19 Senator Heinz. Mr. Chairman, could we agree just to
20 take this --

21 Mr. DeArment. Mr. Chairman, Senator Heinz made a
22 suggestion that I think, if we adopted, would make it
23 acceptable to him, and that is that in expanding this offset,
24 we would not include OAS DI programs. I don't know whether
25 child support enforcement comes under there, but with the

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1 exception of child support.

2 Senator Heinz. It doesn't. OAS DI is the old agent
3 of our disability insurance programs.

4 I really suggest that we hold that out for now. We
5 could always do it later, but we should be very careful.
6 It is a \$200 billion plus program that has administrative
7 difficulties, as well as financial difficulties.

8 The Chairman. I am sorry. I was disconnected here.
9 What is that again?

10 Mr. DeArment. Senator Heinz was suggesting that we
11 take the old age survivors and disability programs out from
12 under this, and that, I think, would be an acceptable
13 proposal, and I don't think it would change it significantly.

14 Senator Heinz. Then I would support the proposal.

15 The Chairman. With still no Treasury's objections.

16 Mr. Pearlman. We can have the Commissioner here in
17 15 minutes. Would you be willing --

18 The Chairman. No, he can come back later.

19 Mr. Pearlman. All right.

20 The Chairman. After we adopt it.

21 (Laughter)

22 The Chairman. Without objection. Now, let's move on
23 to number two. But he was here yesterday.

24 Mr. Pearlman. Yes.

25 Mr. Dorsey. The effective date would be January 1, 1986

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1 then.

2 Mr. Pearlman. I wonder if it might not be worth at
3 least considering the possibility of putting a sunset on it
4 or having some ability to take a look at this program a
5 couple of years down the road and make sure that we don't
6 put in --

7 The Chairman. Yes.

8 Mr. Pearlman. Could we do that?

9 The Chairman. We will sunset it in 1987.

10 Mr. DeArment. Sunset it at January 1st of 1988.

11 The Chairman. 1988?

12 Mr. DeArment. 1988.

13 The Chairman. Yes.

14 Mr. Pearlman. And so, what is the effective date then?

15 Mr. Dorsey. January 1, 1986 through January 1, 1988.

16 The Chairman. That gives us our savings, right?

17 (Laughter)

18 The Chairman. We are really scrounging around here
19 trying to save some money. All right. What about number
20 two?

21 Mr. Dorsey. The second proposal is to mail payroll
22 checks and benefit checks on their due date rather than
23 before their due date. The Grace Commission proposal was
24 to try to encourage the electronic funds transfer to direct
25 deposit of Federal payroll checks and benefit checks.

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1 So, this proposal would require Treasury to mail payroll
2 checks on the due date and also would require that Federal
3 benefit checks, as well, be mailed on the due date. The
4 savings would -- from the three-day slippage of those --

5 The Chairman. It is bookkeeping, right?

6 Mr. Dorsey. It is a three-day slippage, but it moves
7 back some of the Federal outlays one fiscal year.

8 The Chairman. Anybody have any objection to this?

9 Senator Heinz. Mr. Chairman, the idea, as I understand
10 it, is to "encourage the use of EFT." Now, if that were to
11 be the case, what one would expect is that you would pick
12 up revenue in one year -- the year you implemented it -- but
13 basically lose that revenue if you succeeded in encouraging
14 EFT at some future point in time.

15 Now, the numbers we have are all pluses, so what the
16 numbers say is we are not encouraging EFT at all. We are
17 just sending our checks out later, and people are going to
18 continue to receive them later, which strikes me as something
19 different than encouraging electronic funds transfer. I
20 would like a comment on that.

21 Mr. Dorsey. Yes. The numbers -- the estimates -- were
22 based upon the assumption that there would be a relatively
23 low rate of conversion from receiving checks by mail into
24 electronic funds transfer to direct deposit. The savings
25 indeed do come from the slippage of three days of those

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1 checks.

2 Senator Heinz. Why did CBO assume there would be a low
3 conversion? Because these people don't have bank accounts?

4 Mr. Dorsey. They assumed that about 12 percent of
5 beneficiaries do not have bank accounts, and I don't know
6 the basis for it. They assumed, I think, about a 2.5 percent
7 conversion rate. In other words, almost everyone would
8 continue to receive payment by check. That was one reason.

9 Senator Heinz. And let me ask you this. The people
10 who are going to be affected by this -- just the people that
11 are going to be affected by this -- what proportion of them
12 have bank accounts? Not of the total population, but of the
13 people who do not now take EFT?

14 Mr. Dorsey. Twelve percent, I believe, is the CBO
15 estimate on that.

16 Senator Heinz. And that is of the people who don't
17 now take --

18 Mr. Dorsey. Of those people who are now receiving
19 their checks by mail.

20 Senator Heinz. Do we know anything about the
21 characteristics of that population?

22 Mr. Dorsey. I am not aware of any further information
23 on that, but we can check.

24 Senator Heinz. Mr. Chairman, this may be a good idea,
25 but I am a little concerned about people on SSI who have a

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1 hard time making it week to week. Would we want to just
2 exempt the SSI program from this, because there is no doubt
3 in my mind that an awful lot of that 12 percent in SSI
4 certainly don't have bank accounts.

5 The Chairman. We will hear from Treasury.

6 Mr. Pearlman. Let me just indicate that OMB has advised
7 us that they, too, are concerned about the impact on
8 benefit recipients of this proposal, and while the payroll
9 piece sounds much better to us, and I think it is something
10 that we could support, that it clearly is going to mean
11 recipients of benefit checks who do not have bank accounts
12 are going to get their checks late -- several days late --
13 whatever the mail requires. That is going to disrupt
14 people, and it is certainly going to disrupt people who
15 have been receiving SSI checks, but, in addition, other
16 benefit checks. And we are quite concerned about that
17 disruption.

18 We would hope that the committee would consider
19 limiting this proposal only to payroll checks, at least
20 for the time being, until we get a better handle on what
21 we are doing to other people.

22 The Chairman. You limit the savings if you limit it
23 to payroll checks. By how much?

24 Mr. Dorsey. About \$182 million if we just limit it to
25 payroll checks.

1 The Chairman. All right, let's limit it to payroll
2 checks.

3 Senator Chafee. Mr. Chairman, I was going to say that
4 I am getting uneasy here. We spend three days debating
5 whether we can deduct a \$16,000.00 automobile -- whether
6 it should or shouldn't be -- and then we go after somebody's
7 benefit check. I am for saving money. I voted for every
8 one of these savings proposals, but it seems to me we get
9 to a point that we heading down the wrong track.

10 And now we are saying what? The payroll checks will be
11 mailed out on the due date?

12 Mr. Dorsey. Yes.

13 Senator Chafee. My experience with the U.S. mails
14 shows that the poor sucker is going to wait a week for his
15 check.

16 (Laughter)

17 Mr. Dorsey. The estimate would be that it would be
18 about a three-day delay because they are now mailing them
19 three days, approximately, before the due date.

20 Senator Chafee. How does it work now? If we have a
21 holiday, I just know the U.S. Senate gets paid. If we have
22 a holiday on Monday, they give us our check on Friday. Is
23 that the way it works for all Federal employees?

24 Mr. Dorsey. I believe Federal employees are paid on
25 a bi-weekly basis.

1 Senator Chafee. All right. On the bi-weekly, the date
2 comes up on a Monday, when Sunday is a holiday, so then they
3 give us the check on the previous Friday. Is that the way
4 it does work for somebody working for the Naval Underwater
5 Systems Command?

6 How many people have received their checks by mail for
7 their work, anyway? Payroll checks?

8 (No response)

9 Senator Chafee. All I am saying, Mr. Chairman, is
10 that it just seems to me we are really down to some nickel
11 and dime stuff here. And now I know you are going to say
12 if we want to save money, we have got to save money. And
13 I am prepared to save money, and we have taken some tough
14 votes in this committee, but there's a point at which I
15 think it gets a little absurd.

16 You end up in this thrashing around, and we save
17 \$186 million. I am not for it.

18 The Chairman. Okay. Let's just move on to the next one.
19 Let's don't get hung up on this. We will just forget this
20 one, for the time being. Let's take it off the table.

21 Mr. Dorsey. All right.

22 The Chairman. We are not going to get anything done
23 if we spend 30 minutes on each item.

24 Mr. Dorsey. Item number three is to improve income
25 verification for programs SSI, AFDC, food stamps, and

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1 Medicaid. This proposal would make additional income and
2 asset data available to the various programs so that they
3 could verify the eligibility of recipients.

4 Now, most of the savings that is assumed from this
5 proposal focuses on making available the IRS tape on unearned
6 income, and that would require amending the Tax Reform Act
7 of 1976. That additional data on unearned income, CBO
8 feels would be very useful in checking the eligibility of
9 recipients of SSI, AFDC, and Medicaid.

10 In addition, this proposal would require--would allow
11 the Department of Labor to require States to collect
12 quarterly wage data which we believe also would be of use
13 in checking eligibility in various programs.

14 The Chairman. Senator Moynihan.

15 Senator Moynihan. Mr. Chairman, two comments. One is
16 that we were told that we would receive the relevant portions
17 of the Grace Commission Report that we would be dealing with
18 and perhaps I have just not gotten it. Perhaps it was mailed
19 to me.

20 (Laughter)

21 Mr. DeArment. We had this material right here hand
22 delivered to every office last week.

23 Senator Moynihan. I am sorry, Rod. What I wanted to
24 ask -- it is to make a general point about the Grace
25 Commission. They have looked at a lot of questions from the

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1 point of view of private sector enterprises, which they are,
2 and that was their assignment. But not always with the
3 recognition that Government has different kinds of
4 obligations. And one of the obligations the Government has
5 -- since it can require just about any kind of information
6 at once from its citizenry -- we assume the obligation to
7 keep that information--to hold it very closely.

8 It is held in confidence. Our Internal Revenue Service
9 holds out tax returns in confidence. I think we would like
10 to know, with some specificity, what kinds of information
11 are to be made available to whom in this matter because
12 there is a large principle involved even though they are
13 small sums of money. I would just like to know that the
14 committee staff is satisfied that, quite specifically, the
15 kinds of information, and that they are satisfied that those
16 kinds of information shouldn't be passed around from one
17 agency to another.

18 Mr. Dorsey. The most important additional data that
19 would be made available, Senator Moynihan, is the IRS tape
20 on unearned income. Currently, the earned income tape is
21 made available, and this would make the unearned income tape
22 available as well. And so that would allow checking of
23 asset levels for applicants for basically the SSI and AFDC
24 and Medicaid programs. It would make available to those
25 people who administer those programs. It would make it

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1 available to the Social Security Administration, which
2 administers SSI the data on unearned income.

3 Senator Moynihan. Are you satisfied with the
4 methodology by which the estimated savings were reached?

5 Mr. Dorsey. Yes. This is a CBO number, and we have
6 been speaking with them, and that number seems to be as
7 reliable as CBO estimates generally are.

8 The Chairman. I wonder if we might get Treasury to
9 comment also on this.

10 Mr. Dorsey. There was a pilot study done which was
11 the basis of it on this estimate. And it was a pilot study
12 between IRS and SSI, and they found that there were
13 significant numbers of people in the SSI program that
14 claimed no assets for which they could later discover they
15 did have assets. And so that was the basis for this
16 estimate.

17 Senator Moynihan. All right. As to the confidentiality
18 of data?

19 Mr. Pearlman. Yes, let me comment on that. There is
20 a specific item that I am checking now, but I do want to
21 comment. Mr. Chairman, Senator Moynihan, we are concerned
22 about the confidentiality issue as well.

23 It is correct that under current law earned income data
24 is made available. I think I would react this way -- that
25 it is not the expansion to unearned income data that is

1 particularly disturbing -- it is what happens to the data
2 when it gets into the other agency. And I think that if
3 the committee chooses to go forward with this proposal,
4 then we are just going to all have to make sure that the
5 safeguards are there to make sure that that data does not
6 go beyond appropriate officials in the other agency. And
7 that is of concern to us.

8 I guess the institutional reaction traditionally has
9 been that we try to restrict the disclosure of tax return
10 data period because you just know that some of that data
11 is going to get into inappropriate and unauthorized hands,
12 even with the strictest standards.

13 That risk is there today with respect to earned income.
14 And if it is expanded to unearned income, we are just going
15 to have to make sure that the risk is as low as possible.
16 We are uncomfortable about expanding data that is provided
17 by taxpayers on tax returns.

18 Senator Moynihan. Mr. Chairman, you heard that?

19 The Chairman. Yes, but every time you try to do
20 something around here, you have got one agency worried about
21 the other agency. I don't know why the President appoints
22 a commission, and then his own people won't agree to do
23 anything they recommend. Can you write in some safeguards?

24 Mr. Pearlman. As I tried to indicate, Mr. Chairman, if
25 the committee chooses to accept this, that is what we will do.

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1 Senator Moynihan. We have a sacred trust in this
2 committee to see that IRS data is carefully handled.

3 The Chairman. Oh, I agree with that. I don't want to
4 say we can't do it. Why can't we write in some safeguards?

5 Mr. Pearlman. I don't think I said that nor did I mean
6 to, if I did. What I meant to say, simply, was that I think
7 we all have to be concerned by that and hopefully we will
8 be able to write in those safeguards.

9 Mr. DeArment. The GAO study makes recommendations,
10 and concluded that they had considerable merit and were
11 feasible to implement and suggested two tighteners in
12 terms of their qualifications and concerns about protecting
13 it, which we assumed that we would adopt.

14 The Chairman. Why don't we do this? We might--
15 Obviously, we want to protect the information, but obviously
16 we also want to try to make the programs a little more
17 efficient if we can. Could we hope that Treasury could
18 indicate to us that they have some language to satisfy the
19 concerns of Senator Moynihan and the rest of us on the
20 committee?

21 Mr. Pearlman. Sure, we will do that.

22 The Chairman. So, if we can agree to that language,
23 we will agree to the provision. If we can't, we won't.
24 And maybe GAO has some other suggestions that we ought to
25 consider. All right. Now, so we have eliminated two. We

1 have agreed to one. We will wait on three to get the
2 language, and let's move on to number four.

3 Senator Boren. Mr. Chairman, I apologize. On the one
4 on the collection agency matter and the refund offset that
5 we were talking about yesterday -- have we agreed to that?

6 The Chairman. We agreed but we made it effective
7 in January of 1986, and we adopted an amendment of Senator
8 Heinz that it would not affect OASDI.

9 Senator Boren. Okay, but we would go ahead with the
10 collection agency and the refund, both, as of --

11 Mr. DeArment. Just the offsetting refund.

12 The Chairman. Just the offset.

13 Senator Boren. Did we not take action on the collection
14 agency proposal?

15 The Chairman. I thought we had. I thought we had
16 agreed to do that.

17 Senator Boren. I thought we had, too.

18 The Chairman. Treasury doesn't want us to do it.

19 Mr. DeArment. Treasury doesn't want us to do it. The
20 CBO will give us no savings for it.

21 Senator Boren. But you were going to talk to CBO again.

22 The Chairman. Did you talk to them about it yesterday,
23 Stu?

24 Senator Boren. Looking at that experience with the
25 education loans --

1 Mr. Susswein. The Congressional Budget Office on this--
2 I am sorry. On the collection agencies, the Congressional
3 Budget Office says that, since current law permits nontax
4 agencies to do this, it is in the baseline.

5 The Chairman. So, we are just not doing it?

6 Senator Boren. They are just not doing it?

7 Mr. Dorsey. They say they are doing it already. They
8 already have the authority to do it, and therefore, they
9 wouldn't score any additional savings by any further action
10 in this regard.

11 The Chairman. All right. Let's move on to number four.

12 Senator Boren. Can we go on ahead and authorize IRS
13 to do this as well?

14 The Chairman. The IRS doesn't want to do anything,
15 from what I can find out.

16 Mr. Eggar. If we are talking about the collection
17 outside, we did a study in 1981, and indications are that
18 the private sector agencies could collect at about \$1.00
19 of cost for \$2.00 of recovery. Our own statistics are
20 that we get \$24.00 back for each \$1.00 of cost. I don't
21 know how in the world the collection agency could do the
22 things we do without giving them the right to file levies
23 and restrain property.

24 This was tried in 1874 and didn't work then, and I
25 don't believe it will work now. I know of no reason why

1 we should go outside for collection. We are making progress
2 now. Our whole automated collection system is about to be
3 in place and will be in place by June, and I see no basis
4 for this. There is no money to be gained by it in my
5 judgment, and I just think it is a wrong decision.

6 Senator Moynihan. Are we actually considering this?

7 Mr. Eggar. Say again.

8 Senator Moynihan. Are we actually considering this?

9 Mr. Eggar. That was my understanding.

10 Senator Boren. I am urging that it be thought about.

11 Yes.

12 Senator Moynihan. But it is not a proposal?

13 Senator Boren. It is in the Grace Commission report,
14 and it was brought up yesterday. It was on our list of
15 items that we deferred action on.

16 Mr. Eggar. Am I wrong, Senator Boren, that we are
17 not talking about outside collection agencies?

18 Senator Boren. That is what we are talking about, yes.

19 The Chairman. The question was raised whether or not
20 we accepted that yesterday. I thought we had, but apparently
21 we had not.

22 Senator Moynihan. No, we did not.

23 Senator Boren. I thought we had. I think Senator Long
24 was under the impression that we had.

25 The Chairman. I understand we discussed it, but took no

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1 action on it. And Mr. Eggar was here and discussed it.
2 Is there some alternative plan where we can help the IRS?
3 What we want to do is collect the money.

4 Senator Boren. What can we do to these agencies? The
5 present law--these independent agencies. I know Education
6 is doing it under the student loans, and they have had a
7 good recovery. I think we were told -- what -- \$600 million,
8 or something? We were told yesterday they had had a good
9 experience with it, on student loans.

10 Mr. Helms. Yes, sir. Basically, the Office of Mr.
11 Stockman has done a report, and it basically shows that
12 pursuant to the Debt Collection Act of 1982, since it has
13 only been implemented for one year, that there have been
14 about \$2.8 billion of savings to Governmental agencies.

15 A high proportion of that was attributable to the
16 student loans.

17 Senator Boren. Are the other agencies-- Apparently,
18 other agencies are authorized to do this as well, but many
19 of them are not. Is that the situation?

20 Mr. Helms. Yes, sir. There were a couple of
21 procedural problems, one of which was that in the original
22 enacting legislation, there was no mechanism for payment
23 to the collection agencies, and that was authorized early
24 last year, so that the collection agencies could take a
25 percentage of the debt that they were collecting. And that

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1 held up a number of agencies from going ahead and contracting
2 out to the private debt collection agencies for the collection
3 of delinquent debts.

4 Senator Boren. I don't know -- maybe we ought to wait
5 and see what happens to these other agencies, or maybe we
6 could give authority to IRS to act if other agencies did
7 not act, and it would be a discretionary thing with them to
8 act. Maybe that would be something we could consider.

9 Mr. Susswein. Senator, one of the things we found out
10 from the CBO as well as from the Grace Commission report
11 is that the Grace Commission basically said that the IRS
12 on the collection side is doing an extremely good job and
13 that having the IRS use the service of private debt
14 collection agencies would not result in a net efficiency.

15 They did recommend that there be increases in the
16 examination of tax returns -- that that would result in
17 large amounts of revenue.

18 Senator Boren. I thought that this was a Grace
19 Commission recommendation.

20 Mr. Suswein. Not for the IRS, Senator.

21 Mr. Eggar. We were specifically excluded, Senator
22 Boren. The refund portion only that was the recommendation
23 of the Commission for the IRS itself.

24 The only recommendation they made was a refund offset,
25 which I understand you have already voted. I will be

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1 interested to see how that works out, but the outside
2 contracting out -- they specifically excluded Internal Revenue
3 from that.

4 Senator Boren. Okay.

5 The Chairman. Okay. Let's move on to number four so
6 we can get into the nice revenue items. Accelerate deposits
7 and collection of Federal.--

8 Mr. Susswein. Senator, this proposal -- the Grace
9 Commission recommends that the Treasury Department issue
10 regulations basically regarding the cash management of
11 about approximately \$55 billion of nontax receipts that
12 come into the Federal Government. These are considered
13 offsetting receipts to direct appropriations, and so they
14 are considered as a reduction in outlays.

