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OFFICIAL TRANSCRIPT

COMMITTEE ON FINANCE

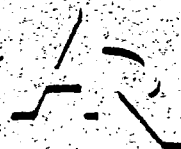
UNITED STATES SENATE

EXECUTIVE SESSION

Monday, August 18, 1980

Washington, D. C.

ALDERSON



REPORTING

400 Virginia Ave., S.W. Washington, D. C. 20024

EXECUTIVE SESSION

MONDAY, AUGUST 18, 1980

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

The committee met, pursuant to notice, at 11:25 a.m., in room 2221 Dirksen Senate Office Building, the Hon. Russell B. Long (chairman of the committee) presiding.

Present: Senator Long, Byrd, Nelson, Bentsen, Matsunaga, Baucus, Dole, Packwood, Roth, Danforth, Chaffee, Heinz, Wallop, Durenberger.

The Chairman. The committee will come to order.

I would think that as the first order business, we ought to let the staff give us the information they have prepared that has to do with the economic situation that exists in the country, and also a little overview of the material that they have prepared for us with regard to the budget.

The reason I suggest this is that the first order of business really ought to be, I think, to decide whether we are going to have a tax cut this year at all. We have heard testimony. Everybody has had a chance to review it. We can see whether we want a tax cut. I know how I am going to

1 vote on that. It will be no surprise to anybody.

2 I think that we will waste a lot of time if we find
3 that maybe people don't want a tax cut. If they don't want
4 one, then, of course, it will not happen. I think that we
5 will probably decide that we do.

6 I would like to let Mr. Shapiro sort of take charge
7 here, and explain the information that he has prepared for
8 us about the situation and the economic aspects of it.

9 Senator Dole. Mr. Chairman.

10 The Chairman. Senator Dole.

11 Senator Dole. We have been meeting, as I assume your
12 side has, this morning trying to find some total agreement
13 on the Republican side, and I think that seven of the eight
14 members attended the session. We have had a similar
15 discussion on what do we do, how much do we do, and when do
16 we do it.

17 I would ask that the statement I have prepared, which
18 recommend that we move quickly, and we act now -- I am not
19 certain that tax cut is a correct word or tax abatement, but
20 at least we are going to reduce the increase in taxes next
21 year by some amount.

22 The Chairman. Let's call it tax restraint.

23 Senator Dole. I have a very good non-partisan
24 statement which I would like to have made a part of the
25 record indicating how bad things have been, and how we can

1 improve upon those things if we act now, and to have the cut
2 take effect next year.

3 Knowing the Democrats' effort to report by September
4 3rd -- Is that a bill, or a report?

5 The Chairman. The Resolution that the Democratic
6 Caucus voted, I think, asks the Finance Committee to try to
7 report by September 3rd its recommendations on the subject
8 of a tax cut. Incidentally, that does not mean that we have
9 to make up our mind about everything.

10 The resolving clause is: "The Senate Finance Committee
11 shall report to the Senate no later than September 3rd a
12 responsible, targeted, anti-inflationary tax cut to take
13 effect in 1981," and so forth. It means to report to the
14 Senate.

15 Senator Dole. That could include Republican ideas,
16 too.

17 The Chairman. I don't see anything about Republicans
18 in here.

19 (Laughter.)

20 The Chairman. So I guess they are not precluded.

21 Senator Dole. I guess our question was, and that is
22 one you have indicated, if in fact we are going to take
23 action, certainly we want to cooperate with the chairman and
24 the majority. If it is only going to be 10 hours of review
25 this week, and we really do not believe that we will have a

1 package to go to the floor, then maybe there are other
2 things that we ought to do.

3 The Chairman. Suppose you go ahead and explain
4 briefly, Mr. Shapiro, the materials you have prepared for us.

5 Mr. Shapiro. Let me say at the outset that the staff
6 thought it would be appropriate to prepare a brief analysis
7 as to the current economic situation because this is a
8 unique situation for the Finance Committee.

9 Traditionally, when the Finance Committee considers a
10 tax bill, you have had before that an Administration
11 proposal in which case there has been an economic analysis
12 prepared by the Administration on the basis of the tax cut.
13 That is, the size of the tax cut in the current year, the
14 future years, and the inclusion of the items in the tax
15 cut.

16 That is based in their proposal that they send to the
17 Congress, which is generally considered in the House first,
18 and when a bill comes to the Senate Finance Committee you
19 have had the basis of the Administration proposal, with
20 their economic analysis which goes into that, and at the
21 same time you have had a House bill, with the Administration
22 testifying at your hearings both on the House bill and with
23 regard to their proposals to modify it.

24 At this particular time, you are beginning a mark-up
25 session, and we thought that it would be appropriate for the

1 committee to look at some of the economic situation which
2 traditionally is done in the Administration, to review the
3 situation which may help you to determine both the size of
4 the tax cut in the current year, in the out-years, and also
5 to determinations as to the portion of it devoted certain
6 individual cuts, productivity cuts. overall effects from the
7 standpoint of economic growth.

8 To very briefly review the situation, we distributed
9 materials which you will have in front of you. It goes
10 first to the current economic situation, which includes
11 recent economic developments, as well as looking at the
12 economy in 1980 and 1981. Also the staff has prepared some
13 background material on the Federal budget to give you some
14 indication as to spending and receipts, both with respect to
15 1980, 1981, and some of the out-years as well.

16 Lastly there is a short one-sheet paper the staff has
17 put out to give the committee some guidance with regard to
18 how they might want to consider a tax cut, and the size of
19 the cut.

20 The page that I am starting with first, and which I am
21 going to briefly summarize, is the one that is headed
22 "Current Economic Situation -- (a) Recent Economic
23 Developments."

24 Let me say that in 1976 to 1978, the economy generally
25 grew at a very rigorous annual rates, and that is somewhat

1 in excess of four percent, which is a very good growth
2 rate. Also, it included all parts of the economy. In 1979,
3 however, economic expansion essentially stopped. Real gross
4 national product -- let me say that the gross national
5 product is the measure of all of the goods and services
6 produced in the United States adjusted for inflation.

7 Most of our economic indication is based off GNP. It
8 was just one percent higher at the end of 1979 than it had
9 been at the end of 1978. So, in other words, productivity
10 and growth had virtually stopped and had slowed down
11 significantly.

12 This affected household spending, especially autos. It
13 affected the automobile industry, the steel industry, and it
14 had it had its effects in the housing market as well. The
15 significant declines, however, were in auto and housing.

16 In the second quarter of 1980, you had what had
17 previously been referred to as a stagnant economy, and
18 started to enter into a very steep decline in all major
19 categories of the private spending and contract. It was
20 more than the auto and housing, although it led the way. It
21 was a general decline in all parts of the economy.

22 Real GNP declines at an annual rate of nine percent,
23 and this took GNP all the way back to levels that existed in
24 the autumn of 1978. So not only were we slowing down, but
25 we had gone backward from the standpoint of real GNP.

1 Two areas that I want to focus on are employment and
2 the rate of inflation.

3 Employment generally follows the rise and fall of the
4 economy. When the economy is going up, the employment tends
5 to go up, and vice versa when the economy starts to go
6 down. In 1976 unemployment was at a rate of about 7.7
7 percent, and it dropped to about 5.8 percent because of
8 expansion in the economy. It remained that way during
9 1979. It, however, returned to a higher level of 7.5
10 percent in the second quarter of 1980, and in July, the last
11 month, unemployment went up to about 7.8 percent.

12 The forecast for unemployment is that it will be
13 somewhere close to eight percent or above at the end of 1980
14 and 1981. So unemployment is at a much higher level because
15 of the stagnation of the economy and the decline that the
16 economy has been in in recent times.

