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HEARINGS

Before the

COMMITTEE ON FINANCE

UNITED STATES SENATE

MARKUP

Washington, D.C.

May 17, 1983

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TUESDAY, MAY 17, 1983

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

The committee met, pursuant to notice, at 10:40 a.m., in room 215, Dirksen Senate Office Building, the Honorable Robert Dole (Chairman of the full committee) presiding.

Present: Senators Dole (Chairman), Danforth, Chafee, Heinz, Durenberger, Symms, Grassley, Long, Bentsen, Pryor and Bradley.

Also Present: Senator Boschwitz.

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Chairman Dole: Our first item on the agenda is the Enterprize Zone Tax Act of 1983. I was just saying in a preliminary way at the last meeting with several others -- I was not the only one there -- with the President, he asked when we were going to start marking up the Enterprise Zone legislation. I was pleased to tell him had it not been for this meeting, we would have started it 30 minutes earlier. So we are in the process of that.

The President also announced, which might be of some interest, that the Soviets have agreed to negotiate a

1 long-term grain agreement. That is the only other.

2 So who is going to be the lead? Dave, will you lead on
3 the Enterprize Zones? Rod, or somebody from somewhere?

4 Mr. Brockway: I think the administration will.

5 Chairman Dole: Mr. McKee or Mr. Brock?

6 Mr. Chapoton: I will ask Mr. McKee to go through the
7 basic provisions of the proposal.

8 Mr. Mc Kee: The tax provisions of the Enterprise Zone
9 proposal are roughly as follows. First, focusing on
10 incentives to employers to attract labor-intensive activities
11 into the Enterprise Zone, there are two types of payroll
12 credits that are being proposed.

13 The first is a 10 percent credit for the incremental
14 increase in the payroll of a business operating in an
15 Enterprise Zone. The credit is limited to 2 1/2 times. The
16 payroll you are dealing with is limited to low and moderate
17 income individuals. The individual cannot be paid more than
18 2 1/2 times the FUTA wage base in any particular year. That
19 is \$17,500 right now. So that if you added such an
20 individual to your payroll, the employee would receive a
21 credit of \$1,750.

22 The second credit is a credit designed to encourage the
23 hiring of disadvantaged individuals. This is a credit equal
24 to 50 percent of the amount paid to a disadvantaged
25 individual, and there are no limits on how much you can pay

1 this individual. So this is a very strong incentive to
2 higher lower income disadvantaged individuals in the
3 Enterprise Zone area.

4 The third credit is a credit for employees. This is a 5
5 percent credit that the employee takes on his or her tax
6 return. This credit is limited to 5 percent of the first
7 \$10,500 of wages paid to the employee.

8 In order to encourage capital investment in an Enterprise
9 Zone, there are substantial incentives. Primarily, the
10 investment tax credit is increased by 50 percent for
11 investments made in an Enterprise Zone. There is a special
12 new 10 percent credit for buildings in an Enterprise Zone.
13 Finally, there is a capital gain exclusion for people who
14 invest capital in an Enterprise Zone and earn a capital gain
15 on that investment. There is no tax on that capital gain.

16 We have tried to be very careful to incorporate
17 provisions which will prevent the abuse of the capital gain
18 exemption by limiting this favorable treatment to capital
19 gains which are directly attributable to Enterprise Zone
20 businesses. And we have tried to draft language so that
21 people cannot take advantage of this capital gain exclusion
22 without actually engaging in a business activity.

23 Finally, the restrictions on small issue industrial
24 development bonds, the general rules of which are to expire
25 at the end of 1985, are not sunseted for Enterprise Zone

1 businesses. Thus, the benefits of being able to use
2 tax-exempt industrial development bonds will continue to be
3 available to Enterprise Zone businesses without the sunset
4 that is due to go into effect.

5 That summarizes the tax provisions of the Enterprise Zone
6 proposal. It is our view that this is a well-balanced
7 package of tax incentives which will encourage the location
8 of businesses within Enterprise Zones. We have tried to
9 tailor the package to get the right mix of labor intensive
10 and capital intensive businesses in Enterprise Zones, and we
11 have struggled to try to be as cost effective as possible so
12 the revenue losses attributable to this bill indeed are
13 effective in encouraging activity within the zones.

14 We have resisted amendments to the proposal which we feel
15 would be very expensive and which would not produce the
16 requisite incentives that we are trying to achieve here.

17 Chairman Dole: Now, what about -- HUD is represented.
18 What about the non-tax provisions? Do you want to comment?

19 Mr. May: Mr. Chairman, the objective of this legislation
20 is to target on cities and rural towns which have a degree of
21 distress. Broadly speaking, UDAG eligibility is the criteria
22 for participation. It would require that the city and state
23 submit a course of action once they have been found eligible
24 to compete for designation of one of the up to 75 zones that
25 can be designated over a three-year period.

1 There is language in this year's legislation which would
2 require that up to one-third of those zones be smaller
3 communities in rural areas. The course of action submitted
4 by the city and state could be quite flexible. There are
5 some indications of what provisions might be included, such
6 as tax and regulatory relief, improvements in city services
7 and infrastructure, and involvement of residents of the area.

8 The Secretary of HUD would winnow through the submissions
9 and make designations on a rather flexible scale, giving
10 priority to those which appear to have presented a strong
11 course of action which appears to offer a likelihood of
12 success, and those which perhaps have some innovative
13 proposals in them from which we can learn lessons for
14 possible replication at the local, state and federal levels.

15 The federal commitment would be for the period which
16 would match the local commitments up to 20 years with a
17 four-year phaseout. We have included in this year's
18 legislation an evaluation procedure so that an understanding
19 of how the program has worked will be available at the end of
20 the three-year period.

21 It is a modest proposal, but we think it has some
22 exciting potential for both cities and rural towns with
23 problems of unemployment, the need for job creation and
24 revitalization.

25 Chairman Dole: I think Senator Bentsen has an

1 amendment. Maybe we can dispose of that now. It seems to me
2 to make some sense, and he could try it out on the
3 administration.

4 Lloyd.

5 Senator Bentsen: Thank you very much, Mr. Chairman.

6 Chairman Dole: It makes a great deal of sense. Excuse
7 me.

8 Senator Bentsen: That is better. Perhaps I should stop
9 now.

10 [Laughter.]

11 Senator Bentsen: Let me say, Mr. Chairman, I am not sure
12 how good a job these particular incentives are going to do.
13 I hope they are very effective. I know Senator Chafee has
14 taken the lead in that, and I congratulate him in it. I also
15 know Senator Danforth has taken a lead in trying to see that
16 some of the rural areas qualify.

17 I have a situation in South Texas where the unemployment
18 rate goes from a minimum of 20 to a maximum of 50 percent, 20
19 to 50 percent, the lowest per capita income in the United
20 States.

21 Now, if you get around McAllen, Texas, you have an area
22 where they are working very hard to get such an Enterprise
23 Zone qualified. They could have qualified possibly under the
24 law as it was proposed last time. Last time it was proposed
25 where you had a population of less than 50,000 or one

1 designated by the Secretary of HUD.

2 The thing has been changed to say "and." All I ask is to
3 move it back to "or," that the discretion be given to the
4 Secretary if he feels that particular area qualifies. I
5 believe that has met with the approval of the parties
6 concerned.

7 Mr. May: That is acceptable to the administration. My
8 understanding is that Senator Danforth, who had been the --

9 Senator Bentsen: I discussed this with Senator Danforth,
10 and he is for that.

11 Mr. May: That is acceptable to the administration.

12 Chairman Dole: Is there any objection?

13 [No response.]

14 Chairman Dole: The amendment is agreed to.

15 Senator Long also had an amendment.

16 Senator Long: I wanted to suggest, Mr. Chairman, that in
17 evaluating these competing applications for zone
18 designations, efforts should be made that they should
19 consider efforts to provide equity sharing for employees of
20 zone businesses. In other words, while we are doing all of
21 this, maybe we can try to see to it that the result of all of
22 this is the people who work there own some of it. I think it
23 would be a good thing if that would be one of the criteria to
24 look at.

25 Chairman Dole: Has the administration had a chance to

1 review the amendment?

2 Mr. May: We have a general understanding, Mr. Chairman,
3 as I understand.

4 Chairman Dole: Mr. Gates I think can clarify it.

5 Mr. Gates: Yes, Mr. Chairman. As I understand, the bill
6 currently lists four examples of courses of action that might
7 be included when HUD and other agencies evaluate the
8 desirability of a zone designation. This amendment would
9 propose a fifth example to read "mechanisms to increase
10 equity ownership for zone residents." For example, a local
11 or state government could establish a revolving fund to help
12 finance employee buyouts in zones.

13 Chairman Dole: It would not be mandatory.

14 Mr. Gates: None of these are mandatory, Mr. Chairman.
15 They are permissive. This would add a fifth to the list of
16 four permissive things that could be looked at.

17 Mr. Chapoton: That would be acceptable to us, Mr.
18 Chairman.

19 Mr. May: Do I understand that this would be -- we would
20 prefer -- I think it is perhaps semantics, Senator, but if we
21 could add that page 11, subsection (d) as an additional part
22 of the sorts of things which can be included in the course of
23 action, I think it would be --

24 Mr. Gates: That is correct. It would be in (e).

25 Mr. May: Do you want it as a separate one rather than

1 just adding it as part of (d)?

2 Mr. Gates: Correct. It would be fifth, a separate one,
3 as (e) in the criteria.

4 There is no difference of substance, Mr. Chairman.

5 Chairman Dole: There is no objection to the amendment
6 once you decide where to put it?

7 [No response.]

8 Chairman Dole: Then the amendment is agreed to.

9 Senator Durenberger, do you have an amendment?

10 Senator Durenberger: Yes, Mr. Chairman. I think this
11 has been discussed with the staff, and at least there is a
12 description for the members of the committee.

13 My amendment is premised on the fact that the legislation
14 we are considering will provide for zone designation that
15 will last some 20 years or so. It seems to me that it is
16 impossible to predict exactly the best method to encourage
17 the most appropriate utilization of Enterprise Zones, both
18 national and state, over that long a period of time.

19 The intention of the amendment is to provide some degree
20 of flexibility and to encourage some experimentation as to
21 the most appropriate methods for achieving the goals the
22 legislation tries to achieve.

23 This amendment would require the Secretary of HUD to
24 establish a procedure for modifying the Enterprise Zone
25 incentives and commitments, and at a minimum the procedure

1 would include initiation of the action by the Secretary of
2 the state involved or any of the local jurisdictions for the
3 modification of the federal, state or local incentives.
4 Prior approval of HUD before any change in the mix of state
5 or local incentives is put into effect. However, nothing in
6 the procedure would prohibit the participating governments
7 from unilaterally adding new incentives, a reasonable
8 transition period for existing zone businesses to operate
9 under prior sets of state and local incentives notice, and no
10 reduction in the overall value of the incentives that
11 originally led to the zone's designation.

12 It just comes from the fact that we have had a lot of
13 state activity out there while we have been anticipating
14 federal legislation. And what we are trying to do here is
15 try to find some modicum of flexibility involving the
16 Secretary and the states so that we do not lose whatever
17 incentives came out of these state programs.

18 I do not have magic language to achieve that, and that is
19 why I have been relatively general here in suggesting what
20 might be the most appropriate language. But I would like to
21 move this in a sort of consensus way and then let us work
22 with HUD or whoever else is specified.

23 Chairman Dole: I wonder if I could have HUD's response
24 to the suggestion of the amendment.

25 Mr. Sloame: We think the proposal is a constructive

1 one. We do have some problems with the details of it. There
2 are a host of problems that are associated with such
3 flexibility. For example, one must be careful not to send out
4 the wrong signal to the investment community that certain
5 kinds of incentives such as property tax abatements might be
6 abrogated in the middle of the Enterprise Zone. That could
7 send the wrong signal and make it much more difficult for
8 businesses to obtain financing.

9 On the other hand, we recognize that, for example, if a
10 course of action included increased police protection, an
11 additional six patrol cars in a zone, and then as a result of
12 the success of the zone the crime rate was reduced
13 dramatically and there was no need to have six patrol cars
14 permanently assigned, certainly some provision ought to be
15 made to modify that commitment in some fashion.