15 Basically, the proposal is that the Treasury would
16 issue regulations requiring a variety of cash management
17 improvements to be made. They would include for very
18 large nonrecurring payments electronic transfers, for
19 recurring payments that are made in automatic withdrawal
20 from an account, essentially similar -- it is the opposite
21 of EFT -- just an EFT withdrawal, and the third would be
22 establishment of something called the "lockbox," which is
23 essentially having checks paid to a safety deposit box
24 which a commercial bank would operate and basically they
25 would immediately deposit the check, rather than having the

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1 checks lie idle in the agency for a number of days.

2 The CBO estimates that the savings from this would be
3 \$800 million in fiscal year 1986, and another \$800 million --

4 The Chairman. Are you talking about savings or are
5 you talking about bookkeeping?

6 Mr. Susswein. No, these are real savings, Senator.

7 The Chairman. All right. Let's hear from Treasury
8 on this.

9 Mr. Pearlman. Mr. Chairman, I think in general as
10 long as the thrust of the proposal is to give us some
11 discretion -- in other words, give us authorization but
12 not mandate certain procedures -- I think we can live with
13 that. One of the things that I know the Commissioner is
14 concerned about is where are the revenues going to come
15 from to implement a number of these procedures. For example,
16 this one is going to require additional automated data
17 capability, and so I think the committee has to understand
18 that, if the funds are not forthcoming, both for the data
19 and for the people, it may not be possible to fully
20 implement much of these recommendations.

21 The Chairman. Are we authorized to take care of that
22 problem?

23 Mr. Susswein. The proposal, Senator, would provide
24 that the Treasury is required to implement these regulations
25 only to the extent that sufficient appropriations are made

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1 available.

2 The Chairman. Then, how are we going to get any savings
3 if they don't do it?

4 Mr. Susswein. The one proposal that would probably
5 involve the least burden on taxpayers--I mean, on people
6 paying the receipts with the lockbox proposal because
7 essentially it is just a question of continuing to write a
8 check, but it is a question of where you send the check.

9 According to the Grace Commission and the CBO, this
10 recommendation does not involve any data processing. It
11 simply involves negotiating agreements with banks, so
12 presumably that could be implemented without any additional
13 appropriation.

14 The Chairman. Roscoe, have you got anything on this
15 one?

16 Mr. Eggar. We have used lockbox system, and have one
17 in place for certain of these remittances, but the refund
18 offset -- the only way to do that is --

19 The Chairman. That is not in this package, is it?

20 Mr. Susswein. No, sir, this is not the refund offset.

21 Mr. Eggar. Oh, I am sorry. Well, we have already got
22 that in place.

23 Mr. Pearlman. Existing regulations have established
24 the lockbox system, so we are in the process of implementing
25 a lockbox system now nationally. I don't think --

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1 The Chairman. What is Treasury saying? Do you support
2 the proposal? Will it work? What are you saying?

3 Mr. Pearlman. I will just restate what I said before.
4 I think we can -- as long as we are not mandated to do things
5 that we don't think either we can do or don't have any funds
6 to do -- I think we can handle this proposal.

7 Senator Heinz. Mr. Chairman, if you accelerate your
8 movement or you go to lockbox system, you will have banks
9 doing things that your employees -- the Federal employees --
10 now do. Now, you can either reassign or in some way shift
11 those personnel resources to doing the other things, or
12 the equivalent in budgetary resources. And it would seem
13 to me that if you phase it in properly, you ought to be
14 able to do it. You know that better than I.

15 Mr. Pearlman. Not much better, Senator. As I indicated,
16 we have promulgated regulations that are designed to
17 implement a national lockbox system today under current
18 law, and we do expect that that will improve cash management
19 within the general framework of the services budget.

20 I guess what I am concerned about is the other things
21 that are required -- or may be required -- by this legislation
22 that can't be done simply by reassigning people but instead
23 require an increased amount of data processing, and an
24 increased number of people. I think the services record
25 in terms of --

1 Senator Heinz. Maybe what we need from them is a report
2 to the committee on how they would go about implementing the
3 mandate in number four and the extent to which they will
4 generate savings -- administrative savings -- both in
5 personnel time and money and whether, in addition to those
6 savings, they are going to need any additional resources to
7 get the entire \$16.6 billion that this shows, and come back
8 to us in some reasonable amount of time -- three months or
9 six months -- with an implementation plan, with any problems
10 spelled out in that plan, and any opportunities also seized
11 in that plan.

12 Mr. Pearlman. If the committee chose to act today, we
13 would be happy to do that -- come back to you.

14 The Chairman. We would like to act today so we can
15 take credit for the savings, but if we can't do anything until
16 you come back with a report, we will never have any savings.

17 Senator Heinz. I wasn't saying that, Mr. Chairman.

18 The Chairman. You are saying go ahead and do it --

19 Senator Heinz. Do it, and then if they run into some
20 snag, have them come and tell us so we can do something
21 about the snag.

22 Mr. Pearlman. Mr. Chairman, I think that is fine with
23 us.

24 The Chairman. Is there any objection? If not, then
25 we will approve that provision.

1 Now, let's move into the-- On number three, we are
2 waiting for Treasury to provide some information. Number
3 two has been eliminated. Number one and number four have
4 been approved.

5 Senator Baucus. I was wondering with respect to number
6 four -- it is related to number four -- whether we have had
7 an opportunity to look at the proposal I have been
8 suggesting over the last couple of days, and that is to
9 speed up the collection.

10 The Chairman. What about the Baucus-Gilman --

11 Senator Baucus. No, it is a Gilman-Roth proposal.

12 Mr. Pearlman. We have talked to the cash management
13 people. That is a long way away from what we do every day,
14 Senator, but they have indicated to us that they are
15 generally in favor of any effort to improve cash management,
16 and your proposal does that.

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

18 Senator Baucus. Fine.

19 The Chairman. Let's start with the Moynihan-- Jim,
20 have you got some more information on the Moynihan minimum
21 taxes?

22 Senator Heinz. Mr. Chairman, how much have we saved
23 out of these four here?

24 The Chairman. Well --

25 Mr. DeArment. Since we put one and three aside, we

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1 have \$1.6, \$.7, \$2.3, plus I think Senator Baucus thought
2 his proposal -- was it \$140 the first year?

3 Senator Baucus. It was \$140 in the first year and
4 \$40 or so the second.

5 Senator Heinz. That would be about \$2.3 or \$2.4 billion
6 over three years?

7 Mr. DeArment. Yes, maybe \$2.5, I would think.

8 Senator Heinz. Mr. Chairman, that is great news. Do
9 you realize that it will only take three more days for
10 the national debt to increase to the amount we just saved?

11 The Chairman. I wouldn't want to predict that we
12 are going to save anything with these gimmicks -- not
13 gimmicks, but it is mostly smoke. Anytime you get the IRS
14 to do anything, it will be less than smoke.

15 Senator Heinz. I just don't want us to rest on our
16 laurels because -- no offense -- our savings will have
17 disappeared in --

18 The Chairman. Now, we are getting into the real -- I
19 won't say what I had in mind -- but very difficult choices.
20 I think if we could agree on Senator Moynihan's proposal.
21 I would hate to do it in his absence, but I think we will
22 send for him. Jim, do you have some more information on
23 the Moynihan minimum tax?

24 Mr. Wetzler. We have got the revenue estimate which is
25 \$2 billion over the 1985 through 1987 period.

1 The Chairman. Did you have the example?

2 Mr. Wetzler. We are still working on getting some
3 examples worked out.

4 The Chairman. I think Lloyd and some others wanted to
5 see some examples. Can you show us how it works on the
6 blackboard?

7 Mr. Wetzler. Yes. Should we put some examples on
8 the blackboard and then wheel it out?

9 The Chairman. Sure.

10 Mr. Wetzler. Let Randy put an example on there.

11 Senator Bentsen. Let me ask you, Mr. Chairman, if you
12 have real losses in some of these investments -- where you
13 might be in syndications -- would you be in a position to
14 be able to charge those against your other income?

15 Mr. Wetzler. What this proposal does is it lets you
16 elect to defer those losses and deduct them in a subsequent
17 year, in effect -- carry them over.

18 Senator Bentsen. So, the answer is no. You would then
19 defer them, and hope you made some profits in the same types
20 of investments in the future. Is that the idea?

21 Mr. Wetzler. Yes.

22 Senator Bentsen. So, you get a real loss. You get
23 no charge-off. You have to hope you are going to have a
24 profit sometime in the future.

25 Mr. Wetzler. That is right. In that respect, it works

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1 the same way as the rules do today regarding capital losses,
2 which are only deductible against a limited amount of
3 ordinary income, and if you don't have capital gains, you
4 have to carry the losses forward.

5 Senator Bentsen. So, it isn't just limited to paper
6 losses.

7 Mr. Wetzler. That is right.

8 Senator Bentsen. It is real losses.

9 Mr. Wetzler. Yes.

10 (Pause)

11 Mr. Wetzler. Senator Bentsen, one other feature of the
12 proposal is that you don't have to defer the loss forever.
13 You can take the loss when you sell your investment.

14 Senator Bentsen. And hope you have a profit.

15 Mr. Wetzler. No. When you sell the investment, you
16 can in effect close out the --

17 Senator Bentsen. Then you take your capital loss.

18 Mr. Wetzler. These are ordinary losses, but then you
19 can take them under Senator Moynihan's proposal.

20 Senator Bentsen. I don't believe that your analogy
21 against capital losses is appropriate. That was part of
22 the trade-off -- really, it seems to me -- for the fact that
23 you pay a lower tax on a capital gain.

24 Mr. Wetzler. Originally, the capital loss limitation
25 came in in the depression when apparently some high income

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1 taxpayers who had a lot of paper losses realized enough losses
2 to zero out their tax, and it became something of a cause
3 celeb, and Congress acted at that time to put a limit on it.

4 Senator Bentsen. Jim, what I am concerned about -- you
5 know, I can understand the merits in trying to do something
6 about paper losses -- but if we are talking about real losses
7 -- a guy really has lost the money -- and then say he can't
8 charge it off against his other income, but he has to hope
9 that someday in the future that he will have some profits
10 in those syndications or that he may finally just give up
11 and sell them out.

12 I have some concerns about that kind of an approach.

13 Mr. Wetzler. I think that is a legitimate concern,
14 and I am not trying to defend the proposal, but keep in mind
15 that we are talking about the minimum tax -- not the regular
16 tax -- a 20 percent tax at a maximum -- and you are talking
17 about not an elimination of the deduction permanently, but
18 rather a requirement in effect that you defer the deduction
19 until you have either got enough income from similar types
20 of activities to deduct those losses against that income
21 or you dispose of the investment and at that point you can
22 deduct the losses that you have been deferring for minimum
23 tax purposes.

24 Senator Moynihan. When the loss becomes real.

25 Mr. Wetzler. Yes.

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1 Senator Bentsen. Oh. No. The losses-- We got to that
2 very point. The loss is real in the year, and you can't
3 take that real loss. I said, you know, if it is a paper
4 loss, that is a different situation, but he says it is a real
5 loss. And if you have it, say in 1984, that you cannot
6 charge it against your 1984 income.

7 And there is a point you know where you push that too
8 far, and there is a point where you just sink the fellow.

9 Mr. Wetzler. The theory of Senator Moynihan's proposal
10 is that you can't really distinguish between real losses
11 and paper losses all that well, and therefore at least for
12 minimum tax purposes, you ought to have a blanket rule.

13 Senator Bentsen. But you can, then, it seems to me,
14 get in a situation where a fellow could have a -- he could
15 have actually had in real losses -- more money than he made.
16 And you would then still have him hit with a minimum tax?

17 Senator Moynihan. Well, Senator Bentsen --

18 Senator Bentsen. Please let me have him answer that
19 question.

20 Mr. Wetzler. Yes, you could have those situations.

21 Senator Bentsen. You could actually have real losses,
22 lost more than he had in the rest of his income and still
23 pay the minimum tax. Is that right?

24 Mr. Wetzler. Yes.

25 Senator Moynihan. Senator, I know that Mr. Hardee can

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1 speak to that point, which is the question of what kind of
2 taxpayers are these. These are very high income taxpayers
3 who have losses and gains and --

4 Senator Bentsen. Senator, I just said that he is not
5 a high income taxpayer if he has just lost more than he made.
6 That is negative.

7 Senator Moynihan. Would that put him into a negative
8 tax situation?

9 Mr. Hardee. This instance will fall mostly on people
10 with high net worths, not necessarily high incomes -- high
11 net worths.

12 Senator Bentsen. Well, that is a different ball game.
13 Would you then want to put a tax on capital? Have we
14 started that now?

15 Mr. Hardee. A typical situation -- more typical than
16 someone who has zero net worth and \$200,000.00 of income
17 and \$200,000.00 real loss -- would be the situation where
18 you have a person with a net worth of \$10 million. He has
19 \$200,000.00 in income. He is able to realize losses of
20 \$200,000.00 because he can select whether he realizes gains
21 or losses, and he defers recognition of the gain side and,
22 in fact, his net worth can go up while his tax liability
23 remains negligible.

24 Just be selectively realizing his losses, and not
25 realizing his gains.

1 Senator Bentsen. But you have also stated to me -- and
2 as I understand it -- and said that if he has a loss that
3 exceeds his income -- a real loss, not a paper loss -- that
4 you are still going to tax him. And now, you come to me and
5 justify it because you say he has wealth.

6 Now, if we are reaching that point, then we are talking
7 about starting, it seems to me, to put a tax on capital, and
8 that is a dramatic change in this country. That is being
9 now done in France. I just want to fully understand what
10 we are doing here.

11 I am after the phony bookkeeping and the paper losses
12 that are not real. And we really ought to approach that
13 problem and try to take care of it. And where a fellow
14 actually makes an income -- net income -- real -- then he
15 darned well ought to pay the taxes. And these people that
16 do the paper route and have enormous incomes and pay no
17 taxes, that is what we try to address and that is why I
18 supported the minimum tax and fought for it.

19 But I want to be sure that that is what we are doing.
20 I am not sure I wouldn't be for what Senator Moynihan is
21 talking about, but I want to be sure that I understand it.

22 Senator Moynihan. Can we ask if this distinction cannot
23 be made between paper losses and real losses?

24 Mr. Wetzler. Would it be helpful if we try to come
25 back later with a proposal that tries to better specify the

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1 distinction between the real losses and the paper losses?

2 Evidently, this is a real problem.

3 The Chairman. It would be because I share the concern
4 expressed by Senator Bentsen.

5 Senator Moynihan. But, Mr. Chairman, that is right, but
6 I hope we don't go away from this subject with the notion
7 that we really aren't going to get back to it.

8 The Chairman. Oh, no.

9 Senator Moynihan. Because this country is just filled
10 with very rich people paying no taxes, and every time we
11 get the idea of how to check up on somebody on food stamps,
12 why that goes right through this procedure. But when we
13 get to people who are on the minimum tax -- and after all,
14 they are paying 20 percent because they raised their taxes
15 so that very wealthy people pay the marginal tax rate of
16 persons making \$17,000.00, and they don't even pay that.

17 And now we have a problem that we can address. Let's
18 go back to food stamps -- which is where we are happiest --
19 but let's not forget that --

20 Senator Bentsen. Well, I really don't think that is
21 a fair statement, Senator. That is not correct. I think
22 the Senators around this table have shown their concern
23 and their compassion to the question of Medicare and
24 Medicaid and food stamps and the rest of it, and I am going
25 to continue to.

1 I spent a good part of yesterday working on a problem
2 in south Texas, and where we have the lowest per capita
3 income in the United States and have as much as 42 percent
4 unemployment in one of the counties. And I am going to
5 continue to do that, but I also want to understand the
6 tax structure of this country and what we are trying to do
7 here.

8 Senator Moynihan. I wonder if we could just -- while
9 we have the example on the board -- have Mr. Wetzler take
10 us through the example.

11 The Chairman. I want Treasury to comment. I know you
12 are not in a position to make a final judgment.

13 Mr. Pearlman. Yes, we definitely have interest in the
14 proposal. I think the main thing is we do want to make sure
15 how it works and who it hits. We want to look at the
16 revenue impact. We want to look at the distribution effect.

17 One of the things for example, that we are somewhat
18 concerned about is the way, as we understand the proposal,
19 there will be a premium on taxpayers who have income from
20 businesses, and we want to make sure that that doesn't
21 produce a shift out of stock investments or debt investments
22 into businesses which may not be good for the overall
23 economy.

24 So, there are a number of broad issues that need to be
25 looked at, but we do have interest in the proposal, and we

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1 want to keep looking at it.

2 The Chairman. When do you think you might have that
3 information, because we would like to finish this some time?
4 You know, this whole package.

5 Mr. Pearlman. We are working on it. We have people
6 now presently looking at it. We have our economist looking
7 at the proposal, trying to figure out exactly what we think
8 it means and trying to coordinate with the staffs. I think
9 that is the best I can tell you.

10 Senator Bentsen. Mr. Chairman, I would like to also
11 comment, in regard to the comment from my good friend from
12 New York. I spent a good deal of time yesterday trying to
13 put \$2 billion more taxes on people who are building
14 commercial buildings that I think have an advantage beyond
15 what they should have, and where we are seeing some
16 substantial abuses in that 15-year period on commercial
17 building.

18 So, I hope that I am being evenhanded here. At least,
19 I am trying to.

20 Senator Symms. Mr. Chairman, one thing I would like to
21 ask the tax people to look at when they are looking at this
22 proposal. I understand what the Senator from New York is
23 trying to get at, and I think that it bothers all of us
24 to think that someone can have high income and not pay any
25 taxes, but my concern is that it seems like what this might

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1 do is -- to the person who already has wealth, that is one
2 thing -- but to the guy who doesn't have the wealth and who
3 is working by the hour, he is not ever going to get rich
4 working by the hour. So, he wants to go out here and invest
5 in some endeavor and take a risk, and if they take a risk
6 and lose, they should be able to deduct that off their
7 earnings.

8 I personally disagree with our law on capital losses.
9 I don't think it is fair when people have capital losses
10 that are, in fact, real -- in the stock market or other
11 markets like that -- they can't deduct off except \$3,000.00
12 a year. And that discourages people from taking risks.

13 And I am afraid that if you try to get at this, you
14 had better be careful or the target you are shooting at
15 will be missed, and what you will hit is the person who
16 is not part of the wealthy that you are trying to get at,
17 but is the young wealth and wants to-- And I think that
18 is one thing Treasury should look at and come back with
19 some kind of -- how does this affect the person who is --

20 Senator Moynihan. Could I say something? We are only
21 talking about the people who are using the minimum tax,
22 which is hardly the kind of person you are talking about.
23 But could Mr. Wetzler explain his example?

24 Senator Symms. Let's take somebody right here that
25 works on the Senate staff and say they make \$50,000.00 a

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1 year, and they don't have wealth. They are working, so to
2 speak, by the hour. And they go out here and invest in some
3 kind of a business that loses money. Why shouldn't they
4 be able to deduct that off their income tax?

5 Senator Moynihan. They are.

6 Senator Danforth. Mr. Chairman, it seems to me that
7 this doesn't have anything to do with the proposal. Maybe
8 I am wrong. My understanding of the proposal is that this
9 goes as the question of sheltered income. This is not --
10 we are not talking about business losses. We are talking
11 about shelter arrangements, and we are not even saying
12 that they are prohibited.

13 We are simply saying that henceforth people cannot so
14 arrange their affairs so that they virtually pay no taxes
15 at all on large incomes. It seems to me that that is
16 perfectly possible to get at without touching the Senate
17 staffer who goes out and buys a hamburger stand.

18 (Laughter)

19 Senator Boren. Mr. Chairman, let me ask this question
20 of Mr. Wetzler. Let's suppose that you had a Senate staffer
21 that had a salary of \$40,000.00 a year -- a committee staffer.
22 They decided they would become a passive investor, believing
23 some of the rhetoric we hear around this table about oil
24 and gas, and they decided that they would become a passive
25 investor, and they take \$60,000.00 that they have saved up

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1 or inherited or otherwise -- they probably haven't saved it
2 on their Senate salary, but maybe it came to them through
3 an inheritance or otherwise -- and they go put \$60,000.00
4 as a passive investor in an oil-drilling operation. And it
5 just happens that -- maybe it was one of those Penn Square
6 bank deals -- and it was all dry holes. So, they have lost
7 \$60,000.00 out of pocket.