17 The rate of inflation has also grown significantly. In
18 1976 we had an inflation rate of about 4.8 percent, and that
19 went up to 6.8 percent in 1977, and it grew to nine percent
20 in 1978, 13.3 percent in 1979, and as you all know it
21 significantly increased in 1980, going to 18.4 percent in
22 the first quarter of 1980.

23 In the second quarter of 1980 it was 13.7 percent, and
24 we find that the effects are going up in July because of the
25 food prices essentially leading the way, and also because

1 the auto and truck prices -- as you know that is usually a
2 one time increase because of the new models that are coming
3 out, but the inflation rate is at a very high level as of
4 now.

5 If you will turn to the next page, you will see Table
6 1, which kind of shows a table summarizing what I have just
7 indicated. It shows, first, from 1976 through the second
8 quarter in 1980, the GNP in the left column, and then it
9 shows you the percentage change. In 1976 it was 4.9
10 percent, and stayed at those high levels through 1978, and
11 then it backed down to one percent in 1979, and all the way
12 down to minus nine percent in the second quarter of 1980.

13 You see the unemployment rate, 7.7 percent in 1976. It
14 went down to 5.8 percent in 1979, and once again up to 7.5
15 percent and going close to eight percent, which is the
16 projection for the rest of the 1980.

17 The Consumer Price Index is the next column. It shows
18 you that that has gone from 4.8 percent in 1976 to rates in
19 the double digit range, with a high of 18.4 percent in the
20 first quarter of 1980, and it 13.7 percent in the second
21 quarter. This is expected to come down, although I must say
22 that all the forecasts of inflation in recent times have
23 underestimated the increase.

24 It has always been assumed that it would come down, and
25 it has generally been higher as a result of the energy

1 prices, and prices that have affected the food industry and
2 energy in general. So it has not been as good as it has
3 generally been forecast to be.

4 The GNP deflator is another indicator for price, but as
5 you can tell that has also maintained a high level. It is a
6 different way of measuring the price level. GNP tends to be
7 a little bit less because of the way it includes what is in
8 the economy.

9 Going over to the next page, looking at the economy in
10 1980 and 1981, as I said, real GNP is expected to decline
11 overall in 1980 to somewhere between 3.0 and 3.5 percent.
12 The projections now for 1981 -- these are all projections
13 without any tax increase -- are that you would have an
14 increase in GNP of somewhere between 2.5 and 3.5 percent.

15 The unemployment rate is expected to rise in the eight
16 percent, going maybe close to nine percent in 1981.

17 The inflation rate is expect to rise to somewhere
18 between nine and 11 percent in the second half of 1980, and
19 somewhere between nine and 10 percent in 1981. I will say,
20 however, that the inflation rates are somewhat unpredictable
21 because of the food prices, energy, and generally the
22 forecasts for inflation rates have been much lower than has
23 proven to be the case in recent times.

24 From an economic point of view, it seems that we are
25 having a slow recovery from the recession that will take

1 hold in 1981. This is generally because there is a drawing
2 down of inventories that usually happens after the recession
3 starts to come out, so the productivity and economic growth
4 begin somewhat slowly as a result.

5 We see that housing starts and the auto sales are
6 improving, but not significantly that they have taken hold.
7 Those sales are still lagging way behind although they may
8 be up a little, lagging behind what was projected from prior
9 years.

10 The interest rates also are higher. They came down for
11 a while, and they went up just a little bit. Right now it
12 is not clear yet where interest rates may be going for the
13 rest of the year and 1981. There is a hope that interest
14 rates will back down, which will spur housing starts, which
15 will help the auto industry, and the economy in general.
16 However, to the extent that interest rates climb a little,
17 it has an adverse effect from the productivity point of
18 view, and the availability of money that goes along with
19 it.

20 The big unknown, of course, is energy. What is going
21 to happen with price increase of gasoline, which also has an
22 adverse impact with regard to the economy, inflation, and
23 other aspects in that regard.

24 Production of exports is also expected to rise less
25 rapidly, and that has an adverse impact with regard to

1 domestic production and productivity in general.

2 All the projections are based, as of now, without a tax
3 increase. All the models factor different items when you
4 consider a tax increase -- tax reductions. I should point
5 out, however, that beginning in 1981, as you all know, there
6 are significant tax increases that will be taken ahold in
7 the economy.

8 The next page, table 2, sets this out in a table form.
9 This is a calendar year tax liability, meaning that these
10 will take effect beginning January of 1981. The first is a
11 \$15.1 billion inflation. This is the bracket creep,
12 individuals being pushed into higher brackets because of
13 inflation, and this means that there will be \$15.1 billion
14 of increased revenues to the Federal treasury as a result of
15 inflation.

16 The second item is the Social Security. This is a
17 legislated tax increase. As you know, beginning on January
18 1, the rate goes from 6.1 percent to 6.65 percent, and the
19 base goes from \$25,700 to \$29,700. The combination of those
20 two increases would be about \$11.9 billion in Social
21 Security increase.

22 I should note, however, that the individual portion,
23 that is the employee side of it, is approximately \$8
24 billion. Of the \$11.9 billion, approximately \$8 billion is
25 for employees, and almost \$4 billion is the employer's

1 share.

2 The next column is the windfall profits tax that is
3 coupled with decontrol. As phased decontrol pushes prices
4 higher, the windfall profits tax captures a significant
5 portion of that to the Federal treasury, and that accounts
6 for approximately \$11.4 billion of increased revenues to the
7 Treasury as a result of the windfall profits tax.

8 I should also note that the conferees in the Congress
9 agreed that approximately 60 percent of the revenues from
10 the windfall profits tax would be dedicated to individual
11 tax reductions.

12 Senator Packwood. Bob, where in my mind did I get the
13 figure \$18 billion for the windfall profits tax?

14 Mr. Shapiro. This is the increase from 1981 over
15 1980. This is how much money is coming out of the economy
16 in that.

17 Senator Dole. Is that a gross tax figure.

18 Mr. Shapiro. We are talking about the net right now,
19 the net increase to the Federal revenues.

20 Senator Wallop. I thought you said the 1980 figures
21 assume no tax increases.

22 Mr. Shapiro. No tax cuts, we are talking about. No
23 reductions. I think I said the wrong words. In other
24 words, all these projections of what happens in the economy
25 are based on no tax reduction.

1 Senator Wallop. I think that it is important that the
2 public knows that they are having a tax increase.

3 Mr. Shapiro. All of this includes the tax increase
4 because that is projected in the models. But it assumes a
5 stable situation with the tax situation because there is no
6 legislated tax reduction, there is no way of knowing if the
7 Congress would enact it, if it would be signed by the
8 President, or what it would be. So the models in the
9 forecasts that you have before you do not contemplate a tax
10 cut.

11 Senator Wallop. But they do contemplate the increases
12 in taxes.

13 Mr. Shapiro: That is correct. All these increases are
14 contemplated in the economic analysis that has been made by
15 the forecasters.

16 Senator Wallop. Thank you very much.

17 Mr. Shapiro: The next item is the reconciliation
18 package, and although it is approximately \$4.2 billion in
19 both the House and the Senate bills, the effect is
20 approximately \$500 million because what we are doing is
21 speeding up from one fiscal year to the next. It is not
22 really a true tax increase. It is a speeding up process,
23 and the amount of revenues that is actually coming out is
24 approximately \$500 million.

25 Senator Heinz. Before you go into expenditures, what

1 does CBO calculate as the increase revenues from Fiscal '80
2 to '81?