16 So what I am suggesting is because the courses, the
17 potential courses of action are so infinite in nature and so
18 different in their consequences, perhaps it might be best to
19 incorporate the suggestion by Senator Durenberger in the form
20 of an amendment that would permit the Secretary of HUD to
21 issue regulations that could take this into account -- broad
22 authority to issue such regulations without being
23 proscriptive in the language of the legislation itself,
24 giving the difficulties and the variety of courses of action.

25 Chairman Dole: I assume -- let us just say you had an

1 Enterprise Zone and there was some obvious too generous
2 treatment being provided in that area. Would you address
3 that with your amendment? Would you modify whatever the
4 benefits might be? Does it go that far?

5 Mr. Sloame: I am sorry. I do not understand.

6 Chairman Dole: I am just saying if someone had -- in
7 other words, if the taxpayers were paying someone a rather
8 generous tax break, when you determine two or three years
9 down the road that it may not be deserved or is more generous
10 than you had intended, this amendment would permit you to
11 move in and make changes, is that correct?

12 Mr. Sloame: Yes. But again, I would like to see this
13 more in the form of regulations. For example, let us say
14 there were a property tax abatement. We would want to be
15 able to make sure that no businesses that relied upon such an
16 incentive in a course of action by moving or building within
17 a zone was adversely affected by such change, for two
18 reasons: one, it would be simply unfair, and secondly, it
19 would increase the difficulties they would have of getting
20 financing, as I said before, if the investment community was
21 under the impression that these property tax abatements, for
22 example, could be lifted at any time.

23 So at the very minimum we would -- again, under
24 regulations, I would hope -- provide for some grandfathering
25 of existing benefits for those companies that would rely,

1 that acted in reliance upon that. But, again, I think this
2 is something more suitable for regulation.

3 Senator Durenberger: I would agree with that. My
4 concern all of the way along in this proposal and the
5 concern, for example, of our metropolitan area in
6 Minneapolis-St. Paul is they started down this track of
7 deregulation and tax equity as a way to take some of the
8 economic competition out of urban development. And I think
9 their original apprehension when the federal legislation was
10 proposed was all of a sudden the federal government is going
11 to come along and start dictating, in effect, through a set
12 of benefits where development in a community, a large urban
13 community, might take place. So we are arguing for that kind
14 of flexibility.

15 I realize you cannot spell out all of the details in the
16 legislation, so if I can frame up in legislative language the
17 flexibility and give to the Secretary the authority to
18 promulgate regulations, that would be most appropriate.

19 Mr. Sloame: We would not be opposed to that.

20 Chairman Dole: Without objection, if you can work that
21 out with Senator Long, the HUD people, and Senator
22 Durenberger on this side -- have you had a chance to look at
23 it?

24 Senator Long: I have not had a chance to focus on it
25 yet, but I am not objecting to it.

1 Chairman Dole: Senator Chafee, do you have any comments?

2 Senator Chafee: Mr. Chairman, first of all, I want to
3 congratulate you for scheduling this markup on this subject,
4 and I am glad we are moving ahead.

5 As you know, it has been a long, difficult road. I want
6 to give credit to Senator Boschwitz who has worked extremely
7 hard on this legislation and has been deeply concerned from
8 the very beginning.

9 As Mr. May pointed out, this is just an experiment. This
10 is not going to solve all of the world's problems. There are
11 a very modest number of these zones that can be designated
12 each year, 25 and 75 over the total of three years. But it
13 is an effort in an area I think all of us are conscious is
14 suffering very badly; that is, the inner city. Not just
15 because of the flight of industry that we are concerned, but
16 it relates right back to jobs.

17 What we are trying to do is provide jobs in the inner
18 city, and this has a variety of approaches, as has been noted
19 previously.

20 Now, Mr. Chairman, one of the problems that has come up
21 has been those raised by the preservationists. They have
22 deep concern, and I admire them for their alertness and
23 dedication to this area. They have deep concern that unless
24 some action is taken before the zones are designated -- an
25 inventory of the buildings, for example, then things will not

1 take place afterwards.

2 We had witnesses from the preservation groups here, and
3 it seemed to me it made more sense instead of requiring an
4 inventory in advance, because there are going to be a host of
5 cities that are going to submit applications that are not
6 going to succeed, and these inventories require some effort.
7 So instead of requiring the inventory in advance, I would
8 propose that those areas that are designated as zones within
9 60 days after the date of designation, an inventory of the
10 historic properties must be completed.

11 Now, I think that meets the concerns of the
12 preservationists, although I will publicly note here that
13 they are not completely happy with that arrangement.

14 I think we find in these urban renewal revitalization
15 efforts that great attention is made to historic structures.
16 We have seen that in Boston, the Quincy Market. We have seen
17 it in Harborplace in Baltimore. We have seen it in DeVaul
18 Square in my own capital city of Providence, Rhode Island.

19 Furthermore, there are tremendous incentives in this
20 legislation, Mr. Chairman, to rehabilitate historic
21 properties. There already exists a 25 percent investment tax
22 credit in the law for the rehabilitation of historic
23 properties, and the zone bill would provide an additional 10
24 percent.

25 Now, that even gets the attention of Mr. Chapoton. That

1 is very attractive. And so you get up to a 35 percent
2 credit. We are not talking deductions. We are talking
3 credits. And historic properties I believe provide one of
4 the most lucrative development opportunities to be found
5 anywhere.

6 So, Mr. Chairman, I would urge the adoption of this
7 amendment that would require an inventory within 60 days
8 after the zone has been designated.

9 Senator Long: Let me just raise a question, if I may.
10 It has not to do with the amendment so much as what Senator
11 Chafee said in the beginning. You said something to the
12 effect that only 25 would be designated the first year, I
13 think.

14 Now, I am under the impression from at the bottom of page
15 4 and the top of page 5 that all 75 areas could be designated
16 immediately after the bill becomes effective. Is that
17 correct or not?

18 Mr. Sloame: The amendment between last year and this
19 year was that within the three-year period the Secretary
20 could designate up to 75. The narrow restriction that he
21 would be forced to designate only 25 in each of the three
22 years was dropped in last year's amendment.

23 Senator Chafee: I apologize. I was wrong in that.

24 Senator Long: The thought that occurs to me about it is
25 that the bill might have been right in the first instance. I

1 guess I am like anyone else. I am usually against any
2 combine I ain't in on. If we are not going to be in on the
3 thing, then I do not want to go forward with it. In fact, I
4 could feel more confident that I was for the bill if I could
5 see who was going to get in on this act to begin with, so
6 that it says right there in the act who gets designated.

7 But now if you are going to designate 75 areas right off,
8 then I would assume with all of the advantages in here you
9 would have a lot of people coming up seeking to be
10 designated. That raises a question in my mind. How do you
11 hope to control the cost of this if you will be designating
12 75 areas immediately?

13 Mr. Sloame: We do not anticipate designating all 75 of
14 the zones immediately. The reason for the amendment last
15 year was because of the period of time between the drafting
16 of the legislation at the start of the administration and
17 this present time. Many, many cities and states have already
18 gone ahead and formulated plans for Enterprise Zones.
19 Sixteen states have already enacted enabling legislation,
20 including the State of Louisiana. And we felt it would be
21 unfair and arbitrary to penalize those communities that have
22 gone ahead.

23 If we were to restrict ourselves in the first year to 25,
24 in the event there were more than 25 potentially good
25 candidates for designation in the first year, perhaps we

1 might designate 30 or 32 if we felt, or even 10 if there were
2 not a sufficient number of applications. We wanted to have
3 that flexibility and take into account the experience many of
4 the cities and states have over the country; because
5 fundamentally we believe that the seeds we have sown with the
6 Enterprise Zone concept are beginning to bloom. And as a
7 result of that, with all of the cities and states going ahead
8 with their own programs, we do not want to be unfair.

9 Senator Long: Then this question is not necessarily
10 conclusive one way or the other about Senator Chafee's
11 amendment. It is all right for me to vote on Senator
12 Chafee's amendment.

13 Senator Chafee: Let me say one more thing about the
14 amendment, if I could return to it briefly.

15 Obviously, in the application if an historic zone survey
16 had previously been completed, then presumably the Secretary
17 would look on that as one of the ingredients that might help
18 him arrive at the conclusion that this is a good package. He
19 could choose that if he wanted. That is his business.

20 But what I am saying in this is that is not required,
21 because in some instances it is rather expensive and
22 complicated; that after the zone is designated, then within
23 60 days it has to be done.

24 Mr. May, how does that strike you?

25 Mr. May: We have no objection to that.

1 Chairman Dole: Is there any objection to the amendment?

2 [No response.]

3 Chairman Dole: Without objection, the amendment is
4 agreed to.

5 Senator Pryor.

6 Senator Pryor: Mr. Chairman, I strongly support what
7 Senator Chafee is attempting to do in historic preservation
8 for the Enterprise Zones. I will probably vote I assume with
9 what may be the majority of the committee in sending this
10 bill to the floor, but I do want in the year 2003, I hope
11 that some historian will look back over this hearing and read
12 a concern I am expressing right now.

13 And that concern is that when we start phasing this out
14 of these particular zones, I do not think it will ever be
15 phased out. I think once you come to expect more or less a
16 gift or a special situation like that, before long it becomes
17 an entitlement. And I think either we will make the whole
18 country at that time a free enterprise zone, but I do not
19 know who will give up this benefit they have had in the year
20 2003. And I know you have a four-year phaseout period. So I
21 want to raise a concern about that.

22 The second concern I have is I remember back in the '60s
23 when the Model Cities program came on board. I do not
24 remember -- do any of you remember -- how many model cities
25 were designated as model cities?

1 Mr. May: I am guessing, 250.

2 Senator Pryor: I do not think that many.

3 Mr. May: It started small.

4 Senator Pryor: Maybe it was 250, but the first model
5 cities that were designated, I think if you would go back and
6 read the records of HUD and whatever, I think there were
7 about 12 people on the Housing and Urban Development
8 Subcommittee on appropriations in the House, and I think
9 there were 12 or 13 members on that subcommittee, and I think
10 those were the 12 or 13 first model cities designated.

11 My point is very simple. I am hoping this is not going
12 to be political. And if it is political, I think we will all
13 be held accountable. And I think that HUD will be
14 scrutinized very carefully by this committee and the
15 Oversight Committee as to how this designation process takes
16 place, and I for one will be watching it.

17 I am not saying in the State of Arkansas I want you to
18 designate one, two, three or four Enterprise Zones, but I am
19 just hopeful that these decisions will not be based upon
20 political considerations.

21 Mr. May: Senator, I think based upon our understandings
22 with Secretary Pierce who would make the final designations
23 that I can assure you we are genuinely committed to an
24 experiment involving a diversity of regions, sizes of cities,
25 different courses of action, whether it is Camden, Arkansas --

1 Senator Pryor: You have done your homework.

2 Mr. May: -- Or Providence, Rhode Island, or Aliquippa,
3 Pennsylvania, we are very much committed to doing it open and
4 above board trying to see what works and what does not.

5 Senator Pryor: I think we will all be watching. That is
6 my point.

7 Chairman Dole: I certainly share the view that it should
8 not be political, but do keep in mind that this committee has
9 jurisdiction of this program.

10 [Laughter.]

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1 Senator Symms: Mr. Chairman, just for my edification,
2 can I ask a question? Who qualifies for the 75 zones
3 eventually? I mean, does it have to be a major metropolitan
4 area?

5 [A chorus of noes.]

6 Senator Symms: What are the criteria?

7 Mr. May: There is within the language -- we have just
8 changed it slightly this morning, Senator -- a so-called
9 rural set-aside, that up to 25 of the 75 zones would come
10 from smaller communities outside large metropolitan areas.

11 Senator Symms: Do you perceive that someplace like
12 Kellogg, Idaho, where the major employer in town shut down,
13 is eligible?

14 Mr. May: Very much so, as long as they meet the
15 eligibility criteria. Simply because we are looking for
16 diversity in terms of different approaches, in other words,
17 yes, we are looking to the South Bronxes, the Harlems, and
18 Watts' of this country, but we are also looking at the
19 Kellogg, Idaho's, and the Cando, North Dakota's, and so on.
20 Wherever there is the possibility of creating jobs and
21 revitalization, that is where we would hope to see the
22 enterprise zone concept tried.