8 They are passive investors. Can they offset that
9 \$60,000.00 loss against their \$40,000.00 salary?

10 Mr. Wetzler. As I understand the proposal, Senator
11 Boren, when they dispose of the investment -- so, when all
12 the wells are dry and they finish investing in that
13 partnership -- at that time, they could deduct the \$60,000.00
14 against their ordinary income for both regular and minimum
15 tax purposes.

16 And I assume that if they are drilling the dry holes,
17 that it will all be over fairly quickly. On the other hand,
18 if they drill successful wells, they get intangible drilling
19 costs -- those are currently subject to the minimum tax.

20 Senator Moynihan. You have to have a \$40,000.00 income
21 before you even start tabulating this. And if you have
22 lost your money, you have lost your money.

23 But this has to do with the shelter arrangements in
24 which it is arranged without disposing of the investment
25 and you take a huge loss in the first year, and that is why

1 you do it. It is a form of straddle, and it is genuinely
2 spreading like the commodity straddles are spreading.

3 Senator Boren. I want to see us avoid that, but I am
4 just concerned in the way some of the mechanisms are set
5 up that you do not have a person -- as Senator Bentsen was
6 saying -- that has an actual real loss that is prohibited
7 because it is a passive investment -- a loss on the passive
8 side as opposed to the active earning side.

9 Mr. Wetzler. Could I suggest that you take a look,
10 for example -- you could have a special rule that would
11 exempt from the proposal dry-hole losses because there you
12 obviously really have lost your money.

13 Senator Moynihan. Sure.

14 Mr. Wetzler. And we can perhaps come up with something
15 to deal with that.

16 Senator Symms. What if it is a restaurant or a service
17 station?

18 Mr. Wetzler. Under the proposal, if the taxpayer
19 actively participates in the management of the business,
20 then it does not apply to him. It applies to limited
21 partners and other businesses where you are not an active
22 participant in the management.

23 Senator Symms. That is the most anti-entrepreneurial
24 thing I have ever heard of. In order words, you want to
25 tell people not to go out and take a risk -- don't try to

1 get a business. I mean, if you have got \$10 million, that's
2 great, but if you don't have \$10 million and you would like
3 to make \$1, you are cutting that person off.

4 Senator Bentsen. Mr. Chairman, let me say that Jim has
5 said that he will try to come up with something that tries
6 to separate a real loss from a paper loss, and that is what
7 I am looking at.

8 I am not giving any solace to those that have paper
9 loss deals where there are shams and that type of thing, but
10 if he can better define it, let's see if that can be done.

11 Senator Bradley. Mr. Chairman?

12 The Chairman. Let's try to move onto something else
13 here. We would like to raise \$10 billion before lunch.

14 (Laughter)

15 Senator Bradley. You say that right before you yield
16 to me. I think it is a good idea to try to do what Senator
17 Bentsen has suggested, but I think that the proposal itself
18 is an important proposal. I mean, ten years ago, there were
19 about 400 tax shelter cases in some stage of audit appeal
20 or litigation, and now there are 327,000. And a lot of
21 these are just total flimflam, and you have to find some
22 way to get at them.

23 It seems to me that this is at least an opening and that
24 we should move in that direction.

25 The Chairman. Let's give --

1 Senator Moynihan. Mr. Chairman, we will pass on, but
2 let's not leave it before we understand that there is an
3 industry that has grown up in this country that is for the
4 specific purpose of providing wealthy persons with tax losses
5 that permit them not to pay taxes. And we have chased it
6 around a dozen ways, and this is a different strategy.
7 This goes to the end result with actual income tax return.
8 We could raise the minimum tax to 50 percent, and I don't
9 know why we shouldn't -- set up a marginal rate.

10 The Chairman. Let's go on to something else, but let's
11 have Treasury work with the Joint Committee and our staff
12 on this proposal. We have to make some judgments here sooner
13 or later, and I would like to move on to something that
14 we might make a judgment on.

15 What about structures? Let me suggest right now. We
16 have on the spending side about \$26 billion, and on the
17 revenue side about \$39. And as I understand, a lot of
18 conversation around here with different people, that we
19 ought to put together a three-part package, so we still
20 have quite a way to go on the revenue side.

21 I think our spending side -- if the Appropriations
22 Committee what they are suggesting -- freeze at a certain
23 level -- that will pick up about \$13 billion. There is some
24 hope of getting some in the USDA area, but I think we are
25 still short on the revenue side, and what we are considering

1 are those that have been recommended by the Administration.

2 Do you have any recommendation to make now? Secretary
3 Regan indicated at one of the White House meetings a few
4 days ago that he would take a look at the charitable
5 contribution and try to come up with some different
6 suggestion and give it to us. Have you had any --

7 Mr. Pearlman. That has not been communicated to us,
8 so I am not aware of that. I can't comment on that.

9 The Chairman. I know that Senator Packwood has strong
10 views on that, as I presume others have.

11 Senator Packwood. Mr. Chairman, I do have strong views
12 on it, and I would just as soon put it to rest by striking
13 out any further consideration of the charitable limit
14 capping this charitable deduction that we just started down
15 the road on three years ago in the hopes of encouraging
16 not appreciated paintings donated to the New York
17 Metropolitan Museum of Art, but \$15 and \$20 and \$25
18 contributions to the Baptist Church and the Catholic Youth
19 Organization.

20 You are talking about a very, very minimal encouragement
21 for small charitable donations at a time when we are cutting
22 out funds from groups that are going to have to be heavily
23 supported by charity. I think we ought to strike out the
24 issue and not any further consider it.

25 Senator Moynihan. Mr. Chairman, if I could just add to

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1 that. We worked hard at this legislation, and there was an
2 enormous constituency that came to us and asked for help in
3 this matter, and they could show that the gradual increase
4 in the zero bracket, as we call it, has really hurt them,
5 and these are institutions you can't live without in this
6 kind of country.

7 The Chairman. I don't know that I quarrel with any of
8 that, but let's just vote on number six. 20-year life for
9 nonresidential structures. That is a proposal of Senator
10 Bentsen. We have put all these down. If somebody has a
11 better idea, then we are going to have to do it.

12 We were talking that first day about \$200 billion, and
13 now we are up to \$39 on the revenue side -- we weren't
14 talking about the revenue side.

15 So, I just think we have to make some very difficult
16 choices. We are doing it in public session, which makes
17 it a little more difficult, but do you want to restate that
18 proposal, Lloyd?

19 Senator Bentsen. Yes. What I have proposed, and I
20 understand a pretty effective lobbying job has been done
21 by the Real Estate Association in the last couple of days --
22 opposing my amendment -- but it picks up another \$2.1 billion
23 in revenue, and would be addressed to the commercial sector
24 buildings -- both new and used.

25 There is no question as to what there have been abuses

1 in syndications, both in commercial structures and in
2 housing. And I know that. But there was a preference given
3 to housing and a substantial one before ACRS came along.

4 That preference was narrowed by ACRS. I am trying to
5 restore some of it because people are having a pretty tough
6 time meeting the costs of housing, and that is certainly
7 true whether you are talking about apartments, or you are
8 talking about someone renting a duplex and the rest of it.

9 If you extend the 20-year life to housing, there is
10 no question but what you raise the rents. If you extend
11 the 20-year life to commercial buildings, that is true also,
12 but I am not as concerned about that as I am about housing.

13 We lowered the useful life on most commercial properties
14 -- and Rich, or Jim, you correct me if I am wrong on this --
15 but as I recall, most commercial buildings -- office
16 buildings and the rest of it -- useful life was probably
17 30 to 40 years. And now, we have reduced it to 15, and two
18 years ago when that was done, I stated that I thought we
19 were being too generous. I finally went along with it, but
20 I think now the events have proven that to be too generous.
21 And I would like to see it moved on up to 20 years, and I
22 believe that will curtail some of the abuses.

23 That is my suggestion, and if we do it fine, and if we
24 don't, we will try to find the revenue someplace else.

25 Senator Danforth. Mr. Chairman, I understand the

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1 Bentsen proposal. I also understand the point that Treasury
2 was making yesterday relating to churning. Is the
3 alternative to Senator Bentsen's proposal still the original
4 proposal relating to --

5 The Chairman. Used structures.

6 Senator Danforth. Used only without the differentiation
7 between housing and industrial and commercial. I mean, has
8 there been any fine-tuning of that in the last 24 hours by
9 the Treasury?

10 Mr. Pearlman. Other than the assumption, Senator
11 Danforth, that whatever we did there would probably be
12 something done with low-income housing but not other than
13 that. Our preference is for a new versus used distinction,
14 rather than a residential versus nonresidential, because
15 our concern is with the churning of property that has been,
16 at least in part, attributed to the shorter life on ACRS.

17 We would prefer to go with the used distinction.

18 Senator Danforth. All right. Mr. Chairman, how are
19 we proceeding? Are we going to vote on the Bentsen
20 proposal and, if that fails, then vote on the original
21 proposal?

22 The Chairman. That is correct. Let's call the roll.

23 Mr. DeArment. Mr. Packwood?

24 Senator Packwood. Aye.

25 Mr. DeArment. Mr. Roth?

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

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1 Mr. DeArment. Mr. Baucus?

2 Senator Baucus. Aye.

3 Mr. DeArment. Mr. Boren?

4 Senator Boren. Aye.

5 Mr. DeArment. Mr. Bradley?

6 Senator Bradley. Aye.

7 Mr. DeArment. Mr. Mitchell?

8 Senator Mitchell. Aye.

9 Mr. DeArment. Mr. Pryor?

10 Senator Pryor. No.

11 Mr. DeArment. Mr. Chairman?

12 The Chairman. Aye. And Mr. Heinz votes no.

13 The ayes are 10. The nays are 5. The amendment is
14 agreed to.

15 Senator Chafee. Mr. Chairman, I would like to now
16 proceed to amend that further by including what you might
17 call everything but low-income housing, and is there such
18 a term as "moderate income housing"?

19 If not, I would go for everything except low-income
20 housing. I don't get the distinction here. You get something
21 like Trump Towers. I suppose that is housing. It is
22 condominiums that they sell. Now, under this proposal, they
23 are entitled to the 15-year depreciation. Is that right?

24 Mr. DeArment. That is correct. If it is a residential
25 unit, then we didn't affect it at all.

1 Senator Chafee. My heart doesn't bleed for that group
2 too much. And I don't see why we shouldn't-- Is there any
3 way of drawing a distinction above low-income housing -- some
4 cut-off understandable?

5 Mr. Wetzler. Senator Chafee, there is already a
6 definition for IDB purposes -- what structures are eligible
7 to be financed with IDBs -- that is a fairly broad definition
8 because you only have to be low to moderate income for a
9 certain limited period of time. But if you picked up that
10 definition, you would basically be only applying your rule
11 to the relatively luxury structures.

12 Or you could tighten up the IDB rule in a number of ways.

13 Senator Chafee. Using that IDB definition in housing,
14 what is the down side if we proceeded with making anything
15 above that subject to the 20-year depreciation?

16 Mr. Wetzler. I would say that to the extent there is
17 a down side, it is probably the additional complexity
18 resulting for having different rules for depreciation. Now,
19 you would be in a situation where there would be one rule
20 for low-income housing, a different rule for moderate-income
21 housing, and then still a different rule for other housing.

22 Senator Chafee. We are only talking 15 years versus
23 20 years. Isn't that what we have got?

24 Mr. Wetzler. But today low income gets -- you have
25 already agreed not to slow down depreciation -- today low

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1 income gets a 200 percent declining balance, and other housing
2 gets 175. So, there is already a distinction between low
3 income and other housing today.

4 As I said, you asked for the down side -- the down side
5 is really simply the additional complexity that would result
6 from having now three categories instead of two in the
7 housing area.

8 Senator Chafee. That doesn't bother me very much.

9 The Chairman. How about Treasury? Could you help on
10 this?

11 Mr. Pearlman. I think the IDB definition would be --
12 I think we could work with that as a dividing line. I think
13 it needs to be refined, perhaps, a little bit, but I think
14 if the committee chooses to make-- I think we are not in
15 favor of a housing versus commercial property distinction,
16 so I think we would be supportive of Senator Chafee's
17 effort to eliminate that distinction. And I think we can
18 work out a moderate income definition along the lines of
19 the IDB definition, at least we would like to take a look
20 at it and define it a bit.

21 Senator Chafee. On that basis, I would move to amend
22 the vote we have just had by including anything above the
23 IDB definition, include that in the category that we have
24 already approved -- namely, the 20-year depreciation.

25 The Chairman. What is the IDB definition again?

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1 Mr. Susswein. The standard for industrial development
2 on low income -- actually it is low and moderate income -- is
3 that 20 percent of the residents have to be below, and 80
4 percent in median income. But there is no restriction on
5 the remaining 80 percent. So, you can still have a project
6 with a small number of people who are low or moderate income,
7 but the substantial majority would be of any income
8 whatsoever.

9 Senator Bradley. So, would the effect of that be that
10 someone that was building a high luxury apartment building
11 in order to qualify for the 15-year write-off might indeed
12 subsidize the rents of the people who would be 80 percent
13 of medium income?

14 Mr. Susswein. That is the theory, Senator, of the
15 income skewing concept -- or the rent skewing concept. The
16 question, of course, is whether or not the detriment to
17 the landlord -- that is, the amount of rent skewing that
18 is necessary to help that small fraction of low-income
19 people -- is disproportionate to the benefit that he is
20 getting with respect to the remaining 80 percent.

21 Senator Bradley. So, the owner of the Trump Tower would
22 be-- Would it be in his interest -- not the Trump Tower --
23 but any luxury building to essentially go out and find the
24 number of people necessary to qualify for the more rapid
25 depreciation? My point is simply to say that -- now this is

1 the old battle between equity and simplicity. And we
2 complicate it more when we try to do what Senator Chafee
3 wants. I support what Senator Chafee wants to do, and I
4 would vote with him to do it, but is there any way we could
5 do it so that it would be a little simpler?

6 Mr. Susswein. Yes, Senator.

7 Senator Chafee. How about Treasury? Treasury indicated
8 -- had some thoughts. Mr. Pearlman?

9 Mr. Pearlman. I think if you are going to do something,
10 Senator Chafee, I think the thing to do is to stay with
11 the specificity of the IDB rule to try to avoid what Senator
12 Bradley is suggesting -- that is more complexity. Just
13 tinker with those percentages and see if, by tinkering with
14 the percentages, we can come up with a rule that the
15 committee is more comfortable with.

16 Senator Mitchell. Before we vote on it, is there any
17 way of estimating what this would do on the revenue side?

18 Mr. Wetzler. We have an estimate for what would happen
19 if you went to 20 years for all residential housing, and
20 that would be about \$1 billion over the three years. Now,
21 this is obviously substantially narrower than that. We
22 are going to have to take a look at just how much is caught
23 by this. That is the best I can do right now.

24 Senator Pryor. Mr. Chairman.

25 The Chairman. Mr. Pryor?

1 Senator Pryor: I really don't want to be an obstacle
2 in this proceeding, but I was out of the room just a moment
3 ago when the vote was called for and I probably would have
4 been defeated anyway.

5 It worries me that we really are changing a basic
6 policy of this country without sufficient information to
7 know what the impact is going to be. Here, even after the
8 fact, or after this vote, we are beginning now to see
9 figures which may or may relate, and I truly believe that on
10 a matter of this significance we ought to at least have a
11 hearing. And I am not asking that the vote be vitiated.
12 I am asking that we consider, Mr. Chairman, having a hearing
13 on this issue. New versus old. Commercial versus
14 residential. And basically the impact that this is going
15 to have should we vote it up or down.

16 And that is all I am asking -- for a little additional
17 time to hold a hearing before we put this basically into
18 concrete and send it to the floor of the Senate. To be
19 able to tell our colleagues that here is what it is going to
20 do and here is what it is not going to do, should we make
21 these changes.

22 Now, I am wondering if that is too much to ask. I am
23 not going to once again ask that the vote be vitiated, but
24 I am wondering if there is a possibility of a hearing to
25 allow the parties to come before this committee and express

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1 to this committee the impact that they feel it might have on
2 this country.

3 The Chairman. That is something that I would certainly
4 consider, but I assume that the same case could be made
5 for nearly every other thing we have done. I think that,
6 obviously, those who don't want anything to be done will
7 be at the hearing with some very bad stories about what it
8 is going to do.

9 We have had a hearing. We had a hearing in 1981, and
10 many on this committee felt we were too generous at that
11 time -- in a rather extensive hearing. They predicted, in
12 fact, what was going to happen -- there would be a lot of
13 churning, a lot of people getting very rich because of this
14 very generous treatment.

15 I don't know but what the House may consider this, too,
16 today, but I don't want to say that we will not have a
17 hearing. I would be willing to try to put one together.

18 If we can sort of leave it at that, maybe two of us
19 can work out some time.

20 Senator Symms. Mr. Chairman, I would just like to ask
21 a question. How many months -- not years -- but how many
22 months have we had the present depreciation rules on the
23 books actually in effect? Since July of 1981 or when was it?

24 Mr. Wetzler. It was August in 1981 -- when you passed
25 the 1981 Act. It was effective as of January 1, 1981. So,

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1 really, they have been in effect for a little over three
2 years.

3 Senator Symms. Two and a half years.

4 Mr. Wetzler. Three years and a month. Three years
5 and two months.

6 Senator Symms. So, in terms of business decisions in
7 commercial construction, we have only had the word has barely
8 gotten out in the countryside of what the rules are now,
9 I suppose. Now, we are talking about changing it again.

10 Mr. Wetzler. Interest rates are a big factor in real
11 estate as well, and interest rates have fluctuated somewhat
12 more violently than the tax law has in the last few years.
13 They may fluctuate some more in the future unless something
14 is --

15 Senator Symms. Mr. Chairman, I suppose I should have
16 spoken up before the vote. It seemed like it happened
17 awfully fast. I just absolutely --

18 The Chairman. We debated this at length yesterday.

19 Senator Symms. I realize that and I was here yesterday,
20 and I heard it. But I just can't imagine why this committee
21 and the rest of the Congress seem to be so afraid to cut
22 spending. I mean, we are not going to solve any problems
23 by trying to tamper with the tax law. This is just TEFRA
24 all over again.

25 And when you get through with it, the budget deficit is

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1 still going to be. The only way we are going to solve this
2 is to take an across-the-board cut and cut everything about
3 10 percent.

4 Senator Bradley. This is better than TEFRA.

5 The Chairman. I will vote with you if you can get the
6 President to sign up for that spending reduction. We have
7 already done more on the spending side than the White House
8 recommends.

9 Senator Symms. I appreciate that, and I support you on
10 that, Mr. President -- Mr. Chairman -- but --

11 (Laughter)

12 The Chairman. You have got me mixed up with Gary Hart.

13 (Laughter)

14 Senator Symms. If I can just finish, I will just say
15 what I said yesterday again. Changing those depreciation
16 rules like that really hit the small businessman. It is
17 the same thing as -- these things all sound good and there
18 probably are some abuses -- but there is a small businessman
19 out there somewhere that is still waiting for the 10-5-3
20 before he goes forward to build his warehouse. And by going
21 the other way, it just seems like it is totally wrong
22 policy -- we should be working towards expensing -- 100
23 percent expensing -- in my opinion, instead of going towards
24 the other direction. We are going the wrong way with all
25 of these changes in the Tax Code to what will encourage

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1 investment and encourage entrepreneurial activities that we
2 need in this country.

3 Senator Durenberger. Mr. Chairman, before we go to
4 John's proposal, let me go back and suggest that there is
5 some merit in your making a commitment of some kind to look
6 at this issue at hearings.

7 I am inclined to go along with John, too, but I know
8 when we get into housing, we are in an area where nobody
9 can afford anything. And we have been mickey mousing this
10 whole capital issue in housing for so long that none of us
11 even know where the income limits are on IDB.

12 And if we are going to pursue John's amendment, I think
13 a lot of us would like to see a commitment from you that
14 we have a hearing before we take this to the floor.

15 Senator Chafee. Mr. Chairman, let me just say this.
16 I know about the housing market to some degree, and the best
17 thing we can do for the housing market is to reduce this
18 deficit so the interest rates will come down. And what is
19 going to surge the housing market isn't whether there is a
20 20-year depreciation or a 15-year depreciation or anything
21 like that. It is the interest rates. That reflects-- That
22 causes changes in the housing starts more than any other
23 element.