3 Mr. Shapiro. We have those listed for you.

4 You are talking just about the Social Security, or
5 inflation?

6 Senator Heinz. Total. As I recollect, their revenues
7 were \$604, is that right?

8 Mr. Shapiro. If you go a couple of pages later than
9 what we call Table 1 -- all this was stapled together. We
10 presented it separately when it was first done. The page
11 that is headed Table 1, Federal Spending, these are figures
12 by CBO. You see that is projected in 1979, 1980, and 1981,
13 and down at the bottom of that chart you will see the
14 receipts for 1979 are \$463.9 billion. Then you see receipts
15 for 1980 as approximately \$517 billion.

16 Senator Heinz. The difference between \$601 billion in
17 1981 and \$517 billion in 1980 is roughly \$84 billion. Yet,
18 the number you have here is \$36.6 billion on the first table
19 2.

20 Mr. Shapiro. Yes. Let me let Jim give you all the
21 details. Jim worked with CBO.

22 Senator Heinz. It seems to me that there is a big
23 difference between \$84 billion and \$36 billion.

24 Mr. Wetzler. Senator Heinz, what happens is, you need
25 some growth in revenues to just keep up with inflation. For

1 example, if there is a 10 percent inflation, income tax
2 revenues go up by about 16 to 16.5 percent. What is shown
3 in the early table about the inflation increase is the 6.5
4 percent, the extent to which the income tax has grown over
5 and above inflation.

6 If all prices go up 10 percent, you need your tax
7 receipts to go up 10 percent just to keep up and pay for the
8 higher cost of government. The real tax increase is that
9 extra 6.5 percent that results from that.

10 Senator Heinz. Don't you think that it would be nice
11 to label it that way?

12 My suggestion is that we ought to have two columns
13 here. One that is the actual figures, and then if you want
14 to do some kind of arithmetic on the columns, which is what
15 we have got, calendar year tax liability, which is not
16 footnoted and does not describe all that, then do so by all
17 means.

18 We have been going through Table 2, the first page, and
19 it is being put forward that we are only going to have a \$36
20 billion tax increase next year, and it is going to be an
21 \$84 billion tax increase.

22 Mr. Shapiro. Traditionally, when the staff presents
23 materials, this has been the way that materials have
24 generally been presented. But you may be correct that
25 perhaps we should have a column to show you both forms of

1 it.

2 Mr. Wetzler. Senator Heinz, in the handout on the
3 individual income and payroll tax deductions, we go into the
4 detail you want.

5 Senator Heinz. I am sure.

6 Mr. Wetzler. It is in the other handout, if you want
7 to turn to that.

8 Senator Heinz. The press did not get the other
9 handout, did they?

10 Mr. Shapiro. Everything has been distributed to the
11 press.

12 Senator Heinz. Thank you.

13 Mr. Shapiro. The last item on that first Table 2 deals
14 with the fact that the Congress has already legislated a tax
15 reduction for next year, and that is the interest and
16 dividend exclusion that takes effect in January of 1981.
17 You are talking about money that goes back into the economy
18 that first begins in January, which is \$2.3 billion as a
19 result of that provision in the windfall profits tax bill.
20 This shows that additional revenues coming out of consumers
21 to the Federal treasury is approximately \$36.6 billion.

22 Senator Dole. Let me ask a question along the same
23 lines as Senator Heinz's. As I understand the \$15.1 billion
24 figure, you used the GNP deflator. Is this a departure from
25 prior practice? If you used the CPI figure, you would have

1 over \$20 billion rather than \$15 billion.

2 Mr. Shapiro. Senator Dole, what causes tax to go up is
3 the income received by U.S. taxpayers because of inflation.
4 That sort of inflation is best measured by the GNP
5 deflator. In the past there had not been too much
6 difference between the GNP inflator and the CPI, and we did
7 not give the matter very much thought.

8 Senator Dole. This makes it look better from the
9 standpoint of increased taxes.

10 Mr. Shapiro. But to the extent that the CPI goes up,
11 for example, because of imported oil prices and the foreign
12 exporting countries get more money, we don't collect any
13 additional income tax from Saudi Arabia, for example, even
14 though price increase is in the CPI.

15 The GNP deflator is the price index of prices of goods
16 produced by American, which is basically the tax base. So I
17 think for this particular purpose, there is a good argument
18 for using the GNP.

19 Senator Dole. The CPI isn't that the figure that wage
20 increases are geared to?

21 Mr. Shapiro. Yes. As those wage increases occur, they
22 will get reflected in the GNP deflator.

23 Senator Dole. On the payroll taxes, you estimated
24 \$11.9 billion in calendar year 1981. However, as I
25 understand it, the total increase in payroll taxes will be

1 about \$25 billion in calendar year 1981, and not this amount
2 of about \$15.4 billion that comes from the 1977 changes to
3 payroll rates or tax base.

4 I assume that there were some offsets there to lower
5 that figure, and maybe that will be furnished in the later
6 information that Senator Heinz asked for.

7 Mr. Shapiro. You are reading from the materials that
8 we passed out with regard to the individual. In other words,
9 it is always difficult to know where to start and how to
10 start.

11 The first materials that we are discussing is the
12 economic situation which kind of lets you see -- We tried to
13 do it very briefly because we could load you down with 30 or
14 40 pages that just go on and on. We tried to summarize as
15 to what the economic effects, from the standpoint of the
16 Federal treasury and taxpayers, are, which is the
17 information you are reading right now gives, instead of the
18 overall economic effects to individuals specifically.

19 On the first page of our handout with individual income
20 tax reductions, it shows that the gross increase of the
21 Social Security is \$22.1 billion, and \$15.4 billion of that
22 is the increase in the rate and the base, and \$6.7 billion
23 results from the expected increase in the wage portion of
24 that base.

25 In other words, we have separated that so that all the

1 material that you have is what the staff has provided,
2 except that we try to allocate it depending on the different
3 discussions in presenting the material.

4 We tried to provide everything to you, and it is
5 difficult to try to allocate it in the best way you can
6 receive it. So we will try to keep on bringing it back to
7 try to help you with it.

8 The budget situation, this is in the next material that
9 is headed (c) Background Material. If you will just go to
10 that table, Table 1, I will try to summarize the situation.
11 The point that we are making here is that spending has grown
12 significantly in 1980. It grew at an overall rate of 17.5
13 percent. If you will look in the middle of the page, where
14 it says, 1980 Percent Growth, you will see that total
15 outlays grew at 17.5 percent.

16 The real growth, that is the growth above inflation,
17 was 7.8 percent. So you really had a very significant
18 increase in spending in 1980 over 1979. Of that increase of
19 7.8 percent, 90 percent of the increase in spending was in
20 four categories:

21 The first one is defense, and that is 6.4 percent; the
22 second one is health, and that is 6.1 percent and it is in
23 the middle of the page there; right below that is income
24 security, which is 10.7 percent; and then the interest
25 expense at the bottom of the page, which is 12.1 percent.

1 Those four categories, defense, health, income
2 security, and interest, accounted for 90 percent of the
3 increased spending of real growth of 1980 over 1979.

4 The Chairman. What was that?

5 Mr. Shapiro: It was 7.8 percent. That is the real
6 growth in spending. As you will note from 1980, it is
7 expected that the budget deficit will be approximately \$63.3
8 billion. These are CBO figures.

9 If you go to 1981, the same four categories will have
10 an increase in spending, but not at the same rate as 1980.
11 It is projected that the increase -- the real growth will be
12 approximately a negative. In other words, a minus two-tenth
13 of one percent.

14 Since defense spending will go up, and also health and
15 income security will go up, the effect of that, as you can
16 see from all the minuses, is that real growth will decline
17 in almost all the other areas. That something that the
18 Congress has to work out in the budgetary prospect for next
19 year.