23 Mr. Sloame: Essentially, if a community is eligible for
24 UDAG it would be eligible for enterprise zone, with certain
25 other requirements.

1 Senator Symms: They would not be eligible for UDAG. It
2 is a small city, 2,000 people.

3 Mr. Sloane: We have a small cities UDAG program which
4 takes that into account.

5 Senator Symms: I have not made up my mind, I would say
6 for the record, whether I will vote for or against this bill,
7 not just because of Kellogg, Idaho, specifically, but because
8 I realize if we were doing the right things in the Congress,
9 which I do not think we are -- we have not cut spending
10 enough, we have failed to address the entitlement programs.

11 With all due respect to the Congress, I think the social
12 security solution was a failure, and to the Administration I
13 would also say that. I still think we have to fix some of
14 these things, and we should be trying to make the whole
15 United States an enterprise zone and not have some kind of
16 discriminatory tax policy going out, giving a special favor
17 to one group or another.

18 I do not want to stand in the way of what the President
19 wants to do, what the promoters of this legislation want to
20 do, and if I do vote against it I do it only because of the
21 principle involved here. We are trying to go out here and
22 say, we really screwed up in the United States, we have lost
23 control of our Congress, and now we will go into some of the
24 worst burned-out areas, so to speak, and try to apply some of
25 what built this country to fix this program, when really we

1 need to do the whole country that way and give the whole
2 country that opportunity to have a free enterprise zone, make
3 the United States a free enterprise zone.

4 We could do that. If we would cut spending by about 20
5 percent of what we are spending, this thing would start
6 straightening out in a hurry. But we fail to see that. So
7 now we are going to try to set aside 25, 50, 75 areas.

8 I do not know how I will vote on it. I might vote for it
9 or against it. But I think that is probably more irrelevant,
10 but I think someone here ought to voice the proposition that
11 this is a discriminatory tax policy that will favor and
12 allocate resources to certain areas of the country and give
13 them an advantage over other areas of the country, instead of
14 allowing a uniform policy of tax code and then if local
15 governments want to bring people in let them do what they
16 want to. If they want to have no property taxes for ten
17 years if someone comes in, let them do it.

18 But do not involve and discombobulate what has been a
19 taxing policy in this country that has tried to be equitable
20 to everyone. And I think the record ought to show that there
21 is some concern for what we are trying to do here.

22 If I thought at the end of 20 years we could expand the
23 enterprise zone into the rest of the United States, I would
24 say to my friend from Arkansas, I think I will vote for it,
25 if that is what our goal is, to have 25 enterprise zones this

1 year and 125 next year and then 1,250 the next year, and just
2 expand it to the whole United States.

3 Then we might have something going here that might be
4 worthwhile.

5 Mr. Sloame: Senator, I would like to make two points in
6 response. The first is, this is indeed an experimental
7 program. It is quite a massive set of tax benefits, and
8 before we make the whole country an enterprise zone we
9 thought it prudent to try it out on 75 communities. And we
10 have built in an evaluation procedure so we can report to the
11 Congress on exactly whether or not these incentives will
12 work. We do not want an unnecessary loss to the Treasury in
13 the event the program incentives do not work.

14 Secondly, in response to your other point, we do not
15 agree with President Kennedy when he said that the rising
16 tide lifts all boats. Thank you, Senator Heinz. There are
17 disadvantaged areas of the country that have structural
18 problems that need special attention, and having a uniform
19 set of incentives for the entire country would essentially do
20 nothing for these particular distressed areas. And they need
21 some special attention and that is what we are doing with
22 this bill.

23 Senator Heinz: The way to use that quotation best is to
24 say a rising tide lifts all boats and therefore will help
25 people who have boats, and the enterprise legislation is

1 designed to give a boat to people who would drown without
2 it.

3 [Applause.]

4 Mr. Sloame: Excellent. Thank you.

5 Senator Symms: There is one other thing I would say, if
6 I can get back the floor. And I appreciate my colleague's
7 wit this morning.

8 It just appears to me that a rising tide may lift
9 everybody up that is in a boat, but I can assure you, when we
10 are running the fiscal side of our government the way we are
11 today, trying to think that -- the problem as I see it is we
12 are spending 25 percent of the GNP on government expenditures
13 and that is 25 percent of the GNP of the country that the
14 people cannot decide how to spend for themselves.

15 So we can have an enterprise zone and try to fix this
16 little area, but in the meantime we will either steal this
17 money from the public by printing it, which is a polite way
18 to say stealing it -- you print it and take away the value of
19 the money they have in their public and inflate the currency
20 -- or we are going to borrow it, which will crowd people out
21 of the loan window, or we are going to come in here and raise
22 taxes across the board on everyone else.

23 So if we do not fix the problem, that is like the guy who
24 has cancer and puts vaseline on it instead of cutting out the
25 cancer. That is my problem with this whole concept. I mean,

1 I like the idea, it sounds good, and I am sure it is great to
2 go out to the city and have the mayor cut the ribbon to start
3 the enterprise zone.

4 But the problem is it will just treat the symptom, and
5 the problem is the overall picture in this country is we
6 still have failed to get a hold of the fact that the Federal
7 Government is spending 25 percent of the GNP. And I am not
8 as concerned about the fact that they only tax for 19 percent
9 of the GNP as I am that we spend 25.

10 If we could get back down to where we were spending 19
11 percent of the GNP, I would be willing to lower taxes back to
12 5 percent of the GNP, if that is what it takes to keep the
13 pressure on government spenders. But this problem, I think
14 the record ought to show, the enterprise zone thing, no
15 matter what we think here, is not going to solve the big
16 problem of the economy in this country, because we cannot.

17 The tide that sinks will sink all boats, that is for
18 sure. It will sure set them down on the mud, anyway. And
19 that is what I think concerns me about these kinds of
20 programs. It is a rifle shot, but we have a big picture
21 problem here and a macro problem in our economy, where
22 generally speaking we are taxing people too much. The
23 Federal Government is giving away too much money to people
24 who are not earning it and taking away incentives for people
25 who work.

1 The priorities of government spending are discombobulated
2 in view of the threat we face militarily in this country. We
3 are arguing about whether or not we want to spend more or
4 less money for defense at a time when the historians will
5 look at that and wonder what we were thinking about.

6 End of my sermon.

7 Senator Long: Mr. Chairman, I am concerned and worried
8 about this program for a number of reasons. One of them is I
9 am concerned about the cost, about these estimates. My
10 understanding is that our experience under the IRA, what we
11 did under recent legislation, is that the IRA is costing us
12 about 13 times what we thought it would cost. Is that the
13 correct amount, Mr. Chapoton?

14 Mr. Chapoton: It is from three to four times -- the
15 participation has been much higher, three to four times what
16 we anticipated.

17 Senator Long: I read somewhere that it costs about --
18 what did you show me?

19 Mr. Gates: That was the Employee Benefit Research
20 Institute. Their indications were it cost 13 times.

21 Senator Long: They estimated it would cost about a
22 billion and it is costing \$13 billion?

23 Mr. Gates: It was projected around a billion dollars and
24 their figures indicate it will be over \$13 billion.

25 Senator Long: And expected to go to \$17 billion next

1 year. Is that correct or not? I would just like to know?

2 Mr. Chapoton: Not by our figures, Mr. Long. I do not
3 have the actual figures with me. We have been over them. It
4 was about three and one-half times original cost.

5 Mr. Brockway: I believe, Senator, the \$13 billion is a
6 combination of old law and the '81 changes. The increase,
7 though, is about three and a half times what was estimated..
8 So basically, both statements are correct, but the increase
9 from '81, combining that with what there was above present
10 law.

11 Senator Long: That is enough right there to run up about
12 \$10 billion of deficit over and beyond the estimate. Now,
13 usually we have not been anything like that far off on these
14 revenue estimates, have we? I mean, you come in here and
15 tell us something is going to cost --

16 Mr. Chapoton: No, we have been back over that, that is
17 correct.

18 Senator Long: You told us it would cost \$3 billion and
19 it winds up costing \$13 billion. That is very far off for
20 Treasury. Treasury is usually pretty close.

21 Mr. Chapoton: I think we are talking about lower numbers
22 than that. I am quoting from memory, but I believe it was
23 about a billion and a half. So we are talking more in the
24 range of four to five billion.

25 Mr. Brockway: Yes, I think we were estimating something

1 in the neighborhood of a billion and a billion and a half,
2 and the numbers will come in around four billion as best we
3 know right now. We will just have to wait until we get more
4 time.

5 The Chairman: How far did we miss the All Savers
6 Certificate, that little plumb we put in in '81 for the
7 S&L's?

8 Mr. Brockway: At All Savers, I think we came relatively
9 close to the estimates. I think the initial reports were the
10 estimates would be far off the mark, but as it turned out the
11 estimates that were given came relatively close to what in
12 fact was.

13 The Chairman: It did not serve any purpose, did it?

14 Mr. Chapoton: We did not think it served any purpose,
15 no, sir.

16 Senator Long: I want to know, how did you arrive at the
17 estimate you have here of what this will cost? I think you
18 estimated it will cost \$3.3 billion, something like that.
19 What is the estimated cost of this program?

20 Mr. McKee: \$3,452 million over fiscal years '84 to '88.

21 Senator Long: \$3.5 billion over four years?

22 Mr. McKee: Five years.

23 Senator Long: Over five years.

24 Now, how do you arrive at that figure? Can you give me
25 some idea how you arrive at that figure? How big are these

1 enterprise zones going to be? Figure 75 enterprise zones.
2 What did you estimate their size to be?

3 Mr. McKee: We assumed each enterprise zone would have
4 about 7,000 employees in it. Necessarily, the revenue
5 estimates here are somewhat rough because the statute does
6 not prescribe exactly how large an enterprise zone is going
7 to be.

8 We worked with HUD and attempted to determine what they
9 thought the size of the zone would be and the number of
10 employees would be in the zone, and then we had to,
11 obviously, make some estimates. But then, based upon the
12 number of employees we were able to --

13 Senator Long: Let me get this straight. Before you go
14 further, I want to get this straight in my mind, because I
15 think we owe a responsibility to the Senate to know what we
16 are recommending.

17 Now, 7,000 employees for the enterprise zone. Does that
18 mean 7,000 will be getting incremental employees? That does
19 not mean 7,000 disadvantaged? Does that mean 7,000 will get
20 some specific advantage out of this program or just 7,000
21 employees in the zone?

22 Mr. McKee: 7,000 new jobs, I think, that will be
23 created, 7,000 employees who will be able in one way or
24 another to use the incremental labor credit, the target labor
25 credit, and the employee labor credit.

1 Senator Long: I am just trying to picture that in my
2 mind. What would that indicate the population of the average
3 zone would be?

4 Mr. Brockway: Mr. Long, that is 7,000 employees within
5 the zone, not increased employees as a result of the
6 program.

7 Senator Long: Not increased employees.

8 Mr. Brockway: 7,000 total employees within the zone.
9 That is the average size.

10 Senator Long: All right. Now --

11 Mr. Brockway: That is in the beginning of the
12 designation. The assumption is it would increase as a result
13 of the program.

14 Senator Long: What does that envision the average size
15 zone being? You say 7,000 employees in the zone. About what
16 would the population of that zone be, just the average?

17 Mr. May: Senator, the only definition in eligibility is,
18 in larger cities you must have at least 4,000 people living
19 within the zone area. In smaller cities, the minimum
20 population would be 1,000.

21 There is a certain self-regulating aspect to it, if you
22 will. Obviously, if a city and a state want to provide an
23 intense set of benefits and incentives, they will want to
24 constrict the area rather than having it terribly large and
25 broad. So we do not envision it would be whole cities. It

1 would be a fairly compact area within a city which meets the
2 eligibility criteria.

3 Senator Long: I am just trying to picture this in my
4 mind. I would like to know what we are doing here, and I
5 think it is my responsibility to try to know what I am
6 doing.

7 Now, you are assuming that the average zone would be
8 7,000 employees. What I want to know is, just thinking in
9 terms of the average zone, what would the population be of
10 that zone that has 7,000 employees? How many people? What
11 would you estimate the population would be?