24 And if we can do something significant up here, then
25 we will really be making progress, and here is a step toward

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1 that direction. Sure, it produces some revenue, but also
2 to me it is an equity measure -- we get both.

3 So, Mr. Chairman, I would move that we apply the Bentsen
4 amendment to residential housing with the exception of low
5 income and moderate income housing which can be defined
6 -- which the Treasury can come forward with a definition
7 with our people.

8 The Chairman. Wouldn't it better to have the Treasury
9 come forward with a definition first?

10 Senator Chafee. Well, I have got some momentum rolling
11 here, Mr. Chairman. I am reluctant to let it go.

12 The Chairman. I don't know, but Senator Bentsen --

13 Senator Bentsen. I would like to know what moderate
14 income is.

15 The Chairman. Maybe we can have that by 2:30 p.m.

16 Senator Chafee. I hate to move with too many facts
17 -- that always drags things down.

18 (Laughter)

19 Mr. Wetzler. Mr. Chairman. Basically, Senator Bentsen,
20 under the IDB definition, 20 percent of the people have to
21 have incomes below 80 percent of the median income. That is
22 a fairly generous rule in the sense that you only have to
23 have 20 percent low and moderate income people in the
24 building. Now, we can come up with -- if the Committee
25 wants -- tighter rules that require higher percentages than

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1 20 percent or --

2 The Chairman. We can find a better way than that.

3 Senator Chafee. I would like to see it tighter than
4 that. I think Mr. Pearlman and Mr. Belas can contribute.

5 Mr. Susswein. Senator, there is one approach we could
6 take to avoid the problem that Senator Bradley pointed out
7 about the different percentages. We could adopt a rule.
8 The current law has a definition of low income, which says
9 essentially all of the residents have to be below 50 percent
10 of the median income. We could just say the same thing
11 except raise the income level to 80 percent of average
12 area median income.

13 Senator Bentsen. Why don't you take some time and come
14 back with something?

15 The Chairman. Senator Packwood?

16 Senator Packwood. Are we done with this issue for the
17 moment?

18 The Chairman. I think Senator Armstrong had something.

19 Senator Armstrong. I just wanted to comment, Mr.
20 Chairman. I guess my proxy was voted against the proposal.

21 The Chairman. I didn't have your proxy.

22 Senator Armstrong. In any case --

23 The Chairman. I would like to have it.

24 Senator Armstrong. I am opposed to it, but I don't want
25 to relitigate the issue, but I understand that after the

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1 vote that Senator Pryor arrived and announced that he felt
2 we ought to have a hearing before we do this, and I want to
3 associate myself with that. I must say I am really
4 flabbergasted to think that the Finance Committee is adopting
5 a change of this import with no notice, no hearing, and then
6 putting it in a bill which is intended to go to the floor
7 as a reconciliation measure where it is subject to limited
8 amendment.

9 Aside from the fact that I am skeptical of the change
10 to begin with, that procedure, it seems to me, is not a good
11 one, and I would hope that at the right time maybe we could
12 reconsider it.

13 Senator Packwood. Mr. Chairman?

14 The Chairman. Senator Packwood?

15 Senator Packwood. I would like to put at rest this
16 charitable issue. I would like to move that we dispense
17 with further consideration of it and simply leave the law
18 where it is, which will phase in that four-year phase-in
19 that we started two years ago.

20 The Chairman. Okay. Let's call the roll.

21 Senator Mitchell. Mr. Chairman, before you do, for
22 myself at least, let me explain how this will work in
23 practice.

24 The Chairman. What Bob is saying is that we just take
25 it off the list. Right?

1 Senator Mitchell. Yes, I know, but before I vote for
2 or against it, I would like to know how it works.

3 Mr. DeArment. We have two variations of --

4 Senator Packwood. You want to know how it works now,
5 don't you? What the law is at the moment.

6 Senator Mitchell. Yes. In other words, you say it
7 is for nonitemizers. Does a person have to itemize?

8 Mr. DeArment. Basically, that is right. That put
9 that above the line in computing what their adjusted gross
10 income is, so that under current law -- say that you
11 contribute \$200.00 and you are not going to itemize. You
12 take 25 percent of \$200.00 and then you put that in computing
13 your adjusted gross income.

14 Senator Mitchell. Is the taxpayer required to itemize
15 the charitable deductions, even though it is not --

16 Senator Packwood. Not in the normal sense that you mean
17 itemize. This is an above-the-line deduction. It is
18 designed to encourage people to give to charities who do
19 not normally itemize.

20 Senator Mitchell. That is a notable goal, but I wonder
21 is there any mechanism for policing this? If you don't have
22 to identify who you give it to, and you are talking about
23 a large number of returns.

24 What is the mechanism for determining that everybody
25 who simply takes 25 percent of the stated figure in fact

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1 contributed?

2 Mr. DeArment. That is just the normal audit process.
3 If you happen to be one of the ones that half percent of
4 people that get audited.

5 Senator Packwood. That is no different than an itemized
6 charitable deduction.

7 Mr. Wetzler. But, Senator, one of the criticisms of
8 this proposal that was made in the debate on it back in
9 1981 was precisely that it is very hard to enforce because
10 you would be greatly adding to the people who would be
11 putting items on their return. And since only less than
12 2 percent of the returns are audited, there would be some
13 temptation for people just to put on \$50.00 or \$100.00 and
14 take the deduction.

15 Senator Packwood. That is no different, Jim, from
anybody else who wants to run the risk.

17 Senator Moynihan. It is different in that an itemized
18 return has to identify.

19 Mr. Wetzler. Senator Mitchell, you don't list your
20 individual contributions on your return unless, I believe,
21 they are cash contributions of above a certain amount.

22 If you get audited, you have to be able to document
23 that you made them in order to substantiate your deductions,
24 but you don't have to actually list them on the return when
25 you file the return.

1 Senator Moynihan. These are small amounts, and they
2 are used by, you know-- They represent the sort of typical,
3 average contribution, where it is 25 percent of \$200.00 --

4 Mr. DeArment. It is 25 percent of \$300.00.

5 Senator Moynihan. Then it goes up to 50 percent. This
6 is what people actually do give.

7 Senator Mitchell. We hope.

8 Senator Moynihan. Well, I think the records are
9 pretty clear that that is what they do give.

10 Senator Mitchell. I am talking about that you hope that
11 the actual charitable contribution comes somewhere close
12 to the amount that is deducted.

13 The Chairman. At the cost to the Government and the
14 Treasury, yes.

15 Senator Chafee. Mr. Chairman, I think we ought to point
16 out that what Senator Packwood is proposing here isn't that
17 we-- He is proposing that we do nothing and thus let the
18 present law go into effect.

19 The Chairman. Right.

20 Senator Chafee. Now, if staff would be kind enough to
21 indicate what happens under present law. It is \$25.00 now,
22 25 percent -- trace the way it goes up.

23 Mr. Wetzler. Senator, last year it was 25 percent of
24 the first \$100.00 of contributions, so it was a maximum
25 deduction of \$25.00. This year it is 25 percent of the

1 first \$300.00 of contributions, so it is a maximum deduction
2 of \$75.00. Next year it will go up to 50 percent of all
3 of your contributions, and then in 1986 it will be 100 percent
4 of all of your contributions, and then the provision sunsets
5 at the end of 1986.

6 And we have listed here two proposals -- one of which
7 is to freeze it at its 1983 level -- which is 25 percent
8 of the first \$100.00 -- and the second of which -- which is
9 down in the second group -- is to freeze it at its 1984
10 level, which is 25 percent of the first \$300.00.

11 And as you can see, there is not that much of a revenue
12 difference in those two proposals.

13 Senator Chafee. And, if I might continue. I think it
14 is important to point out what I think we all know that these
15 are people who are taking the standard deduction which is
16 assumed to take care of some charitable contributions.

17 And what is being proposed now is to give up some
18 potential revenue. In other words, we are nicking away at
19 one more effort to save some money here. Well, that is what
20 it is.

21 Senator Packwood. What we are trying to do is just
22 what Steve Symms and Bill Armstrong argued against a moment
23 ago. We just passed this law a few years ago to encourage
24 small contributions to charities. I say again this is not
25 the appreciated painting that is given to the art museum.

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1 And it is working well. And every charity in this country
2 that depends upon small contributions and more and more and
3 more of them do have found this to work, have found that it
4 increases their contributions at a time when we are cutting
5 funds for programs that the Government used to finance that
6 the kinds of charities that we are supporting are going to
7 be picking up.

8 Senator Moynihan. If I could say --

9 Senator Danforth. Mr. Chairman, basically, the theory
10 of this extra deduction is to get people two deductions.
11 And obviously, if you give people two deductions for doing
12 something, the old standard deduction -- the zero bracket --
13 and an extra deduction on top of it, obviously, it is going
14 to encourage people to do something.

15 I know it is intended to do that, but the fact of the
16 matter is that we are talking about a \$4 billion item on
17 the list here, and while I am sure that it would be
18 beneficial to charities to provide an effective double
19 deduction for them, somebody has got to chip in for the
20 public good here.

21 The Chairman. This was not part of the President's
22 tax package in 1981. It was a floor amendment that was
23 adopted, and again, I don't quarrel with it, but we don't
24 want to --

25 Senator Chafee. Mr. Chairman. we are not eliminating

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1 it -- we are keeping it where it is now, which is what?
2 If Mr. Packwood's motion fails and then we proceed to adopt
3 this, the taxpayer would still get the \$75.00, wouldn't he?

4 The Chairman. It would still be open to negotiation.

5 Senator Packwood. All I am asking is this. Large
6 contributors get 100 percent deduction now, if they itemize.
7 The people who make major donations to major charities itemize
8 and they get it. And all we are trying to do is give people
9 who give \$50.00, \$60.00, \$100.00 a year the same break.

10 And I would like to have a vote on continuing the law
11 as it is.

12 Senator Moynihan. Mr. Chairman, could I just make the
13 point that this was done as a floor amendment, but it just
14 didn't come out of sudden enthusiasm. We have held
15 extensive hearings on this and had the most solid evidence
16 of the drop-off in contributions that has been associated
17 with the rise of the zero bracket.

18 I mean, a case was made and a good one. And we are
19 talking about the Girls Scouts, and we are talking about
20 the local rest homes and the Baptist Church, and this is
21 not --

22 The Chairman. They are all in there.

23 Senator Moynihan. Yes.

24 The Chairman. Again, it is just a question of whether
25 we are going to do anything. If we don't want to do

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1 anything, we won't do anything. There aren't any easy
2 choices. What we are suggesting is not that we end it, but
3 that we restructure it.

4 And it is my understanding that Treasury is supposed to
5 come up with some little broader compromise that might extend
6 it beyond 1986 but still result in some savings which might
7 be attractive to Senator Moynihan and Senator Packwood.
8 They haven't done that.

9 Senator Packwood. Can we have a vote on not ending it?

10 Senator Mitchell. May I make one further comment.

11 Mr. Chairman, I am sympathetic to the point of view expressed
12 by Senators Packwood and Moynihan. The aspect of it that
13 troubles me is the potential for simply dramatically
14 increasing the number of tax returns that will have
15 deductions -- that will take deductions for contributions
16 not actually made.

17 Now, you say that it is the same as the existing law,
18 but it seems to me that there are two essential differences.
19 The first is the total number of returns identifying
20 deductions will be dramatically increased, and since the
21 dollar amount will be significantly less, what is the
22 likelihood that the IRS is going to audit a return over a
23 \$25.00 or a \$50.00 deduction? And that is the only aspect
24 of it that concerns me.

25 If there is any indication that this is going to

1 accomplish the purpose -- which I think we all agree is a
2 very noble purpose -- everybody here would encourage people
3 to give to charities -- without at the same time producing
4 this unfortunate byproduct -- I would support you.

5 Senator Packwood. The independent sector -- which is
6 the lobbying group for this -- and consists of all of the
7 charities involved -- has asked the Internal Service for
8 enforced compliance on this, and the Internal Revenue Service
9 does not want to do it because they have never liked this
10 provision.

11 Senator Mitchell. They asked for what?

12 Senator Packwood. For increased compliance so that
13 there is no allegation of cheating on this. The charities
14 are using this incentive to increase their contributions.
15 They are going out and selling it and it is working. And
16 there has been -- so far -- no allegation in the hearings
17 we have had of abuse in it, but to make sure that there
18 were no allegations, the independent sector -- the lobbying
19 group that is the overview for the charities -- asked for
20 increased auditing of these kinds of returns. The Internal
21 Revenue Service doesn't want to do it.

22 The Chairman. I think what Bob wants is just to get a
23 vote on the present law. And again, if we are looking at
24 the Girl Scouts, we had better worry about what the deficit
25 is going to be when they get to --

1 Senator Matsunaga. Mr. Chairman, one further point in
2 consideration in support of the -- Bob's --

3 The Chairman. If you are in support of it, let's vote
4 on it.

5 Senator Matsunaga. When we proposed to reduce the
6 maximum tax on income from 90 percent to 70 percent, we
7 had a number of organizations appear before the committee,
8 as you will recall, saying that they were going to lose
9 a considerable amount of their contributions and they, in
10 fact, did lose because when we proposed to reduce it from
11 70 to 50, they came forth and testified that they lost
12 one-third of their contributions, and that if we were going
13 to reduce it from 70 to 50, they would be sure to lose
14 another third and maybe 50 percent.

15 So, in consideration of that, we came forth with this
16 proposal, and now after they have gone through all the
17 testifying -- we have had hearings -- and I am a member of
18 the subcommittee. Then -- what is it, just a couple of
19 years now? -- and we want to change it again.

20 The Chairman. Well, we have got these big deficits.

21 Senator Matsunaga. That may be so. We can change the
22 laws in other areas.

23 The Chairman. Have you got a substitute? I will take
24 a substitute for it.

25 Senator Matsunaga. Well, we postponed the indexing of

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1 income.

2 Senator Packwood. Can we have a vote, Mr. Chairman?

3 The Chairman. Yes.

4 Senator Mitchell. Can I just ask -- did you say, Mr.
5 Chairman, that you are going to propose capping it at the
6 1984 level and extending it for a further period of time?

7 The Chairman. Extending it through 1987. Yes.

8 Senator Mitchell. So, what we are merely saying here
9 is to continue the present law and not freeze it. And that
10 is not acceptable.

11 The Chairman. Let's have the vote.

12 Mr. DeArment. Mr. Packwood?

13 Senator Packwood. Aye.

14 Mr. DeArment. Mr. Roth?

15 (No response)

16 Mr. DeArment. Mr. Danforth?

17 Senator Danforth. No.

18 Mr. DeArment. Mr. Chafee.

19 Senator Chafee. No.

20 Mr. DeArment. Mr. Heinz?

21 (No response)

22 Mr. DeArment. Mr. Wallop?

23 Senator Wallop. No.

24 Mr. DeArment. Mr. Durenberger?

25 Senator Durenberger. Aye.

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1 Mr. DeArment. Mr. Armstrong?
2 Senator Armstrong. Aye.
3 Mr. DeArment. Mr. Symms?
4 Senator Symms. Aye.
5 Mr. DeArment. Mr. Grassley?
6 Senator Grassley. Aye.
7 Mr. DeArment. Mr. Long?
8 Senator Moynihan. I have an aye proxy for Mr. Long.
9 Mr. DeArment. Mr. Bentsen?
10 (No response)
11 Mr. DeArment. Mr. Matsunaga?
12 Senator Matsunaga. Aye.
13 Mr. DeArment. Mr. Moynihan?
14 Senator Moynihan. Aye.
15 Mr. DeArment. Mr. Baucus?
16 (No response)
17 Mr. DeArment. Mr. Boren?
18 Senator Boren. Aye.
19 Mr. DeArment. Mr. Bradley.
20 Senator Bradley. Aye.
21 Mr. DeArment. Mr. Mitchell?
22 Senator Mitchell. Aye.
23 Mr. DeArment. Mr. Pryor?
24 Senator Pryor. Aye.
25 Mr. DeArment. Mr. Chairman?

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1 The Chairman. No.

2 The yeas were 12, and the nays were 4, so the present
3 law remains. We will not bring this up again.

4 That does narrow the options. Does anybody else have
5 any easy ones on here? What about -- let's go to capping
6 consumer interest. That is \$2,000.00 and \$4,000.00.

7 Mr. Wetzler. Senator Dole, we have got a handout
8 describing a proposal on consumer interest, which we can
9 distribute.

10 What this proposal does is it says that your interest
11 deduction will be limited to your investment income plus
12 \$2,000.00 for single people and \$4,000.00 for married couples.
13 So, in effect, it defines consumer interest as saying that
14 your nonconsumer interest -- the stuff that is not going
15 to be capped -- is measured by the amount of your investment
16 income. So, if you have borrowed money in order to invest
17 in something -- at least to the extent that you have
18 investment income -- your interest deductions will be allowed
19 in full, and in addition, it will give you an extra \$2,000.00
20 for single people, \$4,000.00 for married couples.

21 Senator Chafee. That is not solely interest income,
22 is it? Is it solely interest income. Dividend income --

23 Mr. Wetzler. Of course, this would exclude mortgage
24 income. It would not be considered. This wouldn't apply
25 at all to mortgage interest. It wouldn't apply to business

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1 interest, which is interest you incur in connection with
2 investing in a business.

3 Senator Mitchell. It wouldn't apply to interest that
4 you used in a tax shelter?

5 In other words, you could offset interests against
6 investment income plus additional income?

7 Mr. Wetzler. As you see in the explanation, there is
8 a rule that says holding as a limited partner not actively
9 participating in the management of Subchapter S corporations
10 and rental activities in which the taxpayer does not
11 materially participate would be treated as investments.

12 So, they would be limited to your investment income and,
13 of course, if it is a tax shelter, it is likely to be
14 throwing off losses rather than income, so that means you
15 would be losing those interest deductions.

16 The Chairman. Does Treasury have anything on this?

17 Mr. Pearlman. Mr. Chairman, this morning is the first
18 time we were aware that this was coming up. I would really
19 hope that we have an opportunity to express our views.

20 The Chairman. All right. We will give you until this
21 afternoon to do that. At least, we have raised it. We want
22 to raise these that we have added on the theory that we
23 would lose some of the others.

24 Maybe we just ought to go back to items left open by
25 the committee.

1 Senator Durenberger. Mr. Chairman, I wonder if before
2 we leave this one, if Treasury could also look at a couple
3 of alternatives. One would be cap each taxpayer's nonbusiness
4 noninvestment interest at 97 percent of interest paid across
5 the board. In other words, you lose 3 percent. See what
6 impact that has and what kind of dollars it raises.

7 Mr. Pearlman. Senator, describe the interest you want
8 to cover again.

9 Senator Durenberger. It is the nonbusiness noninvestment
10 capped at 97 percent.

11 Mr. Wetzler. Senator, would you want this applied to
12 mortgage interest as well?

13 Senator Durenberger. Right. All of it.

14 I am also interested in the figures if we drop the
15 2 and 4 to 1 and 2 -- what kind of revenue that raises.

16 Mr. Wetzler. All right.

17 Senator Bradley. Mr. Chairman.

18 The Chairman. Mr. Bradley.

19 Senator Bradley. Yesterday, did you ask the staff to
20 prepare us a list of the things that we had discussed?

21 The Chairman. Yes. That we had discussed?

22 Senator Bradley. Yes.

23 The Chairman. I think that is available.

24 Senator Bradley. I am sorry. I didn't get a copy of it.

25 The Chairman. We will get you a copy of that, plus we

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1 have the request that Senator Baucus made. Have those been
2 made available -- you know, where cuts have been made on
3 the committee in different programs.

4 Mr. DeArment. We do have those. I don't know whether
5 we have the copies right there. We had them yesterday.
6 We will dig them up.

7 The Chairman. All right. Let's discuss item number
8 four on possible additional proposals to modify Section
9 1231. What does that do? Jim, do you want to explain --

10 Mr. Wetzler. Let Don describe it since I think it is
11 more --

12 The Chairman. All right.

Mr. Susswein. This proposal deals with Section 1231 of
14 the Code. Section 1231 deals with gains and losses on sales
15 of assets used in a trade or business. Generally, that
16 provision provides extremely favorable treatment for
17 business assets. Essentially, you look at the gains and
18 losses in any taxable year, and if the result of the netting
19 out all of those transactions is a loss, the loss is treated
20 as an ordinary loss.