20 Assuming that defense goes up, and the other categories
21 go up to a certain extent, and you do you have a decline of
22 two-tents of one percent in real growth, there is still
23 forecast a budgetary deficit of \$30.4 billion in the budget
24 for 1981. Once again, these are all assuming no tax cut.

25 Going to Table 2, which is a couple of pages later, the

1 purpose of this table is to project forward the size of the
2 tax cut into the future years and the budgetary situation.
3 The staff has tried to give you several options to project.

4 Once again let me make an observation. As you know,
5 when we focused on the windfall profits tax, the staff made
6 the statement that the revenue projections that the computer
7 programs for the 11-year period to 1990 can be plus or minus
8 \$100 billion, when you look that far in advance.

9 These are CBO and Administration figures. The first
10 page is CBO, and the next chart is the Administration. Once
11 again, if you are programming out to 1985 using forecasts
12 these can be off. I don't want to say plus or minus \$100
13 billion, but they can be off significantly because of the
14 economic circumstances, the energy prices, food, and so
15 forth.

16 But these are the projections that the CBO and the
17 Administration are making looking down the road as to what
18 slack would be in the budget without any unusual increase in
19 spending, or any tax cut, to give you an indication as to
20 what size a tax cut you can program for the future and
21 out-years.

22 There are three policies that we have, and that is what
23 we call: a high option, a current policy, and a low
24 option.

25 The high option includes additional defense spending,

1 catastrophic health insurance, welfare reform, plus current
2 policy revenues. That is the high option. That would be a
3 higher spending program.

4 The next one is called the current policy, and it is
5 the policy that is actually implied by the first budget
6 resolution. The staff has made certain discretionary
7 inflationary increases to project it out, to give a fair
8 base of comparison, but that is essentially the first budget
9 resolution policies.

10 The last option is what we refer to as a high option.
11 This includes a reconciliation and a housing bond tax
12 increase, no welfare reform, catastrophic health insurance
13 or additional additional defense spending.

14 This is to give you a range of what the budgetary
15 situation may include. If you look at the 1985 column,
16 which is the last column, you will find that the current
17 policy would show that you would have approximately \$129.9
18 billion. That amount would be available either for tax
19 reductions in the out years, or for additional spending, or
20 other programs.

21 If you will look at the very next page, you will find
22 that the Administration is much more pessimistic than the
23 CBO. Where you see the 1985 projection from CBO, you see
24 \$76.7 billion, and that is a significant difference. The
25 reason for that difference, essentially, is the reduced

1 revenues.

2 In other words, the Administration does not anticipate
3 that we will collect as much revenues by 1985 as CBO does,
4 and that is essentially the difference.

5 So what you are looking at from a budgetary point of
6 view is a situation where it appears unlikely to balance the
7 budget in either 1982, marginally in 1983, given no tax cut,
8 but when you get out to 1985 you have a slack of somewhere
9 in the neighborhood of \$76 billion using the Administration
10 figures, and somewhere close to \$130 billion using the CBO
11 figures.

12 There is hope, of course, that in the tax cut that you
13 decide upon, that you will have enough productivity that you
14 will have the longer range benefits. As we all know, the
15 individual cut is giving individuals back what has been
16 taken out of their increases, but the productivity cut is the
17 one that you hope will add growth to the economy.

18 I should add, however, whenever you have productivity
19 and business cuts, they start slow, meaning that you don't
20 have a return very quickly. It takes time to generate
21 through the economy, and it picks up in later years.

22 Senator Heinz. I have some numbers that are supposed
23 to be CBO numbers that show somewhat lower numbers than you
24 have got on Table 2 for Federal spending projections of
25 current law. For 1982, CBO projects \$683 billion; for 1983,

1 \$729 billion; for 1984, \$772 billion; and for 1985, \$820
2 billion. Why the variance?

3 Mr. Shapiro. The reason for that -- and once again it
4 is a little bit of an arbitrary adjustment in all these
5 cases -- they have not adjusted their programs for inflation
6 in the out-years. We have added an inflationary adjustment
7 for the out-years just to give you some feel. In some
8 programs they have, and in others they have not. We have
9 tried to make an adjustment across the board for the
10 inflationary increases.

11 Senator Dole. They are big differences, though. I
12 have the same figures.

13 Senator Heinz. It is a large difference.

14 Senator Dole. It is \$127 billion.

15 Mr. Shapiro. I will say that CBO has looked at all
16 these tables. I don't want to give the impression they have
17 have endorsed them and this is it because they have their
18 own, but they understand what we are doing, and they
19 understand the concept of why we are doing it. But all of
20 these figures have been dicussed by CBO and the Senate
21 Budget Committee. They have been sent to the Joint Economic
22 Committee. We have tried to get everyone who is involved in
23 budgetary estimates and analyses to have a feel for the type
24 of information we are presenting.

25 Let me say again, as I said earlier, we are guessing in

1 the out-years. We are using the best projections that
2 either the Administration and CBO have as of now to give you
3 some projection. It is very difficult to look that far down
4 the road with such changes, and what can happen to the
5 economy, and know exactly what the situation will be.

6 Mr. Wetzler. Senator Heinz, the lower numbers include
7 inflation where inflation is in the law right now. They do
8 not include discretionary inflation adjustments. They just
9 include mandatory inflationary adjustments. This is what we
10 are committed to.

11 Senator Heinz. The staff numbers, Bob, included, for
12 example, that in the housing and community development
13 program you would have a full inflation adjustment in
14 there.

15 Mr. Shapiro. That is correct.

16 Senator Heinz. For surface transportation, which was
17 cut this year, you would have a full inflation adjustment,
18 and so on.

19 Mr. Shapiro. That is right. We are adjusting for
20 revenues, and we felt that it should also adjust for some of
21 the spending to put them on somewhat the same basis.

22 Senator Heinz. Now I know what you are doing. Thank
23 you.

24 Mr. Shapiro. This completes what the staff has with
25 regard to the information to give you an indication as to

1 the economic situation, the budgetary situation. I think it
2 is clear that everyone agrees that we need a tax cut to try
3 to put back into the economy what has been taken out. The
4 question is when, and the size.

5 I think that there is a general agreement that from a
6 productivity standpoint, we need to have more capital
7 formation, more productivity, and more growth, which is
8 recognized, no matter what you do now, is going to start
9 slow because it takes several years for the productivity to
10 be fed back into the economy.

11 The last piece of paper that we have distributed to you
12 for analysis is the size of the tax cut, to determine what
13 is necessary. You always have the differences of views of
14 economists as to whether or not a tax cut either fights
15 inflation or has an adverse effect on inflation, and whether
16 it fights employment. Different economists will take
17 different views, which is what we have spelled out in that
18 sheet that is headed, "Size of the Tax Cut."

19 I think what this committee wants to do is to fashion
20 the tax cut as a minimum adverse on inflation, and at the
21 same time maximizing the productivity growth in the
22 direction of locking down the road from the growth out of
23 the recessionary situation. Looking, also, at the
24 short-term effects, and the long-term effects.

25 If you are looking at the short-term, a tax cut

1 somewhere in the range of \$25 to \$30 billion, this may be a
2 target that the committee wants to start with for 1981. You
3 must have some type of a target, and you can easily go below
4 it or above it, but you shoot for that type of projection.
5 In the out-years, you may be looking down at five years from
6 now, and you may want to consider somewhere in the
7 neighborhood of \$60 to \$70 billion from the standpoint of
8 your overall program.

9 If you go too much this year, that means you will use
10 all the room, as you can see it today, as to what would be
11 available for any future tax decreases in years between now
12 and 1985. We cannot, of course, clearly and fully
13 anticipate the effect to the economy, or the feedback in
14 this regard, and our revenue effects have a minimum amount
15 of effect for the out-years, and it gives you some slack.