12 Mr. McKee: Senator, in doing the revenue estimates it is
13 not necessary the individual live in the zone. It is that
14 the individual works in the zone. You could have people
15 qualified for these credits who live outside the zone but
16 work inside the zone.

17 I think it is very fair to note that these are,
18 obviously, difficult revenue estimates to come up with,
19 because the statute does not define exactly how large the
20 zone will be, and therefore we are working with some rough
21 estimates. Our revenue estimators do the best job they can,
22 but when the parameters of the program are somewhat
23 undefined, the revenue estimates are somewhat ambiguous or
24 the revenue estimates are not as precise as they might be in
25 other types of programs.

1 Senator Long: If I had the burden of trying to explain
2 this bill to the Senate, which, thank the lord, will not be,
3 but if it were my burden to try to do so, I would like to be
4 able to picture this to the average Senator, to tell him what
5 that might mean as far as his state is concerned, to give him
6 a specific example, just what are we talking about here.

7 So you are talking about an average zone having 7,000
8 employees. I would like to know just in terms of the
9 average, about how many people are we talking about being in
10 the zone, what the population of the zone would be.

11 Mr. Brockway: Senator Long, in making the estimates the
12 population itself was not taken into account. Under the
13 legislation there is a variety of standards you look at when
14 you designate a zone to give priority. But it could in fact
15 have perhaps a relatively low number of employees and a high
16 amount of capital assets in the zone, and that would affect
17 how much revenue. Or it could have a lot of employees
18 working in the zone but a relatively small population. Or it
19 could be an area with a relatively high population, but still
20 a relatively small number of zones.

21 And making the assumptions for revenue, what Treasury did
22 was just make certain limited assumptions, like 7,000
23 employees on the average, because it is very difficult to
24 come up with a precise revenue because you do not know at
25 this moment how large the zones will be, what their nature

1 will be. So they just have to make certain particular
2 assumptions.

3 You will not know until the application process goes
4 forward what your zones will be.

5 Senator Long: Then the answer is you do not have the
6 slightest idea how many people will be in the average zone.
7 I guess that is the answer, you cannot even guess.

8 Mr. McKee: Again, Senator, the revenue estimates depend
9 not on the number of people in the zone, but primarily on the
10 increase in employment that takes place in the zone. While
11 we would certainly agree --

12 Senator Long: You said 7,000 increase in employment. I
13 am told over here it is 7,000 jobs period. Which is it?

14 Mr. McKee: It is 7,000 employees who will receive
15 benefits, tax benefits under this legislation.

16 Senator Long: In the zone?

17 Mr. McKee: That is correct. There are three tax
18 benefits: the incremental labor credit, which requires a
19 firm increase its employment; there is the targeted labor
20 credit. Now, that is something for disadvantaged
21 individuals. A firm does not have to grow in order to get
22 advantage of that credit. It can simply replace one worker
23 who leaves with a disadvantaged worker. And finally, there
24 is the employee credit, which is available to anyone who
25 comes and works for a zone business.

1 There will certainly be some businesses in enterprise
2 zones that do not qualify for any of these credits. If you
3 are already operating in the enterprise zone and you do not
4 expand your payroll or hire any disadvantaged people, or if
5 your business is not located at least 80 percent in the zone,
6 and you happen to just be doing some business in the zone,
7 you will not qualify for credits.

8 Senator Symms: Will you yield for a question on that,
9 Senator?

10 Senator Chafee: One other point I would make, Senator
11 Long, is the criteria that must be met with regard to average
12 unemployment or the poverty rate or so forth within the zone
13 for it to qualify. So you cannot just step out and say, let
14 us make the city of New Orleans, the entire city, a zone.
15 You cannot do that because it would not meet the requirements
16 set forth under the eligibility on page 9 of the Act.

17 Senator Symms: Let me ask a question on that point right
18 there, Bill, if you would yield, Senator Long.

19 What you said is, if I am operating a company -- let us
20 say some guy is operating a shoe manufacturing company, for
21 example, in an area that would qualify for an enterprise
22 zone, and he has been there for 50 years fighting all the
23 problems, and hires 100 people. And if he does not hire new
24 people he is not eligible for the benefits.

25 You see, I have that shoe factory and Senator Long comes

1 in and starts a new one and he hires 100 new people, and he
2 gets the benefits, so he can outcompete me. Is that the way
3 it will work?

4 Mr. McKee: He will get more benefits than you will get.
5 You will still be entitled to the employee credit, which is
6 the five percent credit. And if you hire disadvantaged
7 people, a new disadvantaged person -- let us say someone left
8 your company, you went down to 99 people, and you hired a
9 disadvantaged person to replace the individual who left; you
10 would get that credit.

11 But there is no question that Senator Long, if he starts
12 a new business, would be entitled to more benefits than you
13 would be entitled to. It is our general feeling that most
14 businesses located within enterprise zones are primarily
15 businesses that serve the local community. They are
16 generally very small businesses, a local grocery store or
17 something like that.

18 The purpose of the enterprise zone legislation is
19 hopefully to attract businesses which will serve not only
20 just the local zone but will be much broader in their base.
21 They will be businesses designed to serve a large area around
22 the zone, which simply happen to be located in the zone. We
23 do not think those will be directly competitive with the
24 types of businesses one would expect to see in a severely
25 economically depressed area.

1 It would be relatively unlikely you would have a severely
2 economically depressed area with a reasonably thriving shoe
3 factory in it. Our judgment would be the areas HUD will pick
4 will be areas that do not have a shoe factory, but need one.

5 Senator Symms: It may be that it is not a thriving area,
6 but you have had some entrepreneur who has really done a
7 double-double extra effort to keep his little factory or
8 whatever working. It just seems that sets the stage for the
9 person who has been trying to fight all of the problems, and
10 his reward is we will open up a deal where his competition
11 can come in with an advantage over him, regulatory and
12 taxwise.

13 It seems it is basically inequitable.

14 Mr. McKee: On the regulatory side, your shoe factory
15 would qualify for regulatory relief. But there is no
16 question, we think HUD needs to be sensitive in picking its
17 enterprise zones to exactly those kinds of concerns.

18 Senator Symms: But if you put it in terms of a specific
19 area I mentioned earlier, like Kellogg, Idaho, where you have
20 old companies that have been there a long time, they are not
21 going to really qualify. So the answer would be just to go
22 out and form a shell corporation and come in with a new name
23 and title to get the benefits? Is that what will happen?

24 Mr. McKee: The statute has a provision in it to prevent
25 that.

1 Senator Symms: I do not think they will qualify,
2 frankly, anyway.

3 Mr. McKee: The idea is, for example in Kellogg, the
4 businesses that are there and functioning are probably
5 selling products around the country or at least throughout
6 Idaho and have their own niche in the marketplace. The new
7 company probably has no reason to think it will be
8 particularly directly competitive.

9 Our idea would be a new business trying to serve a
10 different market would be attracted because of these tax
11 benefits, still serving the entire area of Idaho and the
12 other states in that area. And we do not really think it
13 will be a very severe problem.

14 We worried about it a great deal for exactly the reasons
15 you have articulated, Senator. And, having talked it over
16 with HUD, we think they will be sensitive to those kinds
17 of concerns, to try to make sure they do not end up putting
18 someone out of business.

19 Senator Heinz: Will the Senator yield on that point?

20 Senator Long: Go ahead.

21 Senator Heinz: Mr. McKee, I just want to say I do share
22 some of Senator Symms' concerns in this regard. I said as
23 much during the hearings, and I hope we will be able to find
24 a way in particular to give or transfer or make available the
25 equipment or the kinds of tax benefits that this legislation

1 makes available to profitable businesses that may now be
2 operating outside the zone when they move into the zone,
3 which in the case of a substantial number of indigenous zone
4 businesses would probably not be available.

5 Now, I think there are some means of doing this. My
6 understanding of the Administration's position is, however,
7 that you are saying indigenous zone businesses can form up as
8 partnerships and thereby, through partnerships, the partners
9 can take up a pro-rata share of tax benefits.

10 Now, I do not know how practical in point of fact that is
11 for existing zone businesses, to go from a corporation, a
12 corporate form to partnerships. But even if it were
13 practical, which I sincerely doubt, you would have to make
14 two assumptions:

15 One, that those are the kinds of partners who would have
16 enough income so that the tax benefits would be meaningful.
17 But even granted that, there is another problem, which is
18 that under existing law only equity investors can participate
19 in tax benefits, and the zone partnerships are going to be in
20 competition with much more highly leveraged investors from
21 outside. Therefore, they will be on an unequal footing.

22 That is to say in plain English, the people coming in
23 from outside, being financially healthier, will be able to
24 get more credit, therefore they will be able to take larger
25 tax writeoffs.

1 And the Administration's logic, if I have stated it
2 accurately, really is an inadequate response to this
3 problem. Now, I hope that we can work with you to solve this
4 problem. I think there is a method of solving it that is not
5 safe harbor leasing, but would involve some transfer of
6 benefits together with a debenture, so that there would be a
7 linkage.

8 I have been trying to work with the Joint Tax Committee
9 to get all of the information and details of this worked out,
10 but I believe we have a problem, that it is addressable. It
11 will take a little bit of time. I am not prepared to give
12 you a proposal, or my colleagues, today. But I hope you will
13 work with us to address this problem, because I am convinced
14 it is a real problem.

15 Mr. McKee: Senator, we will certainly be happy to work
16 with you. It is our feeling that most of the new capital
17 that comes into the enterprise zones, which will generate
18 from the additional tax credits, et cetera, and will provide
19 the base for the additional wage credits, will come from
20 people who do have a tax base that can absorb them; and that
21 the present tax law contains a myriad of ways, as we all
22 know, to make those tax benefits available to the owners of
23 the equity.

24 It is not only through partnerships, but of course
25 Subchapter S corporations. If a new venture comes in as part

1 of a large corporate operation filing a consolidated return,
2 the tax benefits flow into the consolidated return.

3 We would be happy to try to work with you to see if there
4 is really a severe problem that can be addressed under
5 existing law.

6 Senator Heinz: If Senator Long will permit me one last
7 question, do you have any problems with the concept of
8 structuring something analogous to safe harbor leasing,
9 different from it -- clearly, we have spoken our mind on what
10 that ought to be -- but analogous to it, that would permit
11 the transfer for an appropriate consideration of the tax
12 benefits to the indigenous companies that could not properly
13 take advantage of those tax benefits to someone who is
14 willing, for a consideration, to purchase those tax
15 benefits?

16 Mr. McKee: I would only note that, given the history of
17 safe harbor leasing --

18 Senator Heinz: This is not safe harbor leasing.

19 Mr. McKee: But obviously, we understand the notion of
20 transferable tax benefits, since that is what safe harbor
21 leasing was about. So it is hard for us to say we are not
22 interested in working with you, but I want to reiterate, we
23 have looked at the problem pretty closely and we are not sure
24 the problem is there.

25 Our biggest concern is creating a device that may be

1 somewhat complicated and controversial if it is not
2 necessary. And we can work with you to determine how serious
3 the problem is.

4 Senator Heinz: If you say the problem is not there, how
5 do you respond to the issue of indigenous equity owners who
6 are not leveraged, therefore do not have the opportunities
7 and capital structure of the people from outside?

8 Mr. McKee: As I mentioned with Senator Symms, we are not
9 sure, depending upon how HUD picks the enterprise zones, but
10 our thought is that the zones that will be picked will be in
11 sufficiently depressed areas so there is not very much in the
12 way of indigenous business in there.

13 The whole notion of the program is to try to get outside
14 people to come in and start businesses, to infuse capital
15 into these zones. And as far as those investors are
16 concerned, we think the present tax law adequately takes care
17 of them.

18 I agree with you, to the extent that an indigenous
19 business is owned by people who do not pay very much in the
20 way of taxes because they are not doing very well, they will
21 have a hard time absorbing these deductions and credits. We
22 agree with that. And we need to take a look and see how much
23 tax benefits they will be able to capture.