21 On the other hand, if the result of netting out all
22 those transactions is a gain, the transaction is treated as
23 a capital gain. Essentially this reflects the policy
24 judgments that the Congress has made regarding the favorable
25 treatment that should be afforded sales of assets used in

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1 a trade or business. However, potential abuse exists when
2 taxpayers can manipulate the time at which they sell assets
3 at a gain or at a loss over a multiple-year period.

4 In other words, for example, they could have an
5 alternate of gains and losses so that even though over a
6 three- or four-year period, their gains and losses equal
7 each other, in fact they would manipulate the transactions
8 so that they would result in a net tax shelter.

9 What this proposal would do is it would take the 1231
10 computation, and you would look three years back and three
11 years forward so that the netting would simply be done over
12 a longer period of time. So, if you had an ordinary loss
13 in a taxable year and you had in the year before used the
14 same netting rules and resulted in a capital gain, the
15 ordinary loss would be carried back and offset against the
16 capital gain.

17 Similarly, if you had a capital gain followed by an
18 ordinary loss -- I am sorry an ordinary loss followed by
19 a capital gain -- the capital gain could be recharacterized
20 as an ordinary loss--as an ordinary gain.

21 Mr. Pearlman. We have done an analysis of this, and
22 I think we are again. If you can just give me until this
23 afternoon, I can come back and --

24 The Chairman. As I understand this, Treasury supports
25 this. What about Joint Committee? Have you looked at it in

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1 the Joint Committee?

2 Mr. Wetzler. Yes. I think it addresses the problem of
3 the present law where people, you know -- you have this
4 situation where with these particular types of assets, your
5 losses are ordinary losses. Your gain are long-term capital
6 gains, and people recognize the gains and losses in alternate
7 years in order to basically whipsaw us, and I think this
8 would address that problem.

9 Senator Moynihan. It is a straddle effect.

10 Mr. Wetzler. Well, these aren't really straddles. I
11 think these are ordinary businesses doing this, but they
12 have discretion about when to recognize their gains and
13 losses, and they obviously do it, in some cases, to better
14 their tax situation.

15 The Chairman. I think Senator Bentsen has a question
16 on this, so why don't we give Treasury time to bring it up
17 at 2:30. And Senator Baucus has a question on number six,
18 so I suggest we not take that up.

19 Senator Moynihan. Did you say you have a "slop"
20 proposal?

21 Senator Moynihan. Yes. We mentioned yesterday, Mr.
22 Chairman, and I believe the committee staff has a piece of
23 paper on it, do they not?

24 Senator Symms. Mr. Chairman, before we start on another
25 one, I would like to ask one question on this other one. I

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1 didn't realize that we were going on.

2 What do you do about the amount of money on this
3 proposition that somebody can charge off against ordinary
4 income if they have had only losses?

5 Mr. Wetzler. On Section 1231?

6 Senator Symms. Yes.

7 Mr. Wetzler. I don't think there would be any-- Today
8 there is no limit, and I don't believe there would be any
9 limit --

10 Senator Symms. Yes. There is a limit of \$3,000.00.

11 Mr. Wetzler. Oh, no, that is on-- Today, capital
12 losses are limited to \$3,000.00 of ordinary income, and last
13 fall in the reconciliation bill, it was a kind of a trade-off
14 with the six-month holding period on capital gains that
15 the committee reported out -- a proposal to reduce that
16 \$3,000.00 back to \$1,000.00, which is where it was prior
17 to 1976.

18 That was something that the committee did -- Under
19 Section 1231; the losses are ordinary losses so they are
20 not subject to the limitation, and the gains are capital
21 gains, and so the \$3,000.00 limit doesn't apply to this.

22 Senator Symms. It seems to me that that is extremely
23 unfair to the taxpayer.

24 Mr. Wetzler. No, sir, it is a good deal for the
25 taxpayer because his losses are fully deductible, and only

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1 40 percent of his gains are taxed.

2 Senator Symms. If he lives long enough. If you cut it
3 back to \$1,000.00 a year.

4 Mr. Wetzler. Let me try again.

5 Senator Symms. Let's take a taxpayer who has bought
6 some stock or some capital asset and sold it and suffered
7 a real loss.

8 Mr. Wetzler. The tax law makes a distinction today
9 between capital losses and ordinary losses. Ordinary losses
10 are ones you undergo in your business. Capital losses are
11 investments. There is a lot of law involving just exactly
12 what that distinction is.

13 The present law limits the deduction of capital losses
14 to capital gains and then only up to \$3,000.00 of ordinary
15 income for individuals. For corporations, capital losses
16 can't be deducted against ordinary income at all.

17 Ordinary losses, however, are fully deductible against
18 ordinary incomes. The taxpayer would rather have ordinary
19 losses than capital losses. In terms of just the treatment
20 of capital losses, last fall the committee agreed on the
21 proposal to reduce that \$3,000.00 to \$1,000.00 in order to
22 raise revenue to pay for the six-month holding period.

23 Under Section 1231, assets used in a trade or business
24 are given an especially good deal. The taxpayer nets out
25 his 1231 gains and losses. If he has got a net gain, the

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1 gain is treated as a capital gain -- which means in the
2 case of long-term gains -- only 40 percent of the gain is
3 included in income -- or for corporations, the capital gains
4 are taxed at a 28 percent rate. If these 1231 assets net
5 out to be losses, then those are ordinary losses which are
fully deductible against ordinary income.

7 And what this proposal in front of you here does is
8 tries to address that question dealing with the case where
9 taxpayers with respect to their 1231 assets -- either assets
10 used in trades or businesses -- where they in effect
11 recognize their gains in one year, paying tax on only 40
12 percent of the gains, and then their losses in the next
13 year, fully deducting the losses.

14 So, they are really two related questions, one of which
15 you dealt with last year and the other of which is being
16 looked at in this proposal.

17 Senator Symms. I will talk to you more about that,
18 and you can go back through it. We may be talking about
19 two different things, but it is my understanding that if the
20 taxpayer has a loss, then he can only take \$3,000.00 a year
21 off of his ordinary income.

22 Mr. Wetzler. If it is a capital loss. If it is an
23 ordinary loss, for example the sale of an asset used in
24 your trade or business, then he can deduct it in full against
25 his ordinary income.

1 Senator Symms. Well, that is the point that I was
2 talking about. You are not addressing that at all in this
3 question then?

4 Mr. Wetzler. This proposal doesn't address capital
5 losses at all. This addresses the ordinary losses that are
6 generated from sales of assets used in trade or business.

7 Senator Symms. Okay. Well, that other law hasn't
8 passed the Senate yet, though, has it?

9 Mr. Wetzler. No, and some concern has been expressed
10 about what the committee did last fall.

11 (Pause)

12 Senator Moynihan. Mr. Chairman, the elemental proposal
13 is that it deals with a practice that has been growing owing
14 to the depreciation schedules that we adopted in ERDA in
15 which individuals will buy a property -- let us say a yacht
16 or a condominium -- and rent it to another individual who
17 has done the same and rents it back to them. How extensive
18 a practice this is we don't know. We do know it does take
19 place, and we do know it does cost revenue, and I don't
20 know how much we would gain from this, but again, it is a
21 question of how much we will prevent ourselves from losing
22 if the practice should spread.

23 There is some question about whether the present law
24 does prohibit such transactions. I think probably it does,
25 but this makes it explicit, and it makes persons who behave

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1 in this way eligible to be liable for negligence and even
2 fraud.

3 The Chairman. Right. I defer to Treasury.

4 Mr. Pearlman. Mr. Chairman, we did take a look at
5 this one yesterday. We do think, Senator Moynihan, that
6 current law will permit us to deal with this transaction.
7 I don't think we would oppose trying to do something
8 legislatively. It is a matter of designing it, and I am
9 not sure we are ready to get there.

10 If the committee chooses to go forward with the
11 understanding that we need to make sure it works, this is
12 a transaction that we are concerned about, but we don't
13 want to leave any misimpression that we don't think we
14 have authority under current law to deal with it.

15 I think, for example, we have published a ruling
16 already which involves swapping of rental houses, and I
17 think it would be rather easy to deal with this by ruling.

18 Senator Moynihan. Mr. Pearlman, I would make the point
19 -- and I think Mr. Hardee could speak to it -- that this
20 particular subject -- it needs to be known that it is against
21 the law.

22 Mr. Pearlman. Yes. I don't have any problem with that.

23 The Chairman. If there isn't any objection, why don't
24 we see if we can draft something if Treasury supports it.

25 As I understand, Mr. Hardee is going to --

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1 Mr. Hardee. Yes, just to put it in the Internal
2 Revenue Code so you can explicitly tell people that they
3 can't do it. I am not saying that the IRS has the opinion
4 that you can't do it, but Congress has the opinion that
5 you can't do it.

6 The Chairman. Okay. Let me suggest that it is now
7 12:30. The options -- and I would hope that members who
8 disagree with some of these, and I don't suggest these are
9 the last word obviously -- but if we are getting down now
10 to very few options, and we still need some additional
11 revenue, we will come back at 2:30.

12 If the Treasury can be of any assistance in trying to
13 dig up some more, that would be helpful. But I think what
14 we will do at 2:30 -- as soon as we have a quorum -- is
15 start down the list and see where we end up. And if we
16 vote them all down, then we will have to caucus and figure
17 out some way to recoup enough to fulfill our obligation to
18 this so-called package arrangement, which I think the
19 President will support.

20 So, does anybody else have any other ideas that we
21 can discuss at 2:30.

22 Senator Bradley. There will be an opportunity to
23 offer suggestions that are not on this list.

24 The Chairman. Oh, obviously. Right.

25 In fact, if you would like to -- maybe you may not want

1 to list them -- but you have your olympic checkoff -- is
2 that --

3 Senator Bradley. I wasn't referring to that, but, yes,
4 I do have it.

5 The Chairman. Now, can Treasury -- will that give you
6 enough time to get most of the information?

7 Mr. Pearlman. We will do our best. A couple of hours.
8 We should be able to get most of it. We will do the best
9 we can.

10 The Chairman. If anybody has any ideas on more
11 savings, we would appreciate those, too.

12 (Whereupon, at 12:32 p.m., the hearing was recessed.)
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AFTERNOON SESSION

(2:58 p.m.)

1
2
3 The Chairman. As I understand, we have discussed
4 a technical area that we approved this morning, but we wanted
5 to get back to make certain there was protective language,
6 and that is on the Income Verification, No. 3 on the
7 so-called CBO Estimates of the Grace Commission package.

8 Rod, did you tell me during the noon hour that we now
9 have adequate safeguards?

10 Mr. Pearlman. I think we do, Mr. Chairman.

11 Mr. DeArment. Yes, Mr. Chairman. We have reviewed the
12 safeguards that are in the current Code with respect to
13 earned income data that the various welfare agencies that
14 administer this now have, and we would propose that the
same Code restrictions that have worked well in the earned
income area be added in the unearned income area.

17 The Chairman. I think we need to be sure you go over
18 that with Senator Moynihan or his staff. He raised that
19 question, though I know of no objection, and we will approve
20 it on that basis. But if there is some question by
21 Senator Moynihan, obviously -- but Treasury is satisfied
22 that the safeguards that he indicated are there?

23 Mr. Pearlman. Yes, we are satisfied.

24 The Chairman. Because he had the same concern that the
25 rest of us have and that the Treasury has.

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1 The Chairman. Well, what about the minimum tax? What
2 happened to that during the noon hour?

3 Mr. DeArment. We have spent several hours working on
4 the proposal.

5 The Chairman. Jim?

6 Mr. Wetzler. We have a handout that will try to respond
7 to Senator Bentsen's concern.

8 The Chairman. Well, it was a real concern.

Mr. Wetzler. Basically we are saying the proposal
9 applies to the extent you are deducting losses in
10 excess of your cash investment, including recourse debt.
11 So it would not apply when you are really losing the cash,
12 or when you are really liable for the monies.
13

14 Senator Bentsen. Well, that certainly helps.

15 Mr. Wetzler. We don't yet have a revenue estimate on
16 this. This will have a substantial diminution of the
17 revenues from it, but I think it would safeguard the problem
18 you were concerned about, which is people not being able to
19 deduct their real losses.

20 Senator Bentsen. Their real losses, yes.

21 The Chairman. Treasury, I know you are not in a position
22 to support it, but have you had an opportunity to look over
23 the Joint Committee's suggestions?

24 Mr. Wetzler. Yes, Mr. Chairman. We have looked over
25 the suggestions, and we think from a technical standpoint that

1 the suggestion can be implemented. As you indicated, we are
2 not in a position where we can indicate our support.

3 Senator Bentsen. Your voice dwindles off when you tell
4 me what you are going to do.

5 The Chairman. They can't support it.

6 Senator Bentsen. Cannot?

7 Mr. Pearlman. We cannot support it at this time, but
8 we have reviewed it from the standpoint of whether this
9 approach is workable, whether if the committee chooses to
10 proceed with it, whether it is workable. And we do think
11 it can be put in statutory language that will make the
12 proposal workable.

13 The Chairman. As I understand, neither are you
14 opposing the amendment.

15 Mr. Pearlman. No. I didn't mean to suggest opposition,
16 no.

17 The Chairman. But I think the important point on this
18 issue is whether or not it did satisfy the questions raised
19 by a number of Senators, particularly Senator Bentsen.

20 Do you have any idea of what the revenue estimates would
21 be at this time?

22 Mr. Wetzler. No, we are still running it. Let me just
23 qualify that. This would also income earned abroad; that
24 exclusion is a preference, as per Senator Moynihan's
25 proposal yesterday. But we are still trying to run the

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1 revenues.

2 The Chairman. Senator Long, we are looking at the
3 minimum tax, No. 2 there. Senator Bentsen raised some very
4 legitimate questions, and the Joint Committee has tried to
5 address those questions, and now they are redoing the
6 revenue estimates.

7 Senator Long. What kind of an estimate do you have so
8 far? How much would you raise with it?

9 Mr. Wetzler. Well, the estimators are still running
10 that. I would prefer not to take a completely wild guess.

11 The Chairman. Well, under the original proposal it
12 would have raised about \$2 billion over three years. This
13 would probably be substantially less.

14 Mr. Wetzler. Well, I would like to reserve until the
15 estimators tell me what the answer is.

16 The Chairman. What about prepayments? Have we been
17 able to satisfy the concerns that I have expressed, and
18 Senator Boren, Senator Bentsen, and Senator Long, in that
19 area?

20 Mr. Pearlman. No, I don't think so. I would say this,
21 Mr. Chairman and Senator Boren, that if the committee chooses
22 to act on the prepayment rule, we think that the suggestions
23 that Senator Long and Senator Boren have made help; but we
24 are concerned about a prepayment rule that has a six-month
25 window in it, because we think that is going to let a lot

1 of stuff out. I think our concern will remain.

2 Senator Boren. Mr. Chairman, maybe if we just dropped
3 any reference to time, that from my understanding went with
4 that one-to-one clause, and then use the codification,
5 what has continued to be the codification of the case law
6 on it having a legitimate business purpose, and actual
7 out-of-pocket expense.

8 Mr. Pearlman. Then, in addition to that, can we put a
9 borrowing limit on it?

10 Senator Boren. Yes.

11 Mr. Pearlman. All right. Well, I think that certainly
12 is very helpful.

13 The Chairman. I think the borrowing limit would be
14 of some benefit.

15 Mr. Pearlman. That is correct. Yes. Well, our
16 principal concern is making sure that it's not more generous
17 than current law.

18 Senator Boren. Yes.

19 Mr. Pearlman. And if you will permit us to try to take
20 what you have just said and put it in statutory language.

21 Senator Boren. All right.

22 Mr. Pearlman. We don't it's more liberal than current
23 law. I think that is certainly an improvement.

24 Senator Boren. The borrowing limit would not apply to
25 the person in the business?

1 Mr. Pearlman. No. This prepayment rule would not apply
2 to people in the business, at all.

3 Senator Boren. Right.

4 The Chairman. Again, that would probably -- you would
5 have to substantially revise your revenue figures; is that
6 correct?

7 Senator Boren. We would probably still have some
8 modest savings attached to it, I would think.

9 Mr. Pearlman. Yes, I think so.

10 I don't have a revenue number on the revision.

11 The Chairman. And what did we determine on item No. 2,
12 Distribution of Appreciation Property? I know Senator Heinz
13 and Senator Bentsen and others have an interest in that.
14 Has that been resolved?

15 Mr. Pearlman. No, it hasn't. Unfortunately, we did
16 not have an opportunity to discuss that one at lunch. I
17 tried to do that with Senator Bentsen's staff and simply was
18 not able to. I would like to have the opportunity to do
19 that.

20 The Chairman. All right.

21 Senator Bentsen. There may be some things we can do
22 on that to possibly get at the serious concerns of Treasury
23 in that regard.

24 Mr. Pearlman. Yes.

25 Senator Bentsen. As far as inventories, and that type

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1 of thing.

2 Mr. Pearlman. We appreciate that. Thank you.

3 The Chairman. What has happened on the so-called
4 "luxury" automobile depreciation?

5 Mr. Pearlman. Are you asking me?

6 (Laughter)

7 The Chairman. Anyone who might know.

8 Senator Baucus. Well, Mr. Chairman, as we left it,
as I recall anyway, the staff was going to see if they
10 could draft some rules of some kind to address some of the
11 other issues in addition to cars -- planes, and so forth.
12 If that is feasible.

13 Senator Chafee. For personal use?

14 Mr. Pearlman. Right.

15 Senator, we tried last night. I had expressed the
16 concern about personal use before, and I can go into that
in a bit more detail in a moment.

17 We tried last night to define a rule to focus on the
18 lavish expenditure in a way that would be applicable on a
19 more evenhanded basis to assets, other than simply
20 automobiles. And I must tell you that we were unsuccessful.
21 I mean, we can enumerate assets and then put prices next to
22 them, but we were not able to come up with something that
23 simply is not going to invite continuous controversy between
24 revenue agents and taxpayers as to what is lavish and what
25

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1 is not, and our view is that that is not desirable, that that
2 is going to add subjectivity to the audit process and won't
3 be well received either by taxpayers or by revenue agents
4 to fight about whether a desk chair is lavish or whether
5 draperies and so forth are lavish.

6 We continue to be concerned about the problem of
7 personal use, particularly in connection with cars and other
8 items of personal property that are of the nature that would
9 be used personally by an individual. And we believe that if
10 we can get to the personal-use issue in a way where
11 taxpayers have to be a bit more sensitive in claiming
12 depreciation and other expenses in connection with these
13 types of property on their tax returns, that that will have
14 an effect -- not a perfect effect, admittedly, but an effect
15 -- on taxpayers' willingness to expend money on lavish
16 assets; that is, a business is going to be less willing to
17 buy the \$50,000 car if the person using that car uses it
18 most of the time for personal use and there is not going to
19 be any depreciation allowed.

20 So, while we know that a further effort to restrict
21 personal use is not a perfect answer to the concern you are
22 expressing, we think that is a more pervasive problem. And
23 personally, we would rather deal with the personal use
24 problem.

25 Our approach would be to set up an arbitrary, but

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1 rebuttable, rule that in connection with the types of
2 personal property that are used typically both for personal
3 and use, and a car, or a yacht, or an airplane all might fit
4 that category, that we would require a threshold percentage
5 of business use.

6 Now, we have been talking in terms of 50 percent. There
7 is nothing magical about that percentage, but we would say
8 that if that asset wasn't used at least 50 percent of the
9 time for business use, then ACRS would not be available for
10 that asset, and that some more restrictive depreciation
11 would be available to the extent of the actual business
12 use. Let's assume it's 20 percent business use. In a
13 car, one of the things we might do is use the standard
14 mileage rate; so, to the extent that a taxpayer who doesn't
15 use an automobile at least 50 percent of the time for
16 business use would only be able to get the standard mileage
17 rate -- now, I think 21 cents a mile -- for the actual
18 business use.

19 If a taxpayer is able to demonstrate business use in
20 excess of 50 percent, then ACRS would be available, but only
21 to the extent of the actual use. So, if the use is 80
22 percent, then ACRS would be available only to the extent of
23 80 percent and not to the extent of 100 percent.

24 We believe that that type of rule is going to put a lot
25 more pressure on assets that are susceptible to personal

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1 use provided by employers. And we think that, while it cuts
2 across a variety of asset lines, that it will not disturb
3 legitimate business use of assets.