16 So what we are suggesting is that you may want to look
17 at a tax cut that is somewhere in the range of \$25 to \$30
18 billion in the first fiscal year as a starting point. Once
19 you start working on your package, you may revise that
20 either upward or downward, but it gives you somewhat of a
21 target. Once again, in the out-years, somewhere in the
22 neighborhood of \$60 to \$70 billion as something to focus
23 from as of now. Clearly, as you continue along in the week,
24 you can modify it however you think it would be
25 appropriate.

1 The Chairman. Let me put this question. I would hope
2 that this would sort of a first decision we would make.
3 Many times, when someone brings up a very significant
4 amendment that is subject to all sorts of suggestions. I
5 often ask, "Let me ask you, Senators, do you think that we
6 ought to do anything about this?" Then we have a vote or a
7 show of hands on how many think that we ought to do
8 anything.

9 I would like to suggest, as a starting point, that we
10 just decide as the first order of business, do we think we
11 ought to have this tax cut. Basically, do we think that we
12 ought to try to vote a tax cut before January 1.

13 I think I know the answer to the question, but I
14 sometimes get the impression, or at least the people in the
15 media are hearing from some sources that we don't really
16 mean it, or that maybe we have lost interest in it, and
17 perhaps it is only the chairman who is still carrying the
18 flag for a tax cut.

19 I would just like to submit the question to this
20 committee, and let the committee decide. Do we want to
21 recommend to the Senate a tax cut in the order of magnitude
22 that Mr. Shapiro has suggested here.

23 I know that anybody who votes for something like that
24 reserves the right to vote against it when we report on the
25 basis that he might not like it. He might feel that it

1 ought to be a little more in line with his own personal
2 views. But I think that we can decide whether we really
3 want to have a tax cut of that dimension.

4 Senator Nelson, did you want to say something?

5 Senator Nelson. Are we going to ask for a show of
6 hands or that question?

7 The Chairman. I think that we might have a vote
8 because there are some who are not here, and we will have
9 the absentees record themselves.

10 Senator Nelson. You stated it satisfactorily for me
11 when you added the proviso, provided that the committee
12 comes up with one that I can support.

13 The Chairman. Basically, if we write it your way,
14 would you be for it?

15 Senator Nelson. Yes.

16 (Laughter.)

17 Senator Nelson. At least for one day.

18 I wanted to be recognized to make a different motion
19 after you finished with this one.

20 Senator Bentsen. Mr. Chairman, I believe that as a
21 matter of economics, the facts overwhelmingly call for a tax
22 cut. It is a matter of politics, and maybe it is something
23 else again, but every public opinion poll says that the
24 public does not want a tax cut if it adds to inflation. It
25 is terribly important that this one be structured not to do

1 that.

2 We see the revised estimates to the mid-year report
3 showing that the increase in tax revenues will be \$86
4 billion, with State and local taxes it is another \$30
5 billion. It is a total of \$115 billion in increased taxes
6 that we are facing in 1981. So if we talk about a \$25 to
7 \$30 billion tax cut, and properly structure it, in no way
8 will that be inflationary. But that must be understood by
9 the financial community, otherwise you are going to find
10 problems in the financial market, and you will see interest
11 rates going up. But properly interpreted and properly
12 structured, that will not be the case.

13 I believe very strongly that we ought to pass one
14 effective on January 1, and that if we don't pass it this
15 fall that we will find that we have to have committee
16 assignments, we will have to have a parade of witnesses
17 again, and you are not going to have a tax bill that will be
18 effective before March, April, May, June or July, and it
19 ought to be going into effect the first of the year.

20 So I support it.

21 The Chairman. Does someone want to speak over here, I
22 thought I saw a hand raised.

23 Senator Packwood. Mr. Chairman, as much faith as I
24 have in this committee, and by and large in the Congress, I
25 cannot conceive, by the time a tax cut gets to the floor and

1 through it, if it goes that far, that it is going to be a
2 non-inflationary tax cut. I would prefer that we not start
3 down the road at all, and that we start next January.

4 Senator Baucus. Mr. Chairman, I wonder if the staff
5 has any range or projection as to how inflationary a \$30
6 billion would be in strict economic terms.

7 Mr. Shapiro. I don't think we have a statement that we
8 can have a projection as to whether or not it is or it
9 isn't. You have so many other effects, such as food prices
10 and energy, and how that affects inflation.

11 I think the feeling is that if it is a well structured
12 tax cut, putting the money back with the people who have
13 been adversely affected from the standpoint of increased
14 inflation and Social Security, it could have a minimum
15 effect on inflation.

16 If you have a much larger tax cut that is much more
17 structured in a way that does not just give it back in
18 Social Security or inflationary increases, and is more than
19 just a modest type of an individual cut, it may be
20 inflationary.

21 Senator Baucus. That is the way I phrased the question
22 the way I did. This is obviously a range because the effect
23 of inflation depends upon the structure of the cut. If it
24 is geared toward productivity, I assume that it is less
25 inflationary, and if it is not, it more inflationary. I was

1 just wondering if your staff, or any other organization had
2 picked up any estimates as to the range of the possible
3 inflationary effects of a \$30 billion tax cut.

4 Mr. Shapiro. Let me let Jim respond more to the
5 economic analysis because he has spent more time on it. It
6 is a very difficult thing to make an assessment of.

7 Mr. Wetzler. There are basically two schools of
8 thought on that question. I will just state the arguments
9 and let you decide because nobody really knows.

10 One group, basically the people who do this econometric
11 forecasting who you saw testify, Otto Eckstein and Professor
12 Klein from the Wharton School, they have models which
13 basically show the inflation process as an on-going
14 wage/price spiral. It is not very much affected by what we
15 do.

16 As long as there is a lot of slack in the economy, a
17 lot of unemployment, a lot of excess capacity, a modest size
18 tax cut like this will generally increase production, and
19 employment, rather than increase prices. That is one view
20 that suggests that the tax cut would not be very
21 inflationary, and well structured could even conceivably
22 reduce the price level.

23 Another group, which I think you heard from in terms of
24 Arthur Burns, Chairman Volcker of the Federal Reserve, and
25 some people who are more oriented towards the financial

1 market, they are concerned about the effect any tax cut, or
2 any stimulus to the economy would have on inflationary
3 expectations.

4 They take the view that the wage and price process is
5 determined, to a large extent, by what people think
6 inflation is going to be. The reason everybody is raising
7 their prices is because people think everybody else is going
8 to be raising is going to be raising his prices. Therefore,
9 they don't show very much restraint themselves. In that
10 environment, there is a fear that if you do cut taxes, it
11 will excite people's inflationary expectations, and make the
12 inflation worse.

13 I personally don't know which of these two views is
14 correct, but both have partisans arguing for them, and the
15 only way you are going to find out is to go ahead and do it,
16 and see.

17 Senator Roth. Mr. Chairman, I think that it is
18 important to recognize the situation in which we find
19 ourselves. We are talking about a so-called tax cut. In
20 fact, we have a very substantial tax increase going into
21 effect if Congress does not act. So that it is misleading
22 to talk about the \$25 to \$30 billion being a tax cut, when
23 in fact revenues are going up roughly as much as \$86
24 billion.

25 I think that it is important that we keep in mind that

1 what we are trying to do here is not only restructure the
2 economy short-range, but we are also trying to do something
3 long-range.

4 What we are trying to attack is the problem of
5 productivity. There are quick cures. A tax cut is not
6 going to create any miracles. But the fact is that we have
7 to take that beginning step somewhere, sometime, and it
8 seems to me that the appropriate time is right now.