24 Again, our notion is there will not be very much of
25 that.

1 Senator Heinz: I would like to spend more time with you
2 on this point, but I have imposed enough on Senator Long.

3 Senator Long, I thank you for yielding and I apologize
4 for imposing so much on your time.

5 Senator Long: Let me just get to the point of what I am
6 trying to picture in my mind here.

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1 Just to take an example that would be relevant in
2 Louisiana, I would assume that if this program is law, the
3 city of New Orleans will endeavor to be declared an
4 enterprise zone in whole or in part, assuming they have a
5 substantial amount of unemployment in certain parts of New
6 Orleans but not in all of it. What would the intent be, that
7 they would be eligible in whole or eligible in part?

8 Mr. May: Well, Senator, as Senator Chafee indicated, New
9 Orleans would be UDAG eligible, and then within a city of
10 that size you would need to carve out an area with at least
11 4,000 residents within that area to meet the additional
12 criteria set out in the legislation of either a fairly high
13 degree of poverty or unemployment or population loss. So you
14 are basically talking about a fairly rundown section of the
15 city, and as I have also indicated, let us say that the city
16 of New Orleans working with the state is prepared to offer a
17 fairly attractive property tax abatement incentive. They
18 will clearly not want to spread that citywide because they
19 would not be able to absorb that much loss. They will want
20 to concentrate it in an eligible area in a fairly small, we
21 think, tight area within that city.

22 Senator Long: Well, then, if you assume that they
23 confined it, would it be fair to say they might want to
24 confine it to one-quarter of the city? It is a city of
25 600,000. The metropolitan area is about 1.5 million.

1 Mr. May: I think it is really impossible to project
2 that, Senator. We did do some experimental conversations
3 with a number of cities around the country of varying sizes,
4 and we found, for example, in some cities as large as, say,
5 half a million, they were talking of an enterprise zone of,
6 let us say, it seemed to be about 20,000 people. We also had
7 a city of 50,000 that had a zone that I think was considering
8 only 2,000 people within it, so that you simply cannot make a
9 projection, because it has got to be a call. It is initiated
10 by a decision of the city and state working together.

11 Mr. Sloame: I think what the city will keep in mind,
12 given the requirement and the statute, that the course of
13 action be of a strong character, and I think we ought to
14 remember this is a competition, that the more they spread out
15 these benefits, not only the more will it cost them, but the
16 less value they will get out of it in terms of the
17 competition. In other words, if you are promising increased
18 police protection over a large area, for example, that will
19 cost the city a lot more than in a smaller area, or
20 conversely, they will only be able to promise somewhat less,
21 which would make them less competitive compared with other
22 cities that would be concentrating their resources in a
23 smaller area.

24 So, we hear figures like one to five square miles. Those
25 are the kinds of numbers we are hearing, and the population

1 minimums, as we said, are 1,000 in small areas and 4,000 in
2 larger communities.

3 Senator Long: I should assume in a situation like that
4 that those who are located in the area -- let us take
5 competitive businesses in the area -- would complain if they
6 are left out. They would feel it is not fair, that they have
7 a parallel situation or a somewhat similar situation and are
8 located in the general area, and they are at a competitive
9 disadvantage with the people who will be designated inside
10 the zone.

11 Now, what is your response to that? What shall we tell
12 those people? I am talking about the area just outside the
13 enterprise zone.

14 Mr. May: I think, going back to model cities, it is the
15 same tough decision that local officials have to make all the
16 time. They have to draw lines. They have to make decisions
17 to set some priorities and parameters on the area in which
18 they are going to work. I think you will also find perhaps a
19 drug store just across the line from the factory which has
20 been vacant will benefit if a business comes into that
21 factory, so that there will be some spinoff benefits. I do
22 not minimize. I have been a mayor. I know the difficulties
23 of drawing a line for a model cities area or a conservation
24 district or whatever. That is the kind of tough decision
25 municipal officials will have to make in situations such as

1 this.

2 Mr. Sloame: There is an analogy to different states or
3 different cities having different sales taxes. You could be
4 on one side of the district line and have a 4 percent sales
5 tax, and on the other side have an 8 percent sales tax. We
6 live with those discrepancies. Those are options for local
7 governments. Those are decisions they make. And what we are
8 really talking about here fundamentally is targeting, and
9 that is the effect or one of the side attributes of
10 targeting, that kind of discrepancy. The judgment is, it is
11 what is needed to make things happen in a particular
12 distressed area where nothing has been happening for many
13 years in most cases.

14 Senator Chafee: Also, I think it is fair to point out
15 that some states already have enterprise zones and permit
16 them so cities within those states have met the criteria, and
17 it has not. Mr. Mayor, you will have to help me, but it is
18 my understanding they have not gone beyond what we would
19 anticipate in areas within those cities. It has not
20 encompassed great, broad areas that would go contrary to what
21 the spirit of this Act was. Is that correct, Mr. May?

22 Mr. May: That is correct, to the extent there are zones
23 already designated in Connecticut, for example. Very much
24 so.

25 Senator Long: Let me ask this question. You have a

1 capital gains exclusion here which I look upon as a very big
2 tax advantage, and I am just wondering. Suppose someone had,
3 let us say, a small business, a car wash, and he simply wants
4 to sell the car wash to someone else. Would it be possible
5 for him to simply close the car wash down, then sell it, sell
6 the assets to the other fellow, let the other man open up,
7 and claim all of those employees as new employees?

8 Mr. McKee: If the previous owner and new owner were
9 entirely unrelated, yes.

10 Senator Long: If they are not related?

11 Mr. McKee: If they are not related in any way. In other
12 words, if I come into the zone and I want to start a car wash
13 business and try to build a new, fancy car wash, or whatever,
14 revitalize it, I could go in and buy up the assets of an
15 older operation, refurbish it, and get the credit for my
16 expenditures, the additional investment credit for the new
17 money I put in -- I am still subject to the used investment
18 limitations in the present statute -- and go on trying to get
19 the business going. I would be entitled to those credits.
20 We do encourage people to come in and try to expend
21 additional capital and get things going in the enterprise
22 zone again.

23 The capital gains exclusion which you address, Senator,
24 we have tried to craft that very carefully to make sure that
25 the exclusion is limited to capital gains attributable to the

1 zone business, so any gains that have occurred prior to zone
2 designation do not get this benefit. We have also struggled
3 very hard to draft language so that people cannot put capital
4 gain type passive assets in an enterprise zone situation, and
5 try to claim that the capital gain that occurs over time is
6 exempt. The property has to be actively used in the zone
7 business. You cannot put gold or something like that in a
8 warehouse in an enterprise zone and avoid capital gain
9 treatment on it.

10 Senator Long: My thought is, people would undertake to
11 find ways to get the benefit of this capital gains exclusion,
12 and I would think that if a man had a business for sale, or
13 someone was negotiating a sale, you would say, I can show you
14 how you can get this capital gains exclusion. All you have
15 to do is, we could work our deal out. All you have to do is
16 just say that you are closing down, and then I will sell you
17 the business, and then you can go hire those employees back.

18 Mr. McKee: Again, he has to have a capital gain
19 attributable to the operation of the active business during
20 the period of zone designation, so if I went in and started
21 the car wash business in 1985, and it thrived and prospered
22 from 1985 to 1990, and I could sell my car wash business to
23 you, the stock in my enterprise zone company, for example, I
24 do not have to pay any capital gain tax. That is one of the
25 incentives in this bill to try to get me to go into the zone

1 in the first place and invest my capital. It is a tax break
2 I get for having taken the risk of going into the zone and
3 trying to make something happen in the zone. There is no
4 question that is an intended benefit. We do try, as I
5 repeat, to make sure that the benefit is restricted to people
6 who do conduct zone businesses, active zone businesses. A
7 car wash is a good example. We intend, if I sell my business
8 to you, and I have conducted it in the zone, we intend for me
9 not to pay any capital gains tax on that, because that way
10 maybe I will go in the zone in the first place, whereas
11 without the tax break maybe I would not go into the zone.

12 Senator Long: I want to ask a question about this
13 disadvantage. How much advantage, tax advantage, do you get
14 for hiring a disadvantaged person ordinarily?

15 Mr. McKee: There is a targeted jobs credit now which is
16 a smaller credit that phases out much more rapidly as you
17 hired the person. This credit --

18 Senator Long: How much is that?

19 Mr. McKee: I believe it is 25. Let me look that up,
20 Senator. I think I have that.

21 Mr. Brockway: The current jobs credit is 50 percent the
22 first year, 25 the second year, and the limit is \$6,000 of
23 income.

24 Senator Long: What is the difference between that?
25 Would you mind spelling out the difference between that and

1 what you have in this bill here?

2 Mr. McKee: The credit in this bill for disadvantaged
3 people is a 50 percent credit for three years, and then
4 starting in the fourth year it phases down to 10 percent per
5 year, so the credit stays at the higher level much longer,
6 and phases down more slowly. So it is a larger credit. It
7 lasts for a longer time, and it is designed to encourage the
8 training of these people. It is simply a more substantial
9 credit, and it is part of the overall program in the
10 enterprise zone, part of a package. We think it will be more
11 effective because it is part of an overall approach to the
12 problem of dealing with economically depressed areas.

13 Mr. Gates: One other difference is, there is no dollar
14 cap. The targeted jobs have a \$6,000 cap on the amount of
15 includable wages, and in this case there is no dollar cap.

16 Mr. Brockway: There is also a difference in the
17 identification of employees who would qualify under the two
18 targeted jobs credits.

19 The Chairman: In other words, you can hire someone for
20 \$50,000 and half of it is a credit?

21 Mr. Gates: If they were on the AFDC rolls or the win
22 registry, half of it would be credited for three years, and
23 then it would phase down to 10 percent per year.

24 Mr. McKee: The types of individuals that qualify for
25 this credit would be unlikely, to say the least, to command

1 \$50,000 in the marketplace.

2 The Chairman: It would be unlikely without this
3 provision, but I am not so certain.

4 [General laughter.]

5 Mr. McKee: The employer still does pay the other \$25,000
6 out of his own pocket.

7 The Chairman: Senator Pryor?

8 Senator Pryor: Senator Bradley, but I would like to go
9 after him, if I might.

10 Senator Bradley: Mr. Chairman, I would like a
11 clarification. As I understand the legislation, a city that
12 wants to be designated will submit an application to HUD, and
13 one of the things HUD will look at is the extent to which the
14 applicant will use tax abatement in order to encourage
15 investment in the zone, and I would like to know if the tax
16 abatement is just one of several criterion, and if for other
17 sound reasons, other sound fiscal reasons tax abatement might
18 not be a part of a package, it would still be possible to
19 have a zone if for sound fiscal reasons you did not include
20 tax abatement as a part of your package. Is that correct?

21 Mr. Sloame: Absolutely correct. In fact, the statute
22 specifically says HUD will take into account the fiscal
23 ability of the state to make such tax reductions. Tax
24 reductions is only one of the four broad courses of action
25 described on Page 11 of the bill. You are talking about a

1 reduction of tax rates or fees applied within the enterprise
2 zone. The second is an increase in the level or efficiency
3 of local services in the enterprise zone. For example, crime
4 prevention.

5 The third is actions to reduce, remove, simplify, or
6 streamline government requirements applied within the zone,
7 and finally, there is the involvement in the program by
8 private entities, organizations, neighborhood associations,
9 and community groups, including a commitment from private
10 entities to provide jobs and job training and technical,
11 financial, and other assistance to residents, employers, and
12 employees.

13 So, it is only one of the four general, broad courses of
14 action. The program is very flexible. What we are really
15 asking the cities to do is to take a look at their districts,
16 identify what the problems are, what are the impediments,
17 what is it that caused that area to be distressed in the
18 first place, and then when they do their homework and they
19 come up with a strategy which takes into account the assets
20 they have, whether it be transportation proximity or a good
21 labor force or whatever, and puts together a strategy, we
22 will then give them the kicker of the massive tax credits.

23 Senator Bradley: So the local municipality need not have
24 tax abatement if it has a sufficiently attractive investment
25 package outside of it.

1 Mr. Sloame: Yes, thank you.

2 The Chairman: Senator Pryor.

3 Senator Pryor: Yes. Thank you, Mr. Chairman.

4 Would HUD at this point -- I do not have an amendment
5 proposed, but would HUD at this point be opposed or have
6 objection to someone in addition to the HUD Secretary making
7 the final designation? For example, the HUD Secretary plus
8 someone designated by the House and someone designated by the
9 Senate, assuming from the private sector. Maybe the House
10 would designate the president of the National League of
11 Cities, and the Senate would designate maybe someone from the
12 Governors' Association, something basically to dilute that
13 particular authority or spread it out a little more. Would
14 you oppose anything like that?