4 There is another part to our suggestion that we think
5 will also be helpful, and that is the problem of conversion
6 of a business asset to a personal asset. Assume a business
7 purchases a car for an employee and keeps it for three
8 years until it is fully depreciated, and then says to the
9 employee, "Look, I'll sell it to you for a fairly nominal
10 basis, or we will just let you use it full time for personal
11 use thereafter." We would suggest a rule that, if an asset
12 is converted into personal use or dips below the 50 percent,
13 either way, fully personal use or below the 50 percent
14 threshold, that there would be a recapture of that
15 depreciation, so that employers couldn't get the benefit
16 of depreciation deductions by indeed using a car fully
17 within a business for a few years and then saying to an
18 employee, "Now, you go ahead. You know, we'll keep ownership
19 of the car, but you go ahead and use it for personal use from
20 now on, because it is fully depreciated."

21 We think if we can get to those two problems, it doesn't
22 solve fully the lavish and extravagant concern that is
23 articulated in your proposal, but it will go a long way to
24 businesses expending lavish sums for personal property.

25 Senator Baucus. Mr. Chairman?

1 The Chairman. Senator Baucus?

2 Senator Baucus. Frankly, I think the Commissioner has
3 a good point, because obviously the bigger problem is the
4 degree to which someone uses a luxury asset for personal
5 use and claims that he or she is using it for a business
6 purpose.

7 There is, however, a second problem, at least in this
8 Senator's mind, and that is, what happens when a taxpayer
9 legitimately does use a luxurious asset for a business
10 purpose but still gets full benefit of ACRS and tax credits
11 and so forth, and really the business purpose could be fully
12 served with a less luxurious asset; i.e., not a luxury
13 automobile? That is a separate question, and it's a separate
14 problem.

15 It just seems to me that we can address both problems
16 by, number one, adopting something similar to the bill that
17 Senator Moynihan and I have introduced, and at the same time
18 either ask the Service to do kind of a study, if we need more
19 time on it -- I guess that's the first that comes to mind --
20 or else also adopt some of the measures that the Commissioner
21 has outlined.

22 But there are two separate problems, and I do think the
23 Commissioner has made a very good point, that we have to
24 perhaps tighten up a little bit the availability of
25 luxurious assets for personal uses when they should be for

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1 business uses. I don't know, I tend to think we can address
2 both, and address one albeit if it is a less significant
3 problem, by adopting this bill, and also going through with
4 the study.

5 The Chairman. As I understand the way the bill is
6 drafted, it covers utility multi-purpose vehicles widely
7 used on farms, ranches, and in businesses, light trucks,
8 mini-vans, four-wheel drive vehicles like Chevy Blazers and
9 Ford Broncos. Does it exclude multi-purpose and similar
10 vehicles?

11 Senator Baucus. Mr. Chairman, yes. That's the full
12 intention, exclude the whole list of vehicles that you just
13 listed.

14 My understanding is that it can be drafted in such a
15 way as to accomplish that purpose.

16 The Chairman. I also understand that the average
17 retail price of cars is up to about \$10,500 in 1983; with
18 taxes, delivery charges and a few options, \$15,000 quickly
19 begins to get smaller cars than Cadillacs -- Buick station
20 wagons, for example.

21 Is there any magic in the \$15,000? Can he index it to
22 something?

23 Mr. Wetzler. It is indexed in Senator Baucus's bill.

24 Senator Baucus. Yes. First of all, it is indexed;
25 and second, there is no magic in 15. It could be 17.5 or

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1 something. We will have to draw a line somewhere, and
2 15 indexed seems to me to be an appropriate place to draw
3 the line.

4 Mr. Wetzler. I think, Mr. Chairman, the concern about
5 raising the level much above 15 is that, if you get to the
6 point where you are only affecting foreign cars, then you
7 might have trouble under GATT. I guess Rod can address
8 that, but I think that was one of the concerns at setting
9 the level at \$15,000.

10 The Chairman. Is Treasury just talking about a study?
11 Is that it?

12 Mr. Pearlman. We are prepared to either put the personal
13 use provision before you, or we will do a study -- whatever
14 the committee wishes.

15 Senator Baucus. But, Mr. Chairman, as I understand it
16 we are still talking about two separate questions here:
17 One is the personal use matter, and the other is the
18 availability of ACRS for luxurious assets even though it is
19 for business use.

20 Mr. Pearlman. Let me mention one thing, Mr. Chairman.
21 I am told that the Moynihan-Baucus bill does not cover
22 cars leased. I am not talking now about the person who is
23 in the business of leasing, but if instead of owning the
24 car myself I go to someone and lease it, and it certainly
25 has to do that.

1 Senator Baucus. Can we take care of that?

2 Mr. Pearlman. Sure.

3 Senator Baucus. It seems to me it should cover cars
4 that are leased.

5 Mr. Pearlman. Yes. If you are going to do anything,
6 you've got to do both.

7 Senator Baucus. I agree.

8 Senator Chafee. Has anybody brought up the issue of
9 pickup trucks?

The Chairman. I did.

11 Mr. DeArment. Yes. Senator Dole did, and Senator
12 Baucus indicated it was his intention to take them out.

13 Senator Baucus. That's right. I also understand that
14 Senator Moynihan's bill does cover cars that are leased.
15 But anyway, we can take care of that.

16 Senator Danforth. Mr. Chairman?

The Chairman. Senator Danforth.

18 Senator Danforth. As I understand the proposal -- and
19 I am sorry I got in late -- the idea is to disallow
20 depreciation for corporate vehicles that are used in a private
21 way by officers or employees of a company, provided that the
22 private use is more than a certain percentage of the total
23 use. Is that it?

24 Mr. Pearlman. Well, as Senator Baucus pointed out, there
25 are two proposals, but seeing a way from the lavish proposal,

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1 our proposal would be that in the event that the business
2 use is not 50 percent or more, then ACRS would not be
3 available with respect to that property, without regard to
4 the extent of the business use.

5 So, if you had 20 or 30 percent of business use in a
6 car and 70 percent personal use, then you would use either
7 a stretched-out depreciation schedule or you would use a
8 standard mileage rate for the actual business use -- 20
9 percent, 30 percent, whatever.

10 If the business use exceeded 50 percent, then, to the
11 extent of the business use, 60 percent, 80 percent, or
12 100 percent, again on an actual documented basis, you would
13 be eligible for ACRS.

14 Senator Danforth. If the business use exceeded 50
15 percent then it would be ratable?

16 Mr. Pearlman. Yes, then we would prorate.

17 Senator Danforth. And if the business use would be
18 less than 50 percent?

19 Mr. Pearlman. Then it would likewise be ratable, but
20 you would not be able to use ACRS on the portion that is
21 business use.

22 Senator Danforth. And some vehicles are in and some
23 vehicles are out, is that correct? Do you treat different
24 vehicles differently, for example pickup trucks?

25 Mr. Pearlman. Well, our effort in this approach was

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1 to treat all vehicles that are susceptible to both business
2 and personal use the same, whether they are yachts or
3 pickup trucks or anything.

4 Now, obviously the committee can modify that.

5 Senator Danforth. Then what is the sense of
6 differentiating?

7 Mr. Pearlman. Well, in that regard, we don't think
8 there is any.

9 Senator Danforth. I mean, why should pickup trucks or
10 four-wheel drive vehicles be treated differently if it is
11 for personal use? If you have got a business executive who
12 is a weekend farmer, and you furnish him a pickup truck,
13 there is no sense in treating that differently, is there?

14 Mr. DeArment. Senator Danforth, I think the purpose
15 was for the other half of the proposal; that is, what is
16 lavish and extravagant? And sometimes a heavy duty farm
17 vehicle costs more than a street vehicle. So, when you are
18 applying a \$15,000 threshold, it is appropriate to
19 differentiate between the heavy-duty --

20 Senator Danforth. That is not for the Treasury's
21 proposal; that is for the Baucus proposal?

22 Mr. Pearlman. Right. That is for Senator Baucus's
23 proposal.

24 Senator Baucus. There are two separate questions, two
25 separate problems here.

1 Senator Danforth. Yes?

2 Senator Baucus. And as I understand it, Jack, you are
3 discussing the first problem that the Commissioner raised.

4 Senator Danforth. Right. And his proposal doesn't
5 differentiate between type of vehicle.

6 Senator Baucus. And I don't think it should.

7 Senator Danforth. Have you agreed to that?

8 Senator Baucus. Yes, I agree to that, but I also
9 think we should do something else in addition.

10 Senator Danforth. Yes.

11 Senator Baucus. Namely, disallow accelerated
12 depreciation tax credits for the use of an automobile
13 where the value of the automobile is about \$15,000, to
14 disallow the portion above the \$15,000 when the auto is used
15 in fact for a business purpose.

16 Senator Danforth. Regardless of the kind of car?

17 Senator Baucus. Well, if \$15,000 creates a problem for
18 farm vehicles and vans which are used for business purposes,
19 they are not luxurious, but they cost more than \$15,000.
20 Therefore, it seems to me it is inappropriate to disallow
21 ACRS for the value of the car above \$15,000 in those case.
22 But in my view it is appropriate to disallow above \$15,000
23 where the auto is a luxurious auto and not used to haul
24 goods and materials, and so forth.

25 Senator Danforth. All right.

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1 The Chairman. Senator Chafee?

2 Senator Chafee. Mr. Chairman, I wonder if we could
3 vote on these two things? Start with the Treasury one and
4 then go to the luxury automobile one?

5 Senator Bradley. Mr. Chairman?

6 The Chairman. Senator Bradley, we have already taken
7 this thing for a ride.

8 (Laughter)

9 Senator Bradley. As I understand the Treasury's
10 proposal -- I think I understand what the proposal is. So
11 that would be the first vote?

12 The Chairman. What is the Treasury's proposal?

13 Senator Bradley. As I understand the Treasury's
14 proposal, it is that you will allocate a certain amount of
15 the use to business and a certain amount to personal. Is
16 that correct?

17 Mr. Pearlman. That is correct.

18 Senator Bradley. And that you will find a mechanism
19 of penalizing a greater personal use than you have stated
20 is the norm. Is that correct? You would deny a certain
21 part of ACRS?

22 Mr. Pearlman. Yes. I think the penalty here -- I
23 don't think we would change the rules in terms of the concept
24 of business and personal use. The personal use portion of a
25 car today is not deductible.

1 Senator Bradley. Right.

2 Mr. Pearlman. But what I hope we could do in the
3 legislation is perhaps raise the proof threshold, so that
4 taxpayers have to keep more careful records.

5 But the penalty is, if the use is less than 50 percent
6 so that the car is predominately personal, that we would
7 not make ACRS available. That's correct.

8 Senator Chafee. But the person could come in and show
9 that it is used for 75 percent business, and he could get
the 75 percent.

11 Mr. Pearlman. That is correct. Right.

12 Senator Chafee. Why don't we vote?

13 Mr. Pearlman. And then the second piece, which I had
14 mentioned before but let me mention again to make sure
15 everyone is aware of it, is that if the use drops below
16 50 percent, so that a car is used 100 percent for the first
17 three years for business use and it gets fully depreciated,
18 and all of a sudden it mysteriously gets converted into a
19 personal-use asset, that we would recapture the depreciation.
20 Those two don't have to sit together.

21 Senator Bentsen. What would you do, recapture it above
22 straight line?

23 Mr. Pearlman. No, it's a personal property asset, so
24 I think it would be fully recaptured, just as if it were
25 sold. If it were sold, there would be a full recapture.

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1 The Chairman. We will vote first on the Treasury
2 proposal, then.

3 Is there any objection to that proposal? If not, it
4 will be agreed do.

5 Senator Chafee. Now can we move to the second one,
6 which is essentially Senator Baucus's proposal -- which is
7 his proposal?

8 Senator Bradley. Could Treasury explain the difference
9 between the two?

10 Mr. Pearlman. I think the difference is that we are not
11 -- let me give the easiest example I can think of. If a
12 very fancy car, a big limousine, is used 100 percent of the
13 time for business use, our proposal would not affect that
14 automobile, notwithstanding what it costs.

15 Senator Baucus's proposal, if I understand correctly,
16 would say, "Nevertheless, the depreciable base is limited
17 to \$15,000."

18 Senator Baucus. With respect to cars; that's right. And
19 they are both consistent.

20 Mr. Pearlman. Yes. And so I think that is the
21 distinction.

22 Senator Baucus. That's right, and they work with each
23 other.

24 Mr. Pearlman. Yes.

25 Senator Danforth. This is even for a business use?

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1 Senator Baucus. Yes.

2 Senator Danforth. For an exclusively business use?
3 Let's suppose it is a limousine service.

4 Senator Baucus. No, we are taking care of limousines;
5 they are exempted. A limousine service is exempted from
6 this.

7 I am addressing the problem where somebody, you know,
8 takes a car, uses it partly for personal use and partly for
9 business use, but even where it is 60 or 70 or 80 percent for
10 business use, he says, "Oh, here is a great opportunity to
11 take the full benefit of ACRS, the investment tax credit,
12 depreciate it fully," and so buys a very luxurious car.

13 My view is that the business use can be accommodated
14 very easily for \$15,000 worth of the car. You can
15 depreciate that part of it, but the person should not be
16 able to get the full benefit for even the business use of a
17 luxurious automobile, because I just don't think our Code
18 should encourage that.

19 The fact is, if you get a \$40,000 car, and fully
20 depreciate it in three years and get the full benefit of the
21 investment tax credit, then resell that car in three years,
22 sure, the depreciation is recaptured, but you probably still
23 come out with a net gain on it, because most luxurious cars
24 have very high resale values.

25 Senator Bradley. Mr. Chairman, I think this is a very

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1 arbitrary choice here. There are a lot of abuses in the Tax
2 Code, ranging from the capital gains treatment for timber
3 assets to ACRS to a variety of other measures in the Code.

4 I would hope that, since we have addressed this issue
5 already with the amendment that the committee just adopted,
6 that we wouldn't push this thing to a vote. I think that
7 this singles out a particular items that is termed
8 "luxurious," while not affecting many other items that could
9 equally be termed "luxury items."

10 I would hope that we could refrain from pushing this
11 to a vote. As I understand it, the amendment is open to
12 further amendment, and everyone has their things in the Code.

13 The Chairman. Well, what I would like to do is make
14 some disposition of it. Maybe we could do it on a voice
15 vote. Do you have any objection? Do we have enough here?

16 Senator Long. Is this just for all automobiles?

17 The Chairman. Well, all above \$15,000.

18 Mr. DeArment. There are sort of three exceptions that
19 we are talking about: Any ambulance, hearse, or combination
20 ambulance/hearse used in a trade or business; any vehicle
21 used by the taxpayer directly in the trade or business of
22 transporting persons or property for compensation or hire;
23 or farm vehicles that are multi-purpose farm or utility
24 vehicles that are used. Other than that, they would be
25 subject to this limit.

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1 Senator Long. What will this thing raise?
2 Senator Baucus. It raises about --
3 Mr. DeArment. \$500 million over the period of time.
4 Senator Bradley. That is with the exception of farm
5 vehicles? That was added today after the revenue estimates?
6 Senator Baucus. No, no, no.
7 Mr. Wetzler. No, that was in the original bill.
8 Senator Baucus. That was always in it.
9 Senator Bradley. All right.
10 Senator Chafee. Let's vote.
11 The Chairman. All right. Let's vote.
12 Mr. DeArment. Mr. Packwood?
13 (No response)
14 Mr. DeArment. Mr. Roth?
15 (No response)
16 Mr. DeArment. Mr. Danforth?
17 Senator Danforth. Aye.
18 Mr. DeArment. Mr. Chafee?
19 Senator Chafee. Aye.
20 Mr. DeArment. Mr. Heinz?
21 (No response)
22 Mr. DeArment. Mr. Wallop?
23 (No response)
24 Mr. DeArment. Mr. Durenberger?
25 (No response)

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

1 The Chairman. I vote No, and Senator Heinz votes No.
2 Senator Long. Well, if the Chairman is going to vote
3 No, then I am having second thoughts; I'm going to have to
4 vote No.

5 (Laughter)

6 Senator Bradley. Any others?

7 (Laughter)

8 Senator Long. My political authority is beginning to
9 diminish.

10 (Laughter)

11 Senator Chafee. Let me just say, I think it is a good
12 bill except for the indexing part of it.

13 (Laughter)

14 Senator Baucus. Well, we can cut the deficit if we can
15 keep inflation and interest rates down.

16 The Chairman. I don't have any quarrel with the bill;
17 I just think there is a better way we can do it. I hope
18 this doesn't foreclose maybe Treasury spending some more time
19 with the principal sponsors.

20 Senator Baucus. That's fine, sure.

21 Senator Long. Could I bring up an item, Mr. Chairman,
22 that I think might help a little bit?

23 The Chairman. Certainly. About \$5 billion would help.

24 Senator Long. Let me ask about these abusive tax
25 shelters.

1 Senator Baucus. Could we announce the vote, please,
2 first, Mr. Chairman?

3 Mr. DeArment. The vote was 10 to 3 in favor of the
4 proposal.

5 Senator Bradley. Ten to 4.

6 Senator Long. I changed my vote.

7 Mr. DeArment. Yes, 10 to 4; I'm sorry.

8 Senator Long. Let me ask about the abusive tax
shelters. Can you tell me how much you are doing by way of
notifying these people that this particular tax shelter might
11 be found to be an abusive tax shelter, and if so, they won't
12 get the full benefit of it?

13 Mr. Pearlman. Well, Senator, that is a new program. I
14 do not have statistics with me. I will be happy to get them
15 for you. But the Service has initiated a program whereby
16 it does examine tax shelters that are advertised and with
respect to which people voluntarily send in literature. They
review those programs, and if they determine that one is
19 abusive, then they do notify the promoter, and they have been
20 doing that. We are trying to do that very carefully, so we
21 make sure that we are only doing that in the case of truly
22 abusive shelters. That program is really in its infancy, but
23 I think the Service would say that to date it has been very
24 effective.

25 The Department of Justice is beginning to utilize the

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1 injunction procedures that were provided in TEFRA, and
2 Justice has obtained several and perhaps even more
3 successful injunctions against shelters that have been
4 determined to be abusive. So I think that process is
5 underway. I think only time will tell how successful and
6 how extensive it can be used.

7 Senator Long. Well,--here is the thought that occurs to
8 me:

9 Now, I don't think any of us here really favor these
10 two-for-one and three-for-one and four-for-one type tax
11 shelters; but, obviously, you can't blame the taxpayer for
12 taking advantage of it if it is out there and it's legal.

13 The thought occurs to me that, in view of the fact that
14 only a small percent of the returns are audited on what they
15 call the "lottery system," the accountants advise people to
16 go into these things because the odds are they won't even
17 be audited, the odds are they will get away with it.

18 It seems to me that we ought to shift the odds. And
19 the way to shift the odds, it seems to me, is to say that
20 once you let these people know that this might be found to
21 be an exotic tax shelter or that it is an abusive tax shelter
22 -- I like to use the word "exotic" -- but once it is declared
23 to be such a tax shelter, that from that point forward it is
24 not just an injunction, but if that is so determined, that
25 they are not going to get their depreciation, they are not

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1 going to be able to deduct the interest. So they really
2 get hurt. In other words, the time they gamble, they have
3 something to lose.

4 The way it is now, they gamble, and they are all on the
5 win side; if they don't get audited, they get away with it;
6 if they do get audited, they still might get away with it;
7 and if they do get caught, they don't get penalized,
8 particularly.

9 It seems to me as though if we said, "If you do this,
10 you can't deduct your depreciation, and you can't deduct the
11 interest," we could fix it so they really lose something,
12 get hurt.

13 Then my thought would be, if I ran the program for you,
14 don't tell them whether this is going to be regarded as an
15 abusive tax shelter until the end of the year. Let them get
16 their neck out a mile and then chop it off on them. Make
17 them really lose money with it. After you do that a few
18 times, that will really break some of them up, because
19 people will be scared to death to go into them.

20 Senator Grassley. Well, we did increase the penalties,
21 didn't we, in TEFRA?

22 Mr. Pearlman. Yes. There were increased penalties.
23 Let me emphasize that I can assure you that every time the
24 Service reviews one of these shelters and notifies that
25 promotor and the investors that they determine it to be

1 abusive, whether there is an injunction or not, those people
2 are going to be visited by an Internal Revenue Agent, and
3 those shelters are going to be examined.