9 I just point out that many people, from liberal to
10 conservative economists, from Walter Heller, who has said
11 that one of the worst notions of the time is that a tax cut
12 is necessarily inflationary. He argues very strongly for
13 tax cuts now. I also point out that Alan Greenspan and
14 others on the conservative side have taken exactly the same
15 position.

16 So what I would hope we would do is to take the
17 beginning steps now to give some real tax relief to prevent
18 these very, very substantial tax increases from going into
19 effect. \$25 to \$30 billion is not going to make the average
20 American family whole.

21 I think the typical family of four, who earns something
22 like \$20,000, is going to be paying an additional \$600 in
23 taxes next year because of Social Security increases,
24 inflationary income tax increases, plus the windfall profits
25 tax. So that is a very substantial tax increase.

1 So unless we do something along the lines of what you
2 are suggesting, Mr. Chairman, all we are going to do is make
3 people whole. I don't think that we want to mislead the
4 public back home that they are going to get any substantial
5 tax decrease. What we are saying is that we are going to
6 prevent from taking effect what already is in place.

7 I would hope that as we approach this problem that we
8 would try to do something about productivity that would have
9 some long-term gains. I agree with what Lloyd Bentsen said,
10 there is great advantage in doing it right now because we
11 want the private sector to count on this, and know what
12 steps can be taken to improve their economic picture.

13 The Chairman. Senator Nelson.

14 Senator Nelson. Mr. Chairman, I would guess that there
15 is pretty general agreement with what Senator Bentsen and
16 Senator Roth said respecting the productivity side. We
17 might be well off just to pass that, although it is probably
18 not realistic.

19 I certainly support that, and I think that we have to
20 do something about accelerated depreciation, and faster you
21 are accelerate it, as far as I am concerned, the better
22 because I don't think in the long-pull it makes any
23 difference except that it allows business to replace their
24 productive equipment more quickly.

25 When you get over to the individual tax cut side, that

1 is where the argument starts. I don't pretend to be
2 qualified to make a judgment at what stage some tax cut for
3 individuals becomes inflationary, and at what stage it is
4 not inflationary. I don't guess that the economists all
5 agree on that either.

6 As Chairman of the Social Security Subcommittee, I have
7 had to look hard at those numbers over a long period of
8 time. We are all concerned about how rapidly Social
9 Security has gone up. I do believe that when we do what is
10 the appropriate thing some day and remove Medicare from
11 Social Security, we will be in a much sounder position.

12 It is non-wage related. It should not be there in the
13 first place. There is no other non-wage related provision
14 in Social Security, if you took it out, you would have \$24
15 billion more in the Social Security System, which is what
16 Medicare is costing.

17 I did make that motion in 1977, and it lost on one
18 vote. That is, I made the motion that we start to transfer
19 the cost of Medicare out of the Social Security System,
20 replacing it with general funds, which at some stage I am
21 assuming we will do in some kind of a health insurance
22 program somewhere down the line. That has not happened.

23 If there is going to be a tax cut that affects both
24 individuals and the productivity side, I would like to see
25 that we address the question of at least offsetting, however

1 we do it, the increase in Social Security, which amounts to
2 \$11.6 billion, I believe, in January.

3 So I would like to move at the appropriate time, maybe
4 now, that we ask for the staff to come up with suggestions
5 on a tax that would offset the increase in the Social
6 Security, and do it in a proportional fashion because you do
7 have people in the low-income side who, if you add a 10
8 percent across the board tax cut, would get nothing from it,
9 but they would get the Social Security increase.

10 I know the staff has looked at some of these problems.
11 But I would like, at the appropriate time, to have that
12 motion before us insofar as the individual tax cut is
13 concerned. I think that it is going to be the toughest one
14 to settle.

15 If we are going to agree on a package, I think we can
16 agree, probably, much more easily on a productivity tax cut,
17 all you have to do is figure out how many dollars are you
18 willing to put into it for a period of time, and then work
19 out the formula. But I would make the motion that we reduce
20 individual tax sufficient to offset the Social Security
21 increase, addressing the point of being sure that it is
22 proportional and equitable to those in the lower income
23 bracket who might otherwise not benefit at all.

24 The Chairman. Let me ask the Senator to withhold that
25 motion until we can dispose of this first thing. At that

1 point, he can renew his motion.

2 Senator Matsunaga. Mr. Chairman, I think in addition
3 to an offset for Social Security, we need to have an offset
4 for inflation. As shown in Table 2, the tax increases in
5 1981 --

6 The motion, at least, ought to include a reduction of
7 \$15.1 billion as estimated for inflation because in my trips
8 back home one of the biggest problems, I am sure other
9 senators have come across the same complaint, especially
10 among the low income employees, you find that where they
11 have not had a sufficient wage increase to make up for
12 inflation, they are still paying taxes in the higher income
13 bracket because of the wage increase, which seems to be
14 setting them backwards in their take-home pay.

15 We have got to take care of these people because
16 supposed by this tax reduction we put more money in the
17 hands of the public, the worker, so that they can somehow
18 stimulate the economy. But the way it is now, even with a
19 tax reduction, unless we take care of what they will lose by
20 way of inflation because of being pushed up in a higher
21 bracket, we are not going to place any additional spending
22 money in the hands of taxpayers.

23 So I would hope that Senator Nelson will agree to an
24 amendment which would take care of inflation by way of a
25 reduction in income tax perhaps by way of readjusting the

1 rates at the different levels plus sufficient cuts to take
2 care of the Social Security increase for the employees and
3 to take care of the employers with productivity incentives.

4 Senator Nelson. I don't know what I would support in
5 that respect.

6 The reason I did this is that I think you can clearly
7 separate out the question of what is the bracket increase
8 cost, what is the Social Security increased cost to the
9 taxpayer, and perhaps we ought to address one at a time. I
10 was not making any argument one way or the other.

11 The Chairman. Each Senator is going to get a chance to
12 make these suggestions at the time we decide the first
13 point.

14 Senator Danforth. Mr. Chairman.

15 The Chairman. Yes, Senator Danforth.

16 Senator Danforth. What I would not like, Mr. Chairman,
17 is for us to start making all the individual decisions, and
18 then we end up totally consuming the amount that we decide
19 initially to be the appropriate size of the tax cut. If we
20 were to take an initial vote and determine that the total
21 amount of the tax cut for 1981 should be, say, \$25 to \$30
22 billion, as the Joint Committee Staff proposes, and then we
23 immediately began with Senator Nelson's proposal of \$11.9
24 billion, and then we moved to Senator Matsunaga's proposal
25 on bracket creep of \$15.1 billion, we are up to \$37 billion,

1 almost all of which is individual tax cuts of one sort or
2 another, and none of which has any effect on productivity or
3 industrial modernization, or becoming more competitive
4 abroad.

5 If we are making suggestions as to how we proceed, it
6 would be my thought that we would proceed, first of all,
7 with a determination as to the total amount amount of the
8 cut; and, secondly, a determination of approximately how
9 much of that is to go to business and how much is to go to
10 individuals. Then we can refine it from there.

11 Just because each one of these items is terribly
12 popular, I would hate to have us suddenly spend the \$30
13 billion tax cuts on matters which sound very, very good, but
14 which have nothing to do with the underlying problem, which
15 is the same one that Senator Bentsen pointed out.

16 The Chairman. Again, these are all matters that are
17 important, but these are matters that we will have to decide
18 after we decide, do we think we ought to have a tax cut.

19 Before we take a vote on that, I guess we had better
20 hear from Mr. Lubick over there. So far Treasury has taken
21 the view that they didn't think we ought to vote before the
22 election, and I am not sure that Treasury wants us to vote
23 after the election.

24 What is the Treasury position, Mr. Lubick? What is the
25 latest position, since the convention?

1 (Laughter.)