15 Mr. May: Well, Senator, we do provide, as you know, in
16 the legislation for a fairly broad consultation process with
17 relevant cabinet officers, but I think that the philosophy of
18 the legislation is that the buck has to stop with an
19 appropriate executive agency head, and that the Secretary of
20 HUD was the appropriate one, and we really feel it ought to
21 be focused on one person to make that final decision.

22 Senator Pryor: Let me say that I said earlier in my
23 remarks I assume I will vote for this. I have been sitting,
24 listening to some of the questions, and I would like to
25 reserve now on that vote. I still may vote for it, but I may

1 not. I can see us getting into a situation here, and I guess
2 I am obsessed with the politics of this thing, and it cuts
3 both ways. Let us say, for example, in the state of
4 Arkansas, I know that municipality boundary lines may not be
5 the determination finally of areas of possible designation,
6 but just choosing four towns or areas, Magnolia, Walnut
7 Ridge, Eureka Springs, Mountain Home, Arkansas, all have a
8 project. It gets to Washington. It gets to the Secretary's
9 desk, and sort of by then it is decided that maybe our state
10 will get one, perhaps two at the most. Let us say they will
11 get one ultimately. And let us say Walnut Ridge gets the
12 designation. Those other three areas will never be convinced
13 that Senator Pryor and Senator Bumpers and whoever were
14 involved in this process. They will never be convinced that
15 we did not favor one to the exclusion of the others. And I
16 think that puts us in an impossible position, and that is why
17 I think that we ought to consider the two people from the
18 public sector in helping make these designations.

19 Frankly, I think one of them I would recommend right now
20 might be the Pope, because I do not think there is going to
21 be any easy way to do this. It will have to be someone
22 beyond any political consideration or political judgment, I
23 think. Yes, sir.

24 Mr. Sloame: Senator Pryor, I think in the first
25 instance, given the requirement that both a city and a state

1 jointly nominate an enterprise zone for consideration by the
2 Secretary of HUD, we would hope that the governor of Arkansas
3 in his wisdom would select only those, would make the initial
4 selection or screening out so that we do not get into that
5 problem. So I think that is one of the reasons why we have a
6 joint city-state designation, in addition, of course, to the
7 prime reason of forcing the cities and states to get together
8 and talk to each other.

9 Senator Pryor: We have a fine governor down there. In
10 fact, he testified Friday. He is a good friend, Governor
11 Clinton. And Governor Clinton has to run again next year.
12 Are you going to see Governor Clinton or any other governor
13 turn down applications for areas to the exclusion of the
14 others? I do not think the system works that way. It might
15 be nice if it did, but I do not think that is the way it is
16 going to be in practical application.

17 Mr. Sloame: Perhaps so, Senator, but --

18 Senator Pryor: He got beat once, and he does not want to
19 get beat again. I know. I am just raising these concerns.
20 I am not trying to pick. But I think we have some pretty
21 serious problems with this.

22 The Chairman: Thank you, Senator Pryor. I wonder if we
23 could have for the record how many states now have enacted
24 enterprise zone legislation. Is it 17, 13?

25 Mr. Sloame: Sixteen states have already enacted

1 legislation, and I believe another 16 have legislation
2 pending.

3 The Chairman: Do you know the 16 states offhand? I know
4 my state has. I think Louisiana has. I am not certain about
5 other states, but apparently at least on the state level they
6 must think there is some merit to the concept. I certainly
7 believe -- in fact, we will ask the staff to continue to look
8 at questions raised by Senator Long, so maybe Mr. Gates and
9 Mr. Peeber and others, between now and the time this final
10 action will go through one more time to make certain we will
11 not have egg on our face in a couple of years when someone
12 rips off the taxpayers.

13 Mr. Sloame: In alphabetical order, the first state is
14 Arkansas, Connecticut, Florida, Georgia, Illinois, Indiana,
15 Kansas, Kentucky, Louisiana, Maryland, Minnesota,
16 Mississippi, Missouri, Ohio, Rhode Island, and Virginia.

17 The Chairman: And there are 16 states in which it is
18 pending?

19 Mr. Sloame: Fourteen states with 1983 new legislation
20 pending include California, Colorado, Hawaii, Massachusetts,
21 Michigan, New Jersey, New York, Oklahoma, Oregon,
22 Pennsylvania, Texas, Tennessee, Washington, and Wisconsin,
23 and there are an additional eight states with 1983 amendments
24 to existing legislation, Connecticut, Illinois, Kansas,
25 Maryland, Minnesota, Missouri, Rhode Island, and Virginia.

1 Those are the other states that have enacted it previously.

2 The Chairman: Let me again generalize, but are they
3 pretty much in step with what we propose in this legislation?

4 Mr. Sloame: Generally speaking, yes. We work with the
5 various states. We give them some drafting assistance. We
6 show them the different types of legislation that have been
7 passed around the country, and we certainly are acquainting
8 them with the parameters and details of the federal
9 enterprise zone legislation. So, I would say in general they
10 are compatible with the federal legislation.

11 The Chairman: And I would ask that we include in the
12 record at this point a staff analysis of this legislation.
13 Are there other amendments to this particular bill?

14 Senator Chafee: Mr. Chairman, I would just like to point
15 out one thing. That deals with the -- on the last of Title
16 I, Section 104(c), it talks about designation of an
17 enterprise zone shall not constitute a federal action for
18 purposes of applying the requirements of NEPA, in other
19 words, the environmental protection laws. That is true. But
20 I think it is also important that that does not mean that you
21 disregard the environmental laws when a section is
22 designated. In other words, you do not have to have an
23 environmental impact statement for the designation, but still
24 you must observe the environmental laws.

25 I would like that to be put in report language if I

1 could, Mr. Chairman, to make that clear.

2 The Chairman: Is there any objection to that?

3 [No response.]

4 The Chairman: Any other material that we might want to
5 include in the report language, we can still do, but I think
6 you understand the thrust of the question, whether from
7 Senator Long, Senator Symms, Senator Pryor, or others. We
8 just do not want to get into another model cities type
9 program where there is a lot of criticism, justified
10 criticism, and I am certain that there is always someone
11 going to say politics are involved. I think Senator Pryor's
12 comments were well intended, and not directed at any
13 Administration, but I am certain you are trying to safeguard
14 from any such charge. If you have any problem in deciding
15 whether or not it is political, just check with me and
16 Senator Long. We can help you with it.

17 [General laughter.]

18 The Chairman: If there are no other amendments, I wonder
19 if we might agree to this legislation. We do not have any
20 revenue bill to attach it to. I guess there are enough of us
21 to act on the legislation. Is that correct?

22 Mr. De Arment: That is correct, Senator.

23 The Chairman: Could we call the roll, and then have the
24 absentees recorded?

25 Mr. De Arment: Mr. Packwood.

1 [No response.]
2 Mr. De Arment: Mr. Roth.
3 [No response.]
4 Mr. De Arment: Mr. Danforth.
5 Senator Danforth: Aye.
6 Mr. De Arment: Mr. Chafee.
7 Senator Chafee: Aye.
8 Mr. De Arment: Heinz.
9 [No response.]
10 Mr. De Arment: Wallop.
11 [No response.]
12 Mr. De Arment: Durenburger.
13 Senator Durenberger: Aye.
14 The Chairman: Mr. Wallop, aye.
15 Mr. De Arment: Armstrong.
16 [No response.]
17 Mr. De Arment: Symms.
18 Mr. Symms: No.
19 Mr. De Arment: Grassley.
20 Senator Grassley: Aye.
21 Mr. De Arment: Long.
22 Senator Long: Pass.
23 Mr. De Arment: Bentsen.
24 [No response.]
25 Mr. De Arment: Matsunaga.

1 [No response.]

2 Mr. De Arment: Moynihan.

3 [No response.]

4 Mr. De Arment: Baucus.

5 [No response.]

6 Mr. De Arment: Boren.

7 [No response.]

8 Mr. De Arment: Bradley.

9 Senator Bradley: Aye.

10 Mr. De Arment: Mitchell.

11 [No response.]

12 Mr. De Arment: Pryor.

13 Senator Pryor: No.

14 Mr. De Arment: Mr. Chairman.

15 The Chairman: Aye.

16 Heinze is around somewhere. He wants to vote aye, but I
17 do not have any other proxies. }

18 There are eight ayes and two nays and one pass, and the
19 absentees may record their votes.

20 Now, the next item on the agenda, I know it is five after
21 12:00, and I want to also thank Senator Boschwitz for being
22 here this morning as one of the "pioneers" in this effort.
23 We appreciate your attendance. We hope we can move this
24 legislation along.

25 Senator Boschwitz: Mr. Chairman, if I may say just a

1 short word, I appreciate some of the problems Senator Long
2 has enunciated during the course of the morning. I think
3 these enterprise zones, as they will be carved out of
4 portions of whether it be New Orleans, Minneapolis, or the
5 South Bronx, are just going to be portions of those cities
6 where insurance and police protection is not now available,
7 and where there probably is not a car wash or shoe factory
8 that Senator Symms is concerned about, and the important part
9 of it really is what Senator Bradley touched upon, and that
10 is the local tax abatement. All of the tax advantages given
11 by this bill are really tax advantages that apply in the
12 event profit is made, and the tax abatement that will be
13 given locally will be as strong an incentive to come into the
14 area, because those will be expenses that will be paid in any
15 event, property taxes, interest, and things like that.

16 So, I think that some of the fears expressed about the
17 legislation are legitimate, because sometimes the best
18 intentioned legislation goes askew, but hopefully that will
19 not be in this case. I think one of the strengths of this
20 legislation is, there are relatively few enterprise zones
21 allowed each year, so they will not proliferate and be just
22 like industrial parks in every town and village. I share the
23 Senator from Kansas, the Chairman's feeling that politics
24 should not enter into this whole thing, and to the same
25 degree he feels that way, I feel that way as well.

1 The Chairman: Thank you, Senator Boschwitz. We want to
2 thank the HUD representatives, and we might convey the word
3 to Secretary Pierce that at least the Committee has approved
4 it. The next step may be up to Secretary Pierce. Mr.
5 Chapoton? Is Secretary Chapoton present? Our next item on
6 the agenda -- I am not certain how long it will take to
7 dispose of it -- is tuition tax credits, and I would say at
8 the outset I know this is hardly controversial. We were
9 through this when, Rod, last September?

10 Mr. De Arment: Yes, last fall.

11 The Chairman: So we have gone through this exercise. I
12 know of the strong opposition on this Committee to tuition
13 tax credits and strong support on this Committee for tuition
14 tax credits. I would like to determine, if we can -- we
15 approved a bill essentially last year that addressed some of
16 the concerns raised by Senator Bradley in the discrimination
17 area, those raised by myself and others as far as
18 refundability. I think Senator Grassley had some concerns.
19 Senator Chafee had some concerns. I wonder if we might at
20 least start on tuition tax credits, and see how far we can go
21 in the next 20 minutes. Maybe we will start today with a
22 summary, Mr. Chapoton, or whoever is going to, to sort of
23 quickly summarize what we propose to do, what the President
24 proposes to do in the tuition tax credit legislation.

25 Mr. Brockway: Yes, Mr. Chairman. The bill, S. 528,

1 provides a non-refundable tuition tax credit as 50 percent of
2 the tuition to elementary and secondary schools up to a
3 maximum credit of \$100 in 1983, \$200 in 1984, and \$300 in
4 1985 and thereafter. For 1983, you could not take into
5 account in your estimated tax payments, so the effect, the
6 revenue effect would slip into 1984, and the program has to
7 be provided by a full-time elementary or secondary school.
8 It has to be privately operated, and it has to be a 501(c)(3)
9 organization. In the effective date you provided last year's
10 result to the amendments before the legislation could go into
11 effect, either Section 501(c)(3) would have to provide
12 explicitly that you could not have racial discrimination and
13 qualify for tax exemption or the Supreme Court would have to
14 rule in the Bob Jones and Goldsboro cases that a school could
15 not qualify for tax exemption and therefore for this
16 legislation if it maintained a racially discriminatory
17 policy.