4 In addition to that, the general audit coverage
5 percentage of 1.6 percent is very misleading, as the
6 Commissioner pointed out yesterday, when you talk about
7 these kinds of transactions. The Service has rather
8 sophisticated selection techniques, whereby it is able to
9 identify through the computer system those returns where
10 certain levels of deductions are being taken, and those
11 returns are susceptible to a much higher level of
12 examination than the national 1.5 percent average.

13 Senator, I think that there is no question that the way
14 to deal with the tax shelter, in addition to the kind of
15 legislative efforts that the committee has been willing to
16 look at and indeed support over the last couple of days,
17 is to put people on notice upfront that they have got the
18 risk of examination, disallowance, and penalty.

19 I think it is important to balance that, however,
20 against the risk that you improperly intrude on transactions
21 which we might define as a tax shelter but which are
22 perfectly legal under law; for example, the shelter that
23 takes advantage of investment tax credits or ACRS, or
24 whatever.

25 I think it is important that the Service go easy and not

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1 go overboard and then be accused of being so capricious and
2 arbitrary that we all are critical of examination techniques.

3 Senator Long. I don't want you to be capricious, and
4 I don't want you to be arbitrary; but it seems to me that
5 the odds are overwhelmingly in favor of the people who
6 engage in this kind of activity. In other words, (a) they
7 might not be audited, (b) if they are audited, they might
8 get away with it any way. It would seem to me that we
9 might be able to help get the job done if we would fix it
10 so that if they lose, they really get hurt.

11 I am just asking, do you think there are ways we could
12 improve on that statute to make it more effective?

13 Mr. Pearlman. I have one specific suggestion I can make
14 to you now, and we will be happy to come back to you and
15 offer whatever additional suggestions come to us in our
16 discussions with the Service.

17 Senator Long. What did you have in mind?

18 Mr. Pearlman. As I mentioned a moment ago, there is
19 presently in the Code, as a result of TEFRA, an injunction
20 proceeding that is available to the Government so that it
21 can enjoin the marketing of so-called "abusive tax shelters."

22 One of the problems that the Justice Department has had
23 in using that injunction proceeding has to do with shelters
24 which include -- which is frequently the case -- a serious
25 question about the valuation of a piece of property.

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1 Frequently a tax shelter is abusive because a piece
2 of property is overvalued to a material extent in order to
3 increase the depreciable base for depreciation purposes.

4 When the Justice Department gets into Court in the
5 injunction proceeding in that kind of transaction, the
6 taxpayer brings in his expert witness -- the partnership,
7 for example -- and then the Government brings in its
8 expert witness, and they are 10 miles apart on valuation,
9 and the Court is reluctant, understandably, to issue an
10 injunction in that kind of a situation.

11 We think that it may be desirable for the committee
12 to consider establishing some objective criterion for
13 shifting the burden of proof in these valuation cases, so
14 that the injunction proceeding can operate in valuation
15 cases. One way to do that, and one that we think might
16 be constructive, is, if the valuation claimed by the
17 shelter exceeds a certain percentage of a recent purchase
18 price -- 150 percent, for example, of a recent purchase or
19 sale price -- that the burden should shift to the taxpayer
20 to prove that that is not an excessive valuation.

21 We think that that is more or less what I would say
22 "a minor amendment to a major compliance piece of TEFRA,"
23 and we think that is the kind of thing that the committee
24 might consider as a way to beef up the Service's ability to
25 get at what you are describing as the "exotic" or the

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1 abusive shelter.

2 Senator Long. Well now, that's fine with me. I think
3 I could support that. But I would like to see if we can't
4 do better than that by fixing it so that when people go into
5 these abusive tax shelters, they do so at their peril.
6 That's what I have in mind.

7 For example, the kind of thing I have in mind -- I
8 have had people tell me about them and say, "Well, now, we
9 have a great tax shelter. This is a 3-for-1 shelter; you
10 put up a certain amount of money, and you get three times
11 as much deductions as if you take risk," or something of
12 that sort.

13 And I am saying that I believe the way to break them
14 up is to fix it so that if you go into something like that,
15 that you ought to be on notice that anytime somebody tells
16 you about a 2-for-1 or a 3-for-1 tax shelter, you had better
17 keep in mind that you might really lose a lot of money
18 on that thing, because it might wind up being declared an
19 "abusive tax shelter," and, if so, you would lose all of
20 your deductions. I don't mean all of the appropriate
21 deductions, I mean everything that is involved in that tax
22 shelter, so that you would have the income to pay, but no
23 deduction out of it. That way, you would really lose some
24 money on it.

25 Furthermore, if that happened at the end of the year,

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1 so they had no chance to get themselves out of the trap,
2 so that the gate snapped shut and they were stuck, and they
3 would lose a lot of money at it, I would think
4 heard how taxpayers come up and complain bitterly that they
5 went into a tax shelter, and how outrageous it was that they
6 lost their money and had had denied all their deductions,
7 they would stop going into them. A lot of them would -- they
8 would be afraid to go.

9 So far, you are talking about just getting an injunction
10 that says, "You can't go forward with this thing." Well,
11 I would like to fix it so that they would say, "Oh, yes, if
12 somebody has got you a 3-to-1 tax shelter, you'd better
13 lock out. You are liable to really get hurt." And I don't
14 think you've got it that way yet, have you?

15 Mr. Pearlman. Well, I am not saying we've done
16 everything, but Congress did a lot in TEFRA to put pretty
17 substantial penalties on the taxpayer who goes into that
18 shelter and gets caught down the road. There are
19 overvaluation penalties, there are a variety of things that
20 are going to make that an awfully painful experience for the
21 taxpayer.

22 But I would suggest, let us come back to you and see if
23 there are additional things that we believe need to be done.

24 I think one of the things that is important here is that
25 we gave the Revenue Service a lot of ammunition in 1982, and

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1 I think it may be appropriate to see how those rules work
2 for a couple of years before we load up a bunch more items.

3 But we would be happy to come back to you and make
4 some suggestions.

5 Senator Long. Well, it seems to me that -- up til now
6 I was advocating that minimum tax before we ever had a
7 minimum tax -- we struggled with so many different ideas,
8 and it looks to me like we are always playing catch-up ball,
9 that they've got us beat by \$100 billion a year on this
10 chiseling business. It looks to me like we need to get
11 ahead of the game at some point.

12 What appeals to me is if we fix it so that if they go
13 into something like that, that they might really lose a lot
14 of money by doing it. Now, that's what would make them stop
15 it.

16 I would appreciate it if you would do some more work
17 and see if you can come up with a suggestion before we finish
18 on this bill.

19 Mr. Pearlman. We would be happy to do that.

20 Senator Long. Thank you.

21 Senator Chafee. Mr. Chairman?

22 The Chairman. Yes, Senator Chafee.

23 Senator Chafee. I am unable to stay -- not because of
24 this vote, but I mean return, under the present arrangements
25 anyway. Is there any chance of disposing of my proposal on

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1 the residential structures?

2 The Chairman. Do we have something in writing on that?

3 Senator Chafee. Yes, we do. Somebody has circulated
4 it. What they have said is, they have come up with a
5 series of proposals, and I think the best proposal is as
6 follows: That the proposed rule would be the 20-year
7 depreciation for residential property -- that it would be
8 that -- except for buildings where 85 percent or more of the
9 units are rented to individuals meeting the definition of
10 "low" and "moderate" income. Now, if the definition of low
11 and moderate income is below 80 percent of local median
12 income adjusted for family size.

13 Senator Pryor. Now, what would that change be in the
14 present law, as we now have, Senator?

15 Senator Chafee. Well, the law as it is passed with
16 Senator Bentsen's amendment would exclude all housing from
17 the 20-year rule.

18 The Chairman. Has Treasury had a chance to review the
19 amendment?

20 Mr. Pearlman. Yes, we have, Senator. We continue to
21 believe that it is not appropriate to make a distinction
22 between housing and other property. We share Senator
23 Chafee's view on that point. And while this is an arbitrary
24 way to try to define "low" and "medium" income housing, it
25 is certainly an acceptable way as far as we are concerned,

1 and we will be happy to work on some other alternative.

2 The Chairman. What about the Joint Committee?

3 Mr. Wetzler. Well, this is a workable amendment.

4 Senator Chafee. Let's show a little more enthusiasm.

5 Mr. Wetzler. That's what Senator Chafee intended,
6 which is to keep 15 years for low and moderate, and go to
7 20 years for buildings where predominately they are upper
8 income.

9 The Chairman. As I understand it, there is also someone
10 from GAO here present? Mr. Gaines?

11 I guess what we are trying to determine is whether or
12 not the amendment accomplishes what some indicate they would
13 like to do, and that is to make certain that we -- well, I
14 guess one way to do it across the board is to just put
15 everything under the 20 years. Here there is some
16 exception made.

17 Are you familiar with the amendment?

18 Mr. Gaines. I just saw it a few minutes ago, and I
19 can answer technical questions, but I just want you to know
20 that I am not speaking for a GAO position.

21 The Chairman. Right. Has the GAO reviewed this area
22 at all?

23 Mr. Gaines. We have done some work in the past on the
24 tax-related costs of real estate, and we have some work under
25 way right now.

1 As I understand the proposal, it would just create
2 this distinction between low and moderate income housing,
3 middle income housing, and that the rule that would be used
4 for defining "low and moderate income" would be similar
5 to what has been used in the Tax Code in the past, and that
6 that rule would be less stringent than the one now being
7 applied to low and moderate income housing under say the
8 Section 8 or Public Housing Programs, that Congress just
9 changed that rule to exclude everyone except very low income
10 households.

11 The Chairman. What would be the revenue implications
12 of this amendment?

13 Mr. Wetzler. Well, we are still trying to work on the
14 revenue estimates. It was just worked out, you know, an hour
15 ago, and I hope to have something for you pretty soon.

Senator Chafee. It will pick up revenue, though.

17 Mr. Wetzler. It will certainly gain revenue, yes. If
18 you did all of housing, it would be about a billion-one, and
19 this will be some fraction of that, and we are trying to
20 figure out an estimate of how much.

21 Senator Pryor. May I ask the Treasury what the
22 position is of the Treasury Department on not only Senator
23 Chafee's amendment but also the Bentsen amendment that was
24 adoped earlier, which I understand now is a 10-to-8 vote with
25 two members not having been recorded.

1 Mr. Pearlman. Senator Pryor, we would have preferred --
2 if the committee decides to go from 15 to 20 years, we would
3 have preferred to make a distinction between new and used
4 property rather than between commercial property, on the
5 one hand, and housing on the other.

6 Now that the committee has chosen to make no new and
7 used distinction but instead to make a distinction between
8 residential and commercial and industrial property, we
9 believe that Senator Chafee's approach of narrowing that
10 distinction to make it less of an across-the-board
11 distinction is a good modification to the proposal that the
12 committee has already adopted.

13 Senator Pryor. Is it a good modification to something
14 you support or don't support?

15 Mr. Pearlman. I think we can't support the extension
16 of ACRS from 15 to 20 years for new property. The whole
17 spirit of ACRS was to try to encourage capital investment,
18 and to extend the life for new property we don't think is a
19 wise thing to do now.

20 If the committee is going to do that, however, we think
21 it is not desirable to create a distinction between
22 industrial property, on the one hand, where we think it is
23 important for continued capital investment, and housing on
24 the other, other than low and moderate income housing, with
25 which we have no problem.

1 The Chairman. Well, let me remind the members that we
2 have about five minutes left on this vote.

3 Senator Bradley. Mr. Chairman, are we going to come
4 back, or not?

5 The Chairman. Yes. There are two or three items I
6 think we can accomplish yet this afternoon.

7 Senator Chafee, will you be able to come back?

8 Senator Chafee. Well, I would like to vote on this,
9 if we could, to see where the chips are going to fall.

10 The Chairman. Do you want to vote on it now?

11 Senator Chafee. I would.

12 Mr. DeArment. Mr. Packwood?

13 (No response)

14 Mr. DeArment. Mr. Roth?

15 (No response)

16 Mr. DeArment. Mr. Danforth?

17 Senator Danforth. Aye.

18 Mr. DeArment. Mr. Chafee?

19 Senator Chafee. Aye.

20 Mr. DeArment. Mr. Heinz?

21 (No response)

22 Mr. DeArment. Mr. Wallop?

23 The Chairman. No.

24 Mr. DeArment. Mr. Durenberger?

25 (No response)

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

1 Mr. DeArment. Mr. Chairman?

2 The Chairman. Aye.

3 And I think Packwood votes Aye.

4 Senator Chafee. Senator Durenberger is on his way.

5 The Chairman. Right now the Yays are six and the Nays
6 are six, so the amendment is not agreed to.

7 Senator Symms. Mr. Chairman, is it in order to
8 reconsider the vote on the Bentsen amendment?

9 Has Armstrong got a proxy in here, does anybody know?

10 The Chairman. We will leave the record open.

11 Let's go and come back if we can; there are two or
12 three items we can take care of.

13 (Whereupon, at 3:50 p.m., the session was recessed.)

14 AFTER RECESS

15 (4:13 p.m.)

16 Senator Moynihan. Mr. Chairman, we have been able to
17 spot the gremlin that Senator Bentsen very accurately
18 sensed was in our alternative minimum tax proposal, and now
19 I believe it has been resolved. He was quite right, and
20 resolution was possible. We have resolved it, and I wonder
21 if we might get on with the job and add up our total?

22 The Chairman. Right. I guess we don't need the revenue
23 estimates. They are not ready yet, are they, Jim?

24 Mr. Wetzler. Well, we are hoping to get them within
25 a few minutes.

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1 The Chairman. But the point I would make is, when you
2 have that in the precise language, if you would clear that
3 with Senator Bentsen.

4 Mr. Wetzler. The draft language?

5 Senator Bentsen. Well, he showed me the language. That
6 is the language that you sent me. It at least showed what
7 you were accomplishing. And if you do that with the
8 language, that's fine.

9 Mr. Wetzler. We haven't done drafting on this.

10 Senator Bentsen. No, I understand that.

11 Senator Moynihan. But Senator Bentsen is satisfied
12 with what you mean to accomplish by the draft in that
13 spectacular language in which the tax law is written, then.

14 Then I would propose that we -- I don't know if there
15 is enough of a "we" here. Senator Danforth is out in the
16 corridor.

17 The Chairman. Is that right? Or do we need seven?

18 Mr. DeArment. We need five.

19 The Chairman. Oh, five. Excuse me.

20 What about Section 1231? That was another area we were
21 going to look at during the noon hour. Has Treasury had a
22 chance to review that?

23 Mr. Pearlman. Yes. We had looked at that provision
24 last year, Senator. I am not necessarily in opposition, but
25 I think the committee should understand the effect of the

1 provision, and that is, to the extent that a loss in one year
2 is going to have an effect because of a gain in the other,
3 or vice versa, there is a much greater likelihood that a
4 casualty loss or an involuntary conversion experienced by a
5 taxpayer because his business goes under or he suffers a
6 catastrophe in his business, it is going to be converted from
7 an ordinary loss to a capital loss, and that concerns us.
8 For that reason, we are reluctant to see the proposal enacted
9 in its present form.

10 I would suggest that if the committee pursues this
11 proposal and adopts it, that it might consider excluding
12 from the matching rule losses experienced by casualty or
13 involuntary conversions, so that if someone has a totally
14 unanticipated loss that he can't control -- fire, or other
15 casualty -- that he will not be penalized merely because he
16 had a 1231 gain in another year.

17 I think the abuse here is the planned transaction, where
18 you have some 1231 losses and some 1231 gains, and you make
19 a decision as to when you are going to dispose of a piece of
20 property so that you can maximize the losses and minimize
21 the gains. And it is less likely that that will happen when
22 you are talking about involuntary conversions and casualty
23 losses.

24 So we would suggest, if the committee goes forward, that
25 it consider modifying the proposal to take that into

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1 consideration.

2 The Chairman. Jim, do you have any comment?

3 Mr. Wetzler. Well, Mr. Chairman, we have the revenue
4 estimate now on the minimum tax proposal, which would raise
5 \$1.2 billion, which is less than the \$2.0 billion we had
6 this morning, but it is still a significant revenue item.

7 The Chairman. All right.

8 Senator Danforth. And this includes the foreign
9 taxation?

10 Mr. Wetzler. Yes. This is the original proposal,
11 which includes the foreign earned income and the loss rule,
with the modification to deal with the real loss problem.

12 Senator Moynihan. Mr. Chairman, I would move the
13 measure.

14 The Chairman. All right. Without objection, it will
15 be agreed to.

16 The 1231, Jim. Did you listen to the Treasury's
17 explanation of that?

18 Mr. Wetzler. Yes.

19 The Chairman. Would we make certain exclusions?

20 Mr. Wetzler. Well, I think that would be an
21 appropriate modification; if you want to approve the
22 provisions with Treasury's suggestion I think you would still
23 preserve much of the revenue involved.

24 The Chairman. Pardon?

1 Mr. Wetzler. I think you would still preserve much
2 of the revenue gain that was in the estimate.

3 The Chairman. Does that satisfy the concerns of
4 Treasury? Mr. Pearlman?

5 Mr. Pearlman. Excuse me. I'm sorry.

6 The Chairman. If we do the things you have suggested,
7 does that take care of your concerns in this matter?

8 Mr. Pearlman. Yes. I think that largely takes care
9 of our concerns.

10 Senator Matsunaga. Mr. Chairman, did I hear Jim say
11 that it will bring in 1.2?

12 Mr. Wetzler. The minimum tax would be 1.2 -- the one
13 that was just agreed to. This would be .5, a little less
14 than .5, because of the amendment Treasury is suggesting.

15 (Pause)

16 The Chairman. All right, then. If we agree to the
17 1231 with the modification, as I understand Treasury would
18 have no objection to that 1231 change with the modification?

19 Mr. Pearlman. With the modifications, that is correct.

20 The Chairman. Without objection, we will agree to that.

21 (Pause)

22 Senator Symms. Mr. Chairman? I was just informed by
23 my staff that the minimum tax was just passed. That's not
24 true, is it?

25 The Chairman. Right.

1 Senator Symms. Is there going to be a chance to vote
2 on it?

3 The Chairman. Sure. Do you want to vote?

4 Senator Symms. Well, I guess it is the same things I
5 said this morning; I think that in order to target these
6 people that we want to get at, that Senator Moynihan is
7 talking about, what we are doing is taking away any
8 incentive for anyone who doesn't have wealth to ever be an
9 entrepreneur, and I think that's just absolutely the wrong
10 thing for this committee to be doing. I want to be recorded
11 as No on that. I am not in favor of anti-entrepreneurial
12 activities, and I would like to be recorded as No.

13 The Chairman. All right. Let the record indicate.

14 Senator Bradley. Mr. Chairman?

15 The Chairman. Senator Bradley?

16 Senator Symms. Maybe there are other members. I
17 don't know if any of the other members want to vote on this
18 or not.

19 The Chairman. I asked if there was any objection. We
20 had a quorum present, and there was no objection, so we
21 agreed to the amendment. We addressed the concerns expressed
22 earlier by Senator Bentsen. I think you may have touched on
23 the same thing, as far as real losses were concerned, and
24 they have agreed to clear that draft language with Senator
25 Bentsen. And, based on that, the amendment was adopted

1 without any request for a vote, rollcall.

2 Senator Bradley?

3 Senator Bradley. Mr. Chairman, I wonder, if we don't
4 finish today, it is your intention to come back next
5 Tuesday, as I understand. Is that right? If we don't
6 finish today?

7 The Chairman. Yes.

8 Senator Bradley. I wondered if I could ask the staff
9 some questions, and if they don't have the answers maybe
10 they could get them by next Tuesday.

11 I wonder, what is the total revenue cost of the
12 investment tax credit?

13 Mr. Wetzler. I think it is around \$20 billion a year.

14 Senator Bradley. Twenty billion dollars a year? And
15 then, for half of that, it would be \$10 billion a year?

16 Mr. Wetzler. Roughly, yes.

17 (Laughter)

18 Mr. Wetzler. It's roughly 20, so half of it would be
19 roughly 10.

20 Senator Bradley. Well, you never know. Sometimes that
21 is, and sometimes it isn't.

22 (Laughter)

23 Senator Bradley. I mean --

24 Senator Bentsen. I think that's a legitimate question,
25 Senator, I really do.

1 Senator Bradley. That's right. We passed a tax bill
2 that was supposed to get more revenue and --

3 Anyway, the present ACRS system, if it was returned to
4 essentially the system that existed prior to the 1981 Act,
5 how much revenue would that raise?