2 Mr. Lubick. Mr. Chairman, our position is unchanged
3 from that stated by Secretary Miller. We believe that it
4 would be prudent to wait to make sure that we get the
5 restraints on spending that have been started through the
6 reconciliation process, and that we scrutinize the economic
7 situation, and that we proceed to consider the situation at
8 a later time.

9 The Chairman. Shall we vote? Basically, I am just
10 asking for a vote because I want the absentees to record
11 themselves.

12 Senator Matsunaga. What year, Mr. Chairman, this year
13 or beginning January 1981?

14 The Chairman. Basically, that is what I want the
15 Senators to answer, or at least this committee. Do we think
16 we ought to have a tax cut in about the dimensions that Mr.
17 Shapiro has indicated, and do we think that we ought to vote
18 it before January 1, in this session of the Congress.

19 I think, basically, if the question is answered in the
20 negative, then I think we are wasting our time trying to go
21 any further.

22 Senator Matsunaga. But effective January 1.

23 The Chairman. Yes, effective January 1, 1981.

24 The Clerk. Mr. Talmadge.

25 (No response.)

1 The Clerk. Mr. Ribicoff.
2 (No response.)
3 The Clerk. Mr. Byrd.
4 Senator Byrd. Aye.
5 The Clerk. Mr. Nelson.
6 Senator Nelson. Aye.
7 The Clerk. Mr. Gravel
8 (No response.)
9 The Clerk. Mr. Bentsen.
10 Senator Bentsen. Aye.
11 The Clerk. Mr. Matsunaga.
12 Senator Matsunaga. Aye.
13 The Clerk. Mr. Moynihan.
14 (No answer.)
15 The Clerk. Mr. Baucus.
16 Senator Baucus. Aye.
17 The Clerk. Mr. Eoren.
18 (No response.)
19 The Clerk. Mr. Bradley.
20 (No response.)
21 The Clerk. Mr. Dole.
22 Senator Dole. Aye.
23 The Clerk. Mr. Packwood.
24 (No response.)
25 The Clerk. Mr. Roth.

1 Senator Roth. Aye.

2 The Clerk. Mr. Danforth.

3 Senator Danforth. Aye.

4 The Clerk. Mr. Chafee.

5 Senator Chafee. Aye.

6 The Clerk. Mr. Heinz.

7 (No response.)

8 The Clerk. Mr. Wallop.

9 (No response.)

10 The Clerk. Mr. Durenberger.

11 (No response.)

12 The Clerk. Mr. Chairman.

13 The Chairman. Aye.

14 The vote is 11 ayes and no nays, but Mr. Packwood said

15 that he was going to vote no.

16 Senator Danforth. Mr. Chairman, could I be recognized

17 for another motion.

18 The Chairman. Yes.

19 Senator Danforth. Mr. Chairman, so that we can plan in

20 some orderly fashion what we are going to do, I would move

21 that at least 50 percent of the tax cut be targeted toward

22 increasing savings, investment, research and development,

23 and productivity.

24 Senator Nelson. Do you have to have a specific for

25 each, or just in that general category.

1 Senator Danforth. No, just in that general area.

2 Senator Matsunaga. Projected over how many years?

3 There would be extreme difficulty because when it comes to
4 investment credits, for example, the first two years they
5 may have nothing. It depends on the likelihood of planning
6 the next year or two years. So if you plan for five years,
7 yes.

8 Senator Danforth. All right, let's make it for five
9 years, then, in working out the aggregate amount of alleged
10 revenue loss. Then at least 50 percent would be for capital
11 formation, savings, research and development, and
12 productivity.

13 The Chairman. I would hope that we would put some
14 pieces together on a tentative basis and see what they look
15 like before we cross that bridge. The reason I am thinking
16 that way is that the item which has been discussed a great
17 deal about depreciation, the so-called 10-5-3 proposal,
18 starts out costing a small amount of money and about six
19 years out it costs a great deal. That 10-5-3 proposal
20 reaches up to \$58 billion after a few years. How far is it
21 before it reaches that figure.

22 Mr. Shapiro. In approximate magnitudes, in the first
23 year it maybe somewhere close to a couple of billion, and in
24 five or six years down the road it can be \$50 billion-plus.

25 The Chairman. I saw a figure of about \$58 billion. It

1 looked to me like it was \$58 billion in a period of six
2 years.

3 Senator Bentsen. Mr. Chairman, could I comment on that?

4 The Chairman. Yes.

5 Senator Bentsen. I am very sympathetic to what Senator
6 Danforth is talking about, and I am trying to somehow
7 achieve that objective. But I am concerned about the out
8 years, and how they apply.

9 I have one that is shown in here. It is a simplified
10 class depreciation, and that starts off with a cost of a
11 little over \$6 billion, but by the time you get out to 1985
12 it is up around \$17 billion.

13 I am just not sure how we would come out in this kind
14 of a limitation, even though I supported that kind of an
15 amendment to the budget resolution. I laud the objective,
16 but I am worried about how we accomplish it.

17 Senator Danforth. Mr. Chairman, one way we might
18 accomplish it would be to address the business cuts first.
19 Procedurally to run through them first just to make sure
20 that they are not lost at the end.

21 The Chairman. Senator, I have a lot of sympathy for
22 what you are suggesting here. It may very well be that we
23 can do just exactly what you are suggesting. But I, for
24 one, would like to see us act in an area that is going to
25 benefit the rank and file, the great majority of individual

1 taxpayers, even though if you look at what the committee
2 prepared there and what the staff prepared, they put the
3 capital formation right as the first order of business, and
4 individual tax cuts second.

5 My inclination was to say, I would like for us to at
6 least indicate that we are going to do some of the things
7 that the individuals are going to be most concerned about
8 first, because otherwise it tends to set the stage for the
9 word going out that: "We came in here, and the Finance
10 Committee took care of the business," and some will say,
11 "the wealthy first." Then when we got through taking care
12 of them, we proceeded to vote something for individuals.

13 I would hope that we can move to put together a revenue
14 bill that doesn't squeeze out any of them. In the end, I
15 don't care how we do this, we are all going to wind up with
16 a squeezing down process.

17 Anytime we have a big tax cut bill in these dimensions,
18 regardless of how conservative and fiscally responsible we
19 were in this committee, there has been a tendency for the
20 Senate to add more on top of it for us, and we have had to
21 go to conference, and try to get it down to something which
22 we thought was responsible. So, in the final version, the
23 squeezing of the genie inside the bottle came in
24 conference.

25 I join you in wanting to do business in such a way. We

1 don't squeeze anybody out. They all have their day in
2 court, and that they are carefully considered. I think that
3 we will have to do it in terms of the various combinations.
4 But I would hope that we don't make that decision until we
5 look at what it is that we want to put in.

6 If we say, well, we want this in, and we want that in,
7 and we want the other thing in, we may very well, then, find
8 ourselves in the position that we are going to have to
9 squeeze some things back out, or squeeze some things down.

10 Senator Nelson. Let me make a suggestion that might
11 meet your wish to address individual cuts first.

12 I agree with Senator Danforth. I introduced 10-5-3 on
13 this side, and I don't know of anybody, and I have not run
14 into anybody in finance who is not for some version of an
15 accelerated depreciation and capital formation.

16 Why not address ourselves to some individual reduction
17 equivalent to the Social Security increase of 11.6 percent.
18 I am not saying how you ought to do that, but just
19 individual tax cuts equivalent to that, and that is \$11.6.
20 Then move over and consider the accelerated depreciation
21 question. And then you have got one individual cut and you
22 have the accelerated depreciation question, now you look at
23 what is left to put in the package.