18 There is also a separate procedure, as in the legislation
19 last year, that would provide that if a student or other
20 person made a complaint of a racially discriminatory act or
21 policy or expression of policy by a school, that the attorney
22 general could go through a declaratory judgment procedure
23 that would deny the credit for the year in which the District
24 Court entered a decision, a declaratory judgment that such
25 discriminatory practice existed. There would be no credit

1 allowed for that school until the school came forward and
2 established that the discriminatory practice or program was
3 eliminated.

4 Under the bill generally, the revenue effects of the bill
5 as introduced would result in a revenue cost for the 1984
6 fiscal year of \$245 million, in 1985 \$526 million, in 1986
7 \$753 million, in 1987 \$779 million, in 1988 \$763 million.
8 And as I say, this would go into effect for tuition paid
9 after July 1 of this year.

10 The Chairman: Now, could I ask, have you finished?

11 Mr. Brockway: Yes, Mr. Chairman.

12 The Chairman: How does this explanation differ from the
13 bill approved by this Committee last year?

14 Mr. Brockway: There are three other provisions, or three
15 differences from the bill last year. One, the bill as
16 approved by the Committee last year would not have allowed
17 tuition credit for tuition paid to a school that had an
18 admission policy discriminating against handicapped
19 children. That is one provision not in this bill.

20 Second, last year's bill would have required that tuition
21 be paid to a school that satisfied state compulsory
22 attendance laws. And third, that the phase-out in this
23 legislation is \$40,000. You get a full credit up to AGI of
24 \$40,000, and it is phased out so that there is no credit for
25 AGI in excess of \$60,000. Last year's bill, they reported

1 out the phase-out from \$40,000 to \$50,000.

2 The Chairman: Plus I think we also agreed last year
3 there would be a Committee amendment on refundability.

4 Mr. Brockway: Correct.

5 Senator Bradley: Mr. Chairman?

6 The Chairman: Mr. Bradley.

7 Senator Bradley: I would hope that we could adopt the
8 same Committee amendment on refundability to be added when
9 the bill comes to the floor. I know the sentiment of the
10 Committee last year was for refundability, but that because
11 of the jurisdictional problem, the way we would have to do it
12 is do it as a Committee amendment. I would hope we would not
13 do that.

14 The Chairman: Right. I think those of us who support
15 tuition tax credits, nearly everyone supports refundability.
16 Otherwise, you will not benefit low income families, and if
17 that is the purpose of the legislation, I do not know what
18 the revenue estimates are on refundability, Mr. Chapoton.

19 Mr. Chapoton: The revenue estimates on the fiscal year
20 basis are \$8 million in fiscal 1984, \$22 million in fiscal
21 1985, \$33 million in each of 1986 and 1987.

22 The Chairman: And as I recall, it seemed to me we were
23 going to make certain that even though that is an added cost,
24 it would be paid for within the structure of the legislation
25 by -- I do not remember how we did it.

1 Mr. Chapoton: That was the point in dropping the upper
2 limit on the phase-out from 60 to 50.

3 The Chairman: Was that the Grassley amendment? Is that
4 the same amendment you offered?

5 Senator Grassley: Yes, and I will offer it today.

6 Mr. Brockway: The bill originally had a phase-out from
7 \$50,000 to \$75,000. You scaled it down to save some revenue,
8 and you added an amendment from \$40,000 to \$60,000 phase-out
9 as this bill was introduced, and it was further scaled down
10 to a phase-out from \$40,000 to \$50,000.

11 Senator Danforth: Mr. Chairman, I can remember vaguely
12 asking last fall why such bargain basement costs for
13 refundability. Eight million for one year for refundability,
14 going up to \$33 million in 1985? It seems to me to be so
15 tiny, that is less than \$1 million at maximum cost to the
16 program. It is about what, \$700,000 per state on the
17 average.

18 Mr. Brockway: The \$8 million is just because of the
19 fiscal year split. The first year, in effect --

20 Senator Danforth: But going out after that, in 1985, a
21 \$300 credit?

22 Mr. Brockway: I think that just comes from the fact that
23 there are relatively few people in that category overall, so
24 that is one of the reasons.

25 Senator Danforth: Let us see how many that would work

1 out to. That would be seven, that would be about -- the
2 average state would seem to me to work out at about 2,300
3 kids for whom there would be a refundable credit. Do you
4 mean to say that private schools and church schools in a
5 state the size of Missouri, which is about average size,
6 would only have 2,300 kids in these schools?

7 Mr. Brockway: I do not think you can take the \$300,
8 Senator. It is just that the data indicates that relatively
9 low income people, those people who would qualify for a
10 refundable credit, also tend to go to the church supported
11 schools which are the schools which tend to have tuition
12 below this cutoff point. So you may have quite a number of
13 more people than that who would still qualify for
14 refundability than your numbers suggest. I think we may have
15 a number of -- our numbers indicate about 80,000 families
16 would qualify for some refundability.

17 Senator Danforth: For some refundability?

18 Mr. Brockway: Not necessarily 300. If the tuition was
19 lower than \$300, for example, they would not have a \$300
20 refund, or they may have.

21 Senator Danforth: Is there such a thing as a school with
22 a tuition less than \$300?

23 Mr. Brockway: I am sorry. Less than six. Yes. There
24 are quite a few church-supported schools.

25 Senator Danforth: Would they not automatically increase

1 it to get up to the limit?

2 Mr. Brockway: The credit is only 50 percent of tuition,
3 so if you have many low income families in this school
4 district, and if you were to increase tuition to cover that
5 amount, they would still have to pick up half the costs, and
6 it would still be a burden on them.

7 Senator Danforth: Suppose the tuition is now \$300.
8 Would they not automatically increase it to \$600?

9 Mr. Brockway: That would result still. Of that \$300
10 increase, \$150 would have to be paid for by the parents.

11 Senator Danforth: Why?

12 Mr. Brockway: Because the credit is only 50 percent of
13 the amount they pay, so right now --

14 Senator Danforth: Then they would pay \$600.

15 Mr. Brockway: If right now the tuition is \$300, and the
16 parents are paying the full \$300, the credit would allow them
17 now a credit for \$150. Assuming you enact the legislation,
18 if the school increased, so the parent were paying \$150 and
19 the Treasury would be paying \$150, if they increased the
20 tuition up to \$600, the parent would then be paying \$300, and
21 the general revenue would, and so what you may have still,
22 just the same number of people involved, but you would not be
23 able to get any increased students to come in if you were
24 trying to provide an incentive for them to go to the school.

25 Senator Danforth: Right now, if the cost is \$300, then

1 the parent is paying \$300.

2 Mr. Brockway: That is correct.

3 Senator Danforth: And if we had a tuition tax credit,
4 and the school increased the tuition from \$300 to \$600, the
5 parent would be paying half, and the federal government would
6 be paying half, correct?

7 Mr. Brockway: That is correct.

8 Senator Danforth: So the parent would be paying \$300,
9 the same amount the parent paid before.

10 Mr. Brockway: That is correct, but it would still be
11 \$150 more than they would be paying if the school did not
12 increase its tuition.

13 Senator Danforth: No.

14 Mr. Brockway: There will clearly be increases in
15 tuition, but we have not assumed that everyone would
16 automatically go up to that.

17 Senator Danforth: Let me say I am for the tuition tax
18 credit, but as I will make the point later, I do not know
19 whether it will be today or not, I think the government
20 should start facing up to the costs of programs, and we
21 should start paying for them, and that is going to be an
22 amendment I am going to suggest, but if we start projecting
23 that the cost of refundability for the tuition tax credit is
24 \$8 million the first year, \$22 million the second, and \$33
25 million every year thereafter, that to me is just

1 outrageous. That is so miniscule. And I would hope we would
2 look at that again before we have to make a decision on
3 refundability. I like the concept of a tuition tax credit.
4 I like the concept of refundability. But one way that we get
5 into these traps is, we constantly put new programs into
6 effect and tell ourselves that it will all be hunky dory
7 because the cost is going to be so small. I wonder what the
8 projections were with Medicare and Medicaid, and the various
9 other programs we got into, compared to reality.

10 Senator Durenberger: Nine billion by 1990.

11 Senator Danforth: For what, Medicare? And in fact it
12 will be over \$130 billion, will it not?

13 Senator Durenberger: Over \$100 billion.

14 Senator Danforth: And I would like somebody, before we
15 have to decide on refundability, to come up with an accurate
16 and realistic cost. Thirty-three million is obviously not
17 realistic. It is obviously inaccurate. And then let us see
18 how we are going to pay for it. And the amendment I will
19 offer is the same I offered last year. That is, if we are
20 going to have a program and spend money, let us figure out
21 and earmark before it goes into effect precisely where the
22 money is going to come from, either increased revenue or
23 decreased spending.

24 We have ourselves in a situation in this government that
25 we cannot even collect taxes, as the Chairman has pointed out

1 many times already. We have a total stalemate with the
2 Administration right now on a budget resolution. We are
3 looking at deficits of \$200 billion, and we are sitting here
4 blandly putting in place a program with a cost of a quarter
5 of a billion, half a billion, to three-quarters of a billion
6 dollars, with this tiny projection of the cost of
7 refundability, with absolutely no idea how we are going to
8 pay for it.

9 I would hope, Mr. Chairman, we will not vote on this
10 today, that we will be finding out the true cost of
11 refundability, and also we will be considering the mechanism,
12 and I have one as a matter of fact in the amendment for how
13 we will pay for this program when we put it into effect.

14 The Chairman: I wonder if Secretary Chapoton might have
15 the information now, but if not, he could provide that.

16 Mr. Chapoton: No. Senator Danforth, we are not
17 supporting, as I believe you know, refundability. We have
18 not proposed it as a part of our bill, and we would like to
19 keep it out of this legislation. We did review the figures
20 after our discussion last time, and we do think those figures
21 are accurate. There are relatively few families who are
22 affected by the non-refundability portion of our bill. I
23 guess arguments, disagreements could certainly exist over
24 whether schools will increase their tuition, but as Mr.
25 Brockway pointed out, it would be a burden on the parent. It

1 is not as if they can do it and make the federal government
2 pay for it, but we have gone over those figures, and it is a
3 low number of families, about 80,000 families, we assume, are
4 cut out of the tuition tax credit by the lack of
5 refundability.

6 The Chairman: As I understand it, Senator Boren has an
7 amendment, a series of amendments.

8 Senator Boren: Senator Chafee and I both have several
9 amendments.

10 Senator Chafee: Mr. Chairman, as you know, I have been
11 less than enthusiastic about this measure.

12 The Chairman: Right.

13 Senator Chafee: And I see no reason not to proceed with
14 the adoption of the refundability amendment here. I think
15 the whole bill is bad, but we might as well do what we can to
16 make it less worse, so I would move the refundability
17 amendment, and I cannot understand the rationale that we
18 would defer it and bring it up on the floor somehow.

19 Mr. De Arment: The rationale for that, Mr. Chafee, is,
20 the Appropriations Committee would get referral if we reported
21 the bill out with a refundability amendment in it. So, to
22 take it directly to the floor without referral to the
23 Appropriations Committee, this Committee last year proposed
24 we adopt a separate Committee amendment offered on the
25 floor.

1 Senator Chafee: I would like to see each Committee of
2 the Congress have a chance to examine this in some detail,
3 and certainly if the shoe were on the other foot, and a bill
4 was coming out from those Committees, was being indulged in,
5 Machavellian tactics, to avoid this Committee having its
6 right to review it, I would not think that was quite proper,
7 and I think that this is legislation -- obviously, you get
8 into refundability, and that means an appropriation each
9 year, and therefore it is perfectly proper that the
10 Appropriations Committee have a chance to examine it in some
11 detail. I cannot understand the rationale that you skirt
12 another Committee because they might look at the
13 legislation. Could someone explain that to me? I am sort of
14 a novice around here.

15 The Chairman: I am not so certain it would be fatal if
16 we flat out adopted the refundability provision, but I think
17 we would want to do it in concert with whatever Senator
18 Danforth has in mind on how we are going to pay for it. You
19 are talking about not paying for just refundability but the
20 entire package.