6 Mr. Wetzler. I am not exactly sure, Senator. We will
7 try to get that for you next week.

8 Senator Bradley. Could you possibly get that?

9 But on the investment tax credit, it's \$10 billion a
10 year? What did you say on the investment tax credit?

11 Mr. Wetzler. The whole credit was about 20, and half
12 the credit is about half of that.

13 Senator Bradley. All right.

14 If in this package we are shooting to raise \$48 billion
15 and we have already raised \$21 billion, we are really looking
16 for \$19 billion? How much in revenue would it cost to
17 reduce rates by say basically a couple of points?

18 Mr. Wetzler. Well, the corporate rate is about a
19 billion dollars per point.

20 Senator Bradley. A billion dollars per point? What
21 about on the individual side?

22 Mr. Wetzler. Well, there, of course, you have a
23 progressive rate schedule. So if you reduced each rate by
24 one percentage point, that would, I imagine, probably involve
25 somewhere on the order of \$15 billion.

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1 Senator Bradley. Fifteen billion dollars.

2 So if you could get those numbers, I would like that,
3 because we might have a chance to vote for not only some
4 tax reform but some rate reduction next week.

5 I know Senator Symms wants to vote for rate reduction.

6 The Chairman. Yes, he is for the rate reduction.

7 I think the one item we want to take up yet today is
8 the financed lease rules, and Senator Durenberger has a
9 direct interest in that. He is with another committee.

10 Mr. DeArment. Mr. Chairman, one item that is a matter
11 of housekeeping, that I hoped we could take up today, was
12 approving the committee rules for yet another year.

13 We would propose that the committee rules would
14 continue in their present form.

15 The Chairman. There are no changes suggested?

16 Mr. DeArment. No changes proposed.

17 The Chairman. Do you mean we have been operating
18 without rules?

19 Mr. DeArment. No, we have been operating with rules.
20 But the Senate rules require that on March 1st of every
21 year they be republished.

22 The Chairman. Oh. Is there any objection to republishing
23 the rules, agreeing to the rules?

24 (No response)

25 Senator Bradley. How much does that cost, Mr. Chairman?

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1 The Chairman. That's a revenue gain.

2 (Laughter)

3 Mr. DeArment. We won't actually republish them; we
4 will put them in the Congressional Record.

5 The Chairman. That costs something.

6 Does Treasury have any other areas that we have been
7 working on with members?

8 Mr. Pearlman. We can report to you, Mr. Chairman, on
the nuclear decommissioning piece of the premature accrual
package where we think agreement has been reached, on the
11 nuclear decommissioning exception relief. However, we
12 are still working on the coal mining reclamation piece, but
13 we are very close to agreement. We should be prepared to
14 report to you Tuesday morning on that.

15 (Pause)

16 The Chairman. Let's try just for a minute to reach
17 Senator Durenberger, and if he can't -- I know he is wrapped
18 up in another committee right down the hallway.

19 Can you report what action the House has taken, Jim?
20 Are they still in session?

21 Mr. Wetzler. Well, last I heard they were. They were
22 hoping to finish tonight, and I think they had approved a
23 number of freeze items, including some of the ones approved
24 here, and most of the additional ones in Chairman
25 Rostenkowski's package. I think they had approved a fairly

1 sizeable number of the reform provisions. I am not sure
2 exactly which ones.

3 The Chairman. I think the Administration should know
4 that if they can't come up with some more revenues, we are
5 not going to consider any of their losers. I mean, if we
6 are now asked to subtract -- we don't have what we need
7 right now, but if we are asked to subtract from 45.8, we
8 are back to 37, and I don't get much enthusiastic support
9 from the Administration on a number of these items.

10 We will work out something on structures. I mean,
11 sooner or later we are going to have to work it out. I
12 know there is a lot of jockeying going on right now, but
13 I think that is one area where I think the Administration
14 could be helpful.

15 We will vote on the health care cap, but I think
16 I can count -- I don't think there are the votes to pass it.
17 Maybe there will be some modification that might be
18 satisfactory.

19 But beyond that, the section of the financed lease
20 rules, we have just about covered the waterfront.

21 I don't quarrel with the Administration; they are not
22 in a position to do anything on capping consumer interest
23 unless it were part of the bipartisan agreement. Do I
24 understand that correctly?

25 Mr. Pearlman. That is an accurate statement.

1 The Chairman. And I don't think we want to mess around
2 with the \$100 dividend exclusion repeal.

3 What about the three-year base for income averaging?
4 Is that something they have done on the House side, or is
5 this a new wrinkle on what we have done earlier?

6 Mr. Wetzler.. Well, this is something you considered
7 last Fall and decided not to do, but we just put it on the
8 list again because I think you were fairly close to doing it,
9 and now when you are this close to your revenue target,
10 you know, it might warrant another look.

11 Today your income averaging is based on the four prior
12 years' income and the excess of your current year's income
13 over 120 percent of your base. In the Reconciliation
14 Package, you agreed to raise the 120 percent up to 140
15 percent. This proposal would, in addition to that, shorten
16 the base from four years to three years. That has really
17 two principal effects:

18 First, the three-year base is likely to be higher than
19 the four-year base, because income grows over time, so you
20 would have less averageable income in the current year; and

21 Secondly, income averaging has the effect of spreading
22 the averageable income today over five years, and this would
23 change it so that it only spreads it over four years. So
24 you get basically less benefit from income averaging, and
25 the revenue gain would be \$1.6 billion.

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1 I guess the argument for doing something here is that
2 you have cut rates significantly, and cut the top rate to
3 50 percent, you have indexed, and so there is somewhat
4 less need for income averaging now than there was prior to
5 the 1981 tax cuts. So it is a relatively noncontentious
6 way of raising some money.

7 Last Fall when this was discussed, there was some
8 concern over the effect on farmers. We have looked at the
9 statistics, and really farmers are not affected by this
10 proposal disproportionately to their share of the whole
11 population. Well, they are affected, of course, but they
12 are not really affected any more or less than any other
13 sectors are, not significantly more or less.

14 The Chairman. What kind of person is affected by this?

15 Mr. Wetzler. Well, really two kinds. There are people
16 who have sharp jumps in their income, and they of course are
17 also often people who benefit from the cut in marginal tax
18 rates. And then people, especially ones who are starting out
19 and getting rapid increases in their income over a period --
20 rather predictable, steady increases, as people do when they
21 start working -- and then they benefit from income averaging.

22 Senator Bentsen. But they would still have four years
23 if we cut to three. You would raise the base -- what? To
24 140 percent?

25 Mr. Wetzler. Well, the committee has already agreed

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1 last Fall to raise the threshold, so the income averaging
2 will only apply to the extent that your current year's
3 income exceeds 140 percent of your base. And now the
4 question is, should the base be shortened from four to
5 three?

6 Senator Bentsen. To the three-year base from the
7 four-year base, yes. You would move to a three-year base
8 instead of a four-year base.

9 Mr. Wetzler. This proposal would, yes.

10 Senator Bentsen. How much additional money would you
11 pick up?

12 Mr. Wetzler. About a billion, 600 million over the
13 three years.

14 The Chairman. Does the Treasury have any position on
15 this?

16 Mr. Pearlman. I can't say it's a strong position,
17 Mr. Chairman, but we are concerned about narrowing the base
18 from four to three years. It brings a lot more taxpayers
19 into the averaging system, because you have a fewer number
20 of years. Although I think Mr. Wetzler is right, it does
21 raise more money.

22 Our approach was to leave the base at four years and
23 widen the brackets, and I think that is still our preference.

24 The Chairman. Well, we've done that.

25 Mr. Pearlman. Yes, you have done that. Right.

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1 Mr. Wezler. Treasury's suggestion would lose about
2 half of the 1.6 that the full proposal would. So it is
3 really just a matter of how much do you want to cut back.

4 The Chairman. I think the point they make -- do you
5 have any estimate on how many more taxpayers are going to
6 be affected?

7 Mr. Pearlman. We do, and I'm sorry, I just don't have
8 that data in front of me. But I can provide that. We did
9 do an estimate on the number of taxpayers.

10 The Chairman. Let's just reserve that until Tuesday,
11 but let's put that at the top of the list to vote on or
12 consider in some way.

13 Senator Durenberger?

14 Senator Symms. Mr. Chairman, what did they say about
15 farmers on that? Senator Grassley had asked about that
16 earlier.

17 Mr. Wetzler. Well, we have some statistics on how many
18 farmers would be affected by the proposal, and it is really
19 not significantly disproportionate to their share of the
20 overall population.

21 Senator Pryor. They don't make enough to pay taxes.

22 The Chairman. Well, some do.

23 Mr. Wetzler. I have some actual computer runs.

24 Senator Symms. But you are going to set that over until
25 Monday, right?

1 The Chairman. On Tuesday.

2 Senator Symms. All right.

3 The Chairman. Why don't we get that information for
4 Senator Symms.

5 Senator Durenberger? I know you are anxious to be
6 heard on this issue.

7 Senator Durenberger.. Which issue is this?

8 Mr. DeArment. This is the proposal to freeze the
9 financed lease rules.

10 Senator Durenberger. I would be glad to be heard on
11 that one. Thank you.

12 Mr. Chairman, in a way I appreciate your delaying the
13 discussion of this subject until the end of the big ticket
14 items, because it takes me back two years to where we were
15 with something called "safe harbor leasing."

16 I am not going to spend a lot of time explaining to you,
17 certainly, or to Spark or to Dave or to Steve what the
18 issue is, but let me just say why I oppose this notion.

19 First, it isn't the freeze that was contemplated by some
20 of the other freeze proposals that ran around here to cut
21 deficits, and that is freezing taxes. This is not a tax
22 matter; this is a financing matter, largely. It affects
23 people who have made decisions since July of 1982 on a
24 variety of financed leasing measures, and it is going to
25 disrupt a whale of a lot of contracts that are out there,

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1 some of them small and some of them extremely large.

2 But I think probably from my standpoint, more important
3 than that is a personal matter. I sat around here in 1982
4 with most of the rest of you and handed out bennies labeled
5 "Roth-Kemp" right and left to about half of America, while
6 the other half of America -- agriculture, steel, autos,
7 airlines, the basic industries in America -- got nothing
8 out of that process.

9 In 1981, after we did the big bennies, we had something
10 called "safe harbor leasing," and safe harbor leasing was a
11 modification of a system that grew up through investment
12 tax credits by which people could buy and sell the tax
13 credits -- it had been through leveraged leasing -- and it
14 became a great business. A lot of people made money selling
15 tax credits in this country. Big money center banks made a
16 lot of money, General Electric was the biggest hog of all --
17 they sucked up the money on leveraged leasing. A lot of
18 lawyers made money, a lot of tax people made money, everybody
19 who had to draft the contracts made a lot of money.

20 The people that didn't make much money were the
21 railroads and the airlines, and all the folks that weren't
22 profitable enough to have tax credits.

23 So we said, "Now that we are making it more profitable
24 for all the other folks out there with ACRS," Don Regan
25 said, "let's at least do something to access some of the basic

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1 industries in this country to some of the tax credits that
2 come with their investments. After all, they were making
3 the investments," so they created safe harbor leasing.

4 And somebody read a story where General Electric had
5 not paid any taxes because it took advantage of safe harbor
6 leasing. Well, General Electric had it both ways; they could
7 get it coming, they could get it going. They could make it
8 on leverage, they could make it on safe harbor. But they
9 got to be the example of the big hog at the trough on safe
10 harbor leasing.

11 So we came in here and pretty well did away with safe
12 harbor leasing. In the process, this Senator did one of those
13 things I was always told that Senators do, and he sold his
14 vote in order to save some of this safe harbor leasing and
15 to save some of the stuff that I am arguing for right now.

16 I gave you withholding. I was the key vote on
17 withholding, and it was at midnight one night in the
18 Chairman's office, to save that bill in 1982, and to save
19 what I thought was good for America, that we have had 10
20 months of withholding.

21 So, I want to pardon you, Mr. Chairman, for it. I
22 know you didn't want to go through this yourself, but I
23 could personalize the issue a lot more if you wanted me to.

24 (Laughter)

25 The Chairman. Could I just suggest we did freeze

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1 withholding, for a long time.

2 Senator Durenberger. Yes. I stuck with you to the
3 end on that one, too.

4 (Laughter)

5 Senator Durenberger. The poin here, simply, is that
6 this looks like a good goose to cook, time and time again.
7 But I sit here and think we are cooking the wrong geese. And
8 for that reason, Mr. Chairman, I think we ought to vote on
9 whether or not we get rid of this, or postpone it for four
10 years, or whatever this proposal is. I would like a record
11 vote on it.

12 The Chairma. What I would like to do, if it is all
13 right with Senator Durenberger, we have raised it today, is
14 to withhold the vote until Tuesday, to give Treasury some
15 time to find some alternatives, additional alternatives.

16 Would that be all right?

17 Senator Durenberger. Hold the vote?

18 The Chairman. Yes. We are down to about five members,
19 and there are three or four in the back of the room.

20 Mr. Wetzler. Mr. Chairman, could I just clarify that?

21 The Chairman. Yes.

22 Mr. Wetzler. On financed leasing, the revenue estimate
23 assumes that the proposal here will have transition rules
24 similar to the ones in Chairman Rostenkowski's amendment
25 over in the House side, which would grandfather in situations

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1 where the leases have already been signed, or they are
2 binding contracts, or construction has already begun on
3 the properties.

4 Senator Durenberger. Well, if I don't get the votes,
5 I would be glad to sit down and see what kind of
6 grandfathers and mothers got created.

7 For me this is a matter of principle. I mean, I feel
8 that strongly about it. So I hope that I can find nine or
9 ten other votes here just to keep it in place.

10 I have offered up billions of dollars in tax savings
11 that cut across the board and don't single out certain
12 industries in America like this does, but I would be glad to
13 support in lieu of it.

14 Senator Matsunaga. Mr. Chairman, perhaps the
15 personalization of his argument threw me off track, but is
16 the Senator for or against the proposal?

17 The Chairman. He is against it.

18 (Laughter)

19 Senator Durenberger. I am for the continuation of the
20 financed leasing.

21 Senator Matsunaga. All right.

22 The Chairman. All right, let's postpone that until
23 Tuesday. As far as I know, that pretty much covers every
24 proposal we have here, with probably two or three exceptions.

25 Now, are we available on Tuesday all day?

1 Mr. DeArment. Yes, Mr. Chairman, we are available
2 Tuesday all day.

3 The Chairman. How about Wednesday?

4 Mr. DeArment. Wednesday we have a hearing on the
5 Social Security Advisory Council's recommendations on the
6 Medicare Trust Fund Solvency.

7 The Chairman. When is that?

8 Mr. DeArment. At 10:00.

9 The Chairman. We may need to postpone that.

10 Mr. DeArment. All right. We can take that action.

11 The Chairman. Now, I have suggested to Senator Bentsen
12 and Senator Chafee and Senator Long that maybe on Monday if
13 Mr. Chapoton is available and Mr. Belas, and others, that
14 we might discuss the insurance package, sort of a
15 subcommittee, and then present that to the full committee
16 hopefully Tuesday afternoon. Otherwise, we never are going
17 to complete action on this total package.

18 So how many other add-ons are there? We are not going
19 to have room for any add-ons, as I can see. We are still
20 about \$6 billion short, and nobody wants to add anything to
21 that figure, so I don't want to add anything to the bill.

22 Senator Durenberger. Mr. Chairman, I made some
23 suggestions yesterday, and I wonder if there has been a
24 chance to look at that and come up with any estimates for the
25 revenue package?

1 Mr. Belas. Mr. Chairman, we have been spending a fair
2 amount of time with the various staffs, in particular on
3 the VIVA and cafeteria plan provisions. We still have a
4 little bit farther to go on both of those provisions. I
5 think, without any doubt, we will be ready on Tuesday to
6 discuss it in detail.

7 The Chairman. Well, maybe by Tuesday afternoon we
8 would like to get into the -- maybe at that time we could
9 offer the insurance report from the so-called "working
10 group" to the full committee. Obviously, we are not trying
11 to deny anybody their right to offer amendments, but it
12 might make it a little easier to facilitate. Maybe
13 Senator Durenberger would like to join that group on
14 Monday afternoon -- 3:00.

15 Is there anything else?

16 Senator Matsunaga. Mr. Chairman, do you recall that
17 last year before we adjourned I requested that a study be
18 made by the staff relative to a gross income tax for debt
19 payment purposes only? According to my figures, here we
20 have been dealing with half a million here, 1.1 billion,
21 1.2 billion; but if we do as I propose, have a gross income
22 tax of 1 percent, we will raise \$20 billion a year --
23 \$60 billion over the next three years. And if we raise that
24 to 3 percent, which is such a small amount that I don't think
25 anybody will really complain, if we explain that this is for

1 for the purpose of retiring the national debt, we will raise
2 \$180 billion, according to my estimate, in the next three
3 years. And it is so simple. I think the IRS would have no
4 problems in calculating it; it is based on the gross income.

5 We had in Hawaii a four percent gross income tax, so
6 easy to administer, so easy to collect. I don't know whether
7 the staff has made any study on this or whether anyone
8 thought I was serious about it; but if next week we are asked
9 to propose revenue measures, I will propose this, and I
10 would like to have the staff work out the figures on it.

11 Mr. Wetzler. We will be happy to do that, Senator.

12 Senator Matsunaga. Thank you.

13 The Chairman. Well, maybe you can report on that
14 Tuesday?

15 I need to go down and question Mr. Meese.

16 Senator Baucus. Mr. Chairman, I was gone when the
17 minimum tax measure came up -- I had to handle an amendment
18 on the floor, and I didn't know it was going to be coming up;
19 I know Senator Wallop had interest in it, too -- did it apply
20 only to things that were at risk? Is that what I understand?
21 Things that were covered under the at-risk rule would not be
22 covered under it, is that correct?

23 Mr. Wetzler. No. Essentially what we did was take
24 Senator Moynihan's original proposal and added an amendment
25 saying it would not apply to the extent that your losses

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1 equalled your actual investment plus the amount of recourse
2 indebtedness. So essentially it would not apply in cases
3 where you have a real out-of-pocket loss.

4 Senator Baucus. A real loss. Well, I think I agree
5 with that, but I just want to raise the caveat, and I know
6 Senator Wallop did, too, that we might want to reopen it.

7 I just want to look at it carefully. I think that
8 sounds all right, and I apologize, I had to be over there or
9 I would have been here to look at it.

10 The Chairman. Let's make certain we show the draft
11 language to Senator Boren and Senator Wallop.

12 Senator Baucus. Senator Wallop had an interest in it,
13 too, and I think we both want to reserve the right to look at
14 that before the record be deemed that we are recorded in
15 favor of it. We want to look at it. I think it sounds all
16 right, but I do want to see some language.

17 The Chairman. All right. We have tomorrow that we can
18 meet, but we are sort of -- I wouldn't say we're at a dead
19 end, but we are at the end of the list. There are two or
20 three things we are working on that I think will make a lot
21 of people happy, but we don't quite have it worked out.

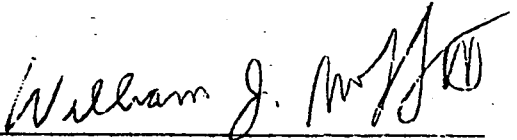
22 It would be a good time for staff to work with members
23 and with Treasury and the Joint Committee, and I assume you
24 are very busy drafting this material, in any event.

25 Thank you very much. Then, at 10:00 Tuesday.

1 (Whereupon, at 4:50 p.m., the mark-up session was
2 recessed, to reconvene Tuesday, March 6th, at 10:00 a.m.)
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C E R T I F I C A T E

1
2 This is to certify that the foregoing proceedings of
3 a mark-up session of the Committee on Finance, held on
4 March 1, 1983, in re: Deficit Reduction Proposals, were
5 held as herein appears and that this is the original
6 transcript thereof.

7
8
9 

10 WILLIAM J. MOFFITT

11
12
13 My Commission expires April 14, 1984.