24 Senator Danforth. Mr. Chairman.

25 The Chairman. Yes, Senator Danforth.

1 Senator Danforth. The immediate problem that that
2 would run into is that the individual portion of the Social
3 Security tax cut would be about \$8 billion, and the business
4 portion of it would be about \$4 billion.

5 Senator Nelson. What is it you are talking about?

6 Senator Danforth. If you are going to do the Social
7 Security credit for an offset of some sort. So it would be
8 partly for individuals, and partly for business, and the
9 business portion of that, the \$4 billion for business, would
10 be a reduction in the payroll taxes, and some say that that
11 is a non-inflationary tax cut.

12 However, if whatever the portion of the tax cut that
13 goes for business is to be more carefully targeted to
14 reindustrialization, modernization, and increasing our
15 competitive ability that is \$4 billion of the business share
16 of the tax cut which really does not have anything to do
17 with modernization.

18 Senator Roth. Mr. Chairman, I have a great deal of
19 sympathy about what is being said to help business. But one
20 thing that concerns me, it seems to me that we have got to
21 recognize that if we are really going to do something about
22 productivity, then this nation has to become a savings
23 nation. That means that the citizens of this country have
24 to be given some incentive to save. Before they can begin
25 saving, it is also important that they be able to keep more

1 of their hard earned income.

2 The problem is that over the last three years, or let
3 us say by the end of this year, the typical American family
4 is paying an additional \$2,000 worth of taxes. What I want
5 to make sure, in trying to do something about productivity,
6 that we build some real tax relief for the individual,
7 including some incentive save, and not just talk about
8 business tax cuts.

9 One of the real problems we have in this country is
10 that in comparison with the Japanese and the Germans, the
11 American people do not save. I know there are differences
12 in how you account for that, but they say that roughly in
13 Japan the typical Japanese family saves between 20 and 25
14 percent, and in Germany between 10 and 15 percent. In this
15 country, in good times, it is about four percent, but it has
16 fallen below that.

17 So I want to urge and say that when we are putting into
18 place these changes, we want to incorporate income tax
19 reductions that ultimately result in incentives for the
20 American people of all classes to save. I think that this
21 should not be overlooked.

22 The Chairman. Mr. Bentsen.

23 Senator Bentsen. Mr. Chairman, I feel very strongly
24 that you are going to have to do something in the way of the
25 Social Security tax increase on the individual in

1 particular, and I will support something along those lines.

2 As far as on the business side, that tax cut would
3 certainly take some time before it passes through insofar as
4 helping on inflation. So I will be supportive of that
5 effort.

6 I get back again to the problem of Senator Danforth. I
7 tried very hard to find a way to structure this where we
8 could assure that we do something substantial about
9 productivity, and I don't know how you can pass a resolution
10 that does it. I think that we are going to have to look at
11 what the proposals are, and then we are going to have to
12 work very hard to see that within the limitations of the \$25
13 to \$30 billion that we bring it about. I think that we are
14 going to have to look at the individual components rather
15 than a flat resolution.

16 The Chairman. Mr. Chafee.

17 Senator Chafee. Mr. Chairman, as I understand what we
18 are doing here this morning, we are trying to set out some
19 guidelines as to how we are going to proceed.

20 First we decided that we are going to have a cut, that
21 has been determined, in this rough area of \$30 billion in
22 the first year. Now what we are trying to decide is how to
23 proceed with our next step, and everybody around the room
24 has a pet scheme proposal which they wish to advance. But
25 it seems to me that we should get on with the provision of

1 how the basic division is going to be between the
2 individual, if you wish, and what you might call -- I don't
3 want to call it a business cut, I must prefer to call it a
4 job creation bill. I believe that that should be in the
5 50-50 category.

6 Obviously, you cannot do it in the first year because
7 the more rapid depreciation, as it has been pointed out,
8 costs relatively little in the first year. So isn't it
9 possible for the staff to come up with a five-year program,
10 if you proceed, of how you divide it between job creation on
11 the one side, and the individual on the other, but using the
12 \$30 billion as a starting figure for each year.

13 The Chairman. That is not a bad suggestion, if we
14 could just the staff to do that.

15 Mr. Matsunaga, did you want to say something further?

16 Senator Matsunaga. Along the lines suggested by
17 Senator Roth, I might point out that beginning January 1, we
18 will have that additional \$200 per and \$400 interest credit,
19 as you know. So that would mean a loss of \$1.7 billion. Of
20 course, initially Senator Bentsen and I had introduced a
21 bill calling for doubling that, if you will recall, so we
22 might go along that line, too.

23 I am inclined to agree, Mr. Chairman, that we ought to
24 go into a long-term planning as well as short-term. Within
25 the term of five years, then I think we could show that a

1 business is not being lost sight of. But in the short term,
2 I would agree with the chairman that we ought to take care
3 of those who are suffering most, the low income tax
4 taxpayer.

5 Senator Dole. I think that we have already made great
6 progress regarding the major decision. I know that our
7 staff is meeting this afternoon on this side, and I am sure
8 the Joint Tax Committee is available. The Republicans will
9 be meeting each morning an hour before our regular session.

10 I think before we make any other decisions now, we
11 ought to regroup and have a discussion on each side. I
12 think that we could probably reach some consensus here the
13 way we are moving without any other decision being made at
14 this time.

15 The Chairman. I would suggest that the Democrats ought
16 to meet at 2:00 o'clock. I will let them know where we will
17 meet when I arrange a place. I would like to ask the
18 Senate, if it is all right, that the committee be permitted
19 to meet during the session of the Senate this week to try to
20 work this out.

21 I would hope that our staff, working with both the
22 majority and the minority members and Mr. Shapiro, who works
23 for all of us, that they try to help us put together some
24 pieces to see how these piece might sort of fall together.
25 They are usually in a pretty good position, as they hear the

1 Senators talk and confer, and talk with their staff
2 assistants, to see what measures have substantial support,
3 and what measures do not.

4 Maybe you can help us put together a suggested
5 combination, Mr. Shapiro, so that in effect the tax cut for
6 the workers does not squeeze out the tax cut for
7 productivity, and that we try to get some of the various
8 suggestions in there. Then we can talk about which ones
9 claim the highest priority among the senators.

10 How does that appeal to you, Senator Danforth?

11 Senator Danforth. I think that that is very good, Mr.
12 Chairman. I believe that there is a very strong consensus
13 on the committee on both sides, and it is just a matter of
14 working it out. Obviously, all of us have our own pet
15 projects, but I think that there is a large amount of
16 flexibility, and if we could get some sort of a listing from
17 the staff by categories as to what the possibilities are,
18 and what the revenue effects would be over a five-year
19 period of time, we would be in a position to reach an
20 agreement in fairly short order.

21 The Chairman. With the consent of the Senate, why
22 don't we try to meet at 3:00 o'clock this afternoon. Mr.
23 Stern will have to get a room for us over at the Capitol
24 Building.

25 Do you have a room for us over at the Capitol

1 Building?

2 Mr. Stern: Room S-207.

3 The Chairman. That is the reception room right off the
4 floor.

5 Then I suggest that we recess until 3:00 o'clock, if we
6 can gain consent of the Senate to meet at the Capitol
7 Building. The Democrats can have a meeting at 2:00 o'clock,
8 and our Republican colleagues might want to have a meeting
9 and discuss this matter at about that same time.

10 Senator Byrd. Mr. Chairman, there is a piece of
11 legislation that the Secretary of the Treasury is very much
12 interested in. I don't know whether this would be an
13 appropriate time to try to consider it, but maybe this
14 afternoon.

15 The Chairman. Yes, at 3:00 o'clock.

16 The committee stands in recess until 3:00 o'clock this
17 afternoon.

18 (Whereupon, at 12:40 p.m., the committee adjourned, to
19 reconvene in room S-207 the same day.)

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