21 Senator Danforth: Yes, the whole bill.

22 Senator Bradley: Mr. Chairman, on refundability, and I
23 would ask Mr. Chapoton to confirm if this is not correct, if
24 we adopted the Grassley amendment which reduced those
25 eligible to a lower income level, would that not more than

1 cover the cost of refundability?

2 Mr. Chapoton: If memory serves, I think that is correct,
3 but let me look at my figures.

4 Mr. Brockway: The number we have is that refundability
5 using our numbers would be about \$125 million over the 1984
6 through 1988 period, and the effect of the Grassley amendment
7 would be to reduce costs by 204, so that more than pays.

8 Senator Bradley: Then we have met the test.

9 The Chairman: Obviously, this Committee is very closely
10 divided on the whole issue, whether it is refundability or
11 whether all of the amendments will be adopted. I think the
12 vote is probably eleven to nine or ten to ten. There may not
13 be enough votes to report out tuition tax credits, but I have
14 indicated as recently as 10:15 a.m. this morning to the
15 President that we would do our best to at least approve it.
16 We have not got anything to add it to. We cannot report it
17 out by itself. We need a revenue bill from the House of some
18 kind before any floor action can be taken, but I would like
19 to let everyone have their shot at tuition tax credits, and
20 those who oppose it will oppose it tomorrow or next week as
21 strongly as they did today, and those that are for it, I
22 assume, will maintain that stance. We went all through this
23 last, was it September? It seems like last week.

24 I would like to just bring out that record and vote on
25 that record again, and move on to something else, but

1 obviously, everyone has an opportunity to present their
2 amendments. No one will be deprived of that. I would think,
3 though, that there are only six of us here, and what do we
4 need to act on an amendment, seven?

5 Mr. De Arment: Seven.

6 The Chairman: Seven.

7 [General laughter.]

8 The Chairman: So we will take up the Grassley amendment.

9 Senator Grassley: I hope that is a good sign for me.

10 The Chairman: You are key in this deliberation, since it
11 takes seven to operate and you are just number seven.

12 Senator Grassley: Do you mean I can move ahead then with
13 my amendment?

14 Senator Chafee: I thought I had an amendment on before
15 us, Mr. Chairman.

16 Senator Grassley: Then excuse me.

17 Senator Boren: Refundability. Is this refundability? I
18 think we should vote on that. I think it is very important,
19 because if we do not, as we said during the hearings, we are
20 excluding 37 percent of all Hispanic families and 46 percent
21 of all black families with school-aged children from coverage
22 if we leave it at \$10,000 a year or less.

23 Senator Danforth: And we have a wonderful opportunity to
24 provide for how many families, how many black and Hispanic
25 families, Senator?

1 Senator Boren: Forty-six percent of all black families
2 in the country are excluded as now written.

3 Senator Danforth: And we can do it for only \$33
4 million?

5 Senator Chafee: That is a bargain we cannot pass up.

6 Senator Boren: I do not think we can address that, but I
7 would say if we are going to go down this road at all, we
8 certainly should not exclude people from it. If we think we
9 have the resources to shift the money from public schools and
10 elsewhere to pay for this, we ought to apply it to everybody
11 we should not exclude, then you really do admit to the
12 argument of skimming. We are going to just skim off the
13 people in the top from the public schools and leave the
14 rest. So I think it is important we have an opportunity to
15 vote on refundability.

16 The Chairman: If that would make it acceptable to the
17 Senator from Oklahoma and Rhode Island, we would probably do
18 that right off.

19 Senator Chafee: I think I made my position quite clear,
20 Mr. Chairman. I think take a bad bill and try to make it
21 less worse.

22 Senator Boren: That is a fair statement of my position,
23 too.

24 Senator Bradley: Mr. Chairman, it is the Committee's
25 position as of last year that we are for refundability, and I

1 think that Senator Grassley's amendment would address Senator
2 Danforth's concern.

3 The Chairman: What happens if we adopt the amendment?

4 Mr. De Arment: At this point, if we adopt the amendment
5 and then report out a bill with refundability in it, then it
6 is referred to the Appropriations Committee for a period of
7 time.

8 The Chairman: Who decides that?

9 Mr. De Arment: The parliamentarian. The rules provide
10 for that.

11 The Chairman: So it could be a limited time?

12 Mr. De Arment: It is 15 days, but the whole bill,
13 whatever you attach this to will go.

14 The Chairman: I think there is some --

15 Mr. Jones: Mr. Chairman, may I address the question of
16 refundability?

17 The Chairman: No. We know you are against it. We are
18 just trying to work out the procedure.

19 Senator Bradley: Senator Chafee's objection to doing it
20 as a Committee amendment is --

21 Senator Chafee: I do not understand what games we are
22 playing here.

23 The Chairman: I offer as a substitute we do it as a
24 Committee amendment to the Chafee amendment to the bill.

25 Senator Chafee: Well, see if you can explain that. That

1 means what, that we do not adopt it here in the Committee?

2 The Chairman: Right.

3 Mr. De Arment: We could adopt a Committee amendment to
4 provide for refundability.

5 Senator Chafee: In order to skirt the Appropriations
6 Committee?

7 The Chairman: Not to skirt.

8 [General laughter.]

9 Senator Grassley: So as not to complicate the process.

10 Senator Boren: But that helps draw the issue of where we
11 are going to come up with the money. I mean, we are going to
12 have to come up with money to pay for this if we pass it.

13 Senator Bradley: We are going to come up with the money
14 to pay for refundability with Senator Grassley's amendment.
15 It more than pays for refundability. So the issue of paying
16 for it will be answered as soon as we act on Senator
17 Grassley's amendment.

18 Senator Chafee: That is an amazing way of paying for
19 something. You vote an expensive bill, and then you cut it
20 down and say, we have paid for it. No wonder this country is
21 in the shape we are in.

22 Senator Danforth: Mr. Chairman, I am trying to inquire.
23 This would amount to an entitlement program, would it not?

24 Senator Chafee: Sure.

25 The Chairman: I think it might be so characterized.

1 Senator Danforth: Would it be subject to annual
2 appropriations?

3 The Chairman: I do not think so.

4 Mr. De Arment: The refundable credit would.

5 Senator Danforth: It would?

6 Mr. De Arment: The credit itself would not, but all new
7 refundable credits are subject to annual appropriation.

8 Senator Danforth: What if the Appropriations Committee
9 said, we are tired of this and will not appropriate it any
10 more?

11 Mr. De Arment: We have not encountered that situation.
12 We only have one refundable credit that predates the
13 establishment of that rule.

14 The Chairman: What is that, the earned income tax credit?

15 Mr. De Arment: Yes.

16 The Chairman: But if they did decide not to fund it,
17 there would not be any refundable credit.

18 Mr. De Arment: I beg your pardon?

19 The Chairman: If they did decide not to fund it, you
20 would not have a credit.

21 Mr. Brockway: If they decide not to appropriate it, yes,
22 it simply would not be allotted.

23 Senator Bradley: So in effect if we adopted the Dole
24 substitute, while it would come as a Committee amendment, it
25 would be subject to your concern, Senator Chafee, in

1 subsequent years.

2 The Chairman: Is there any objection to the substitute?

3 Senator Chafee: Yes, I object.

4 The Chairman: The Clerk will call the role.

5 Senator Boren: Did you say what this is now, the
6 substitute?

7 Mr. De Arment: This is the Chairman's motion to provide
8 for a Committee amendment to make the tuition tax credits
9 refundable.

10 Mr. Packwood.

11 Senator Chafee: As opposed, I think you might point out,
12 as opposed to a substitute for an amendment that we would
13 adopt here.

14 Mr. De Arment: It is a substitute for having it as a
15 part of the bill.

16 Senator Boren: Would it be part of the bill on the floor
17 then?

18 The Chairman: No, it would be offered as a Committee
19 amendment.

20 Senator Boren: So we would have to vote on it again on
21 the floor. We would not be adopting it.

22 The Chairman: You would get another chance to defeat it
23 on the floor.

24 Senator Danforth: I am perfectly prepared to vote with
25 the Chairman. I believe in refundability, and I think your

1 procedure is all right, but I want to satisfy myself that the
2 figure of \$33 million by 1985 has been reviewed by the
3 Administration in connection with last year's bill, and
4 further, that it has been reviewed by the Administration with
5 respect to this year's bill. Is that correct?

6 Mr. Chapoton: That is correct, Senator Danforth. I do
7 not know -- I cannot now give you the assumption, but we will
8 be happy to supply the assumption to any degree that there is
9 an assumption of increased enrollment in private schools as a
10 result of the tuition tax credit, a slight increase in
11 enrollment. I do not have with me anything on the assumption
12 of increased tuition.

13 Senator Danforth: All I want to do is to assure myself
14 that the Administration has been faced with this question,
15 that it has seriously addressed the question of the cost of
16 refundability not once, but twice, that it has analyzed the
17 statistics, and that it stakes its reputation --

18 [General laughter.]

19 Senator Danforth: -- on this projection. I do not want
20 any waffling figure, any fingers crossed on this. I want to
21 make it absolutely clear today, on May 17th, 1983, that the
22 Reagan Administration is going firmly on record for the
23 proposition that refundability in the tuition tax credit is
24 going to cost \$33 million in 1985 and every year thereafter.

25

1 Mr. Chapoton: Senator, that is our present revenue
2 estimate. It is after review, and I do not know what more I
3 can say than that. It is, as our estimates always are, based
4 upon assumptions of enrollment and assumptions of tuition,
5 and as I said I do not know whether there is an assumption of
6 increased tuition, but it seems to me that would not be
7 unreasonable.

8 Senator Danforth: Does the Administration need any
9 further time to analyze this figure?

10 Mr. Chapoton: I think in view of your strong statement I
11 would not mind having time to review that second assumption,
12 whether tuition is involved. But every time we go back to an
13 estimate such as this, we do not -- they do not change. We
14 review them thoroughly, but most of the consideration that
15 you and I would add to the picture have fully been taken into
16 account.

17 So I will be happy to get back to you in response to the
18 very strong statement you have made, and perhaps that would
19 be the prudent thing to do.

20 Senator Danforth: Well, Mr. Chairman, let me say, I will
21 vote with the Chair in connection with this proposition, on
22 the understanding that the Administration will further
23 analyze this situation and will provide me in writing with an
24 analysis of the cost of refundability and the cost of the
25 entire program, which I intend to place in the Congressional

1 Record when this comes to the floor.

2 Mr. Chapoton: We will be happy to do that, sir.

3 The Chairman: I think the record has indicated the
4 Administration does not support refundability.

5 Senator Boren: Did we ever get the estimates? We asked
6 Mr. Bell for those figures on the demographic changes that we
7 expected in the schools as a result of this. Was that ever
8 provided to us? In other words, how many more white children
9 would go to private schools and how many black and Hispanic
10 students would shift to public schools. Did we ever get
11 those figures?

12 I guess you have to have some assumption on that because
13 of the very low cost that is being projected here. You
14 apparently do not expect many of those minority children to
15 move to private schools. You must have some assumptions on
16 demographic change.

17 Mr. Jones: The report you are referring to, Senator, and
18 you asked us for about two weeks ago, has not been
19 completed. And I told you at that time it would be some time
20 before it was completed; that this was a report focusing on
21 preferences of parents as opposed to any attendance patterns
22 or whatever.

23 There is evidence to suggest that there has been
24 increased enrollment by minorities in private schools,
25 particularly Catholic schools, in the last few years. And I

1 think what you would find if you passed tuition tax credits
2 is, you will find an increased enrollment pattern by
3 Hispanics and blacks.

4 Senator Moynihan: Mr. Chairman, could I just speak to
5 that very briefly to my friend Senator Boren, to say this is
6 a subject with which I have been involved for a quarter of a
7 century, and I have done some of the research and I know some
8 of the numbers.

9 One of the difficulties we have is that of the words we
10 use to describe the different institutions. We say public
11 schools and private schools, and the different regions about
12 which we talk. In the region of the country which I come
13 from, the schools available to children on a free basis or a
14 very small fee basis began in the late eighteenth century and
15 began to receive public moneys about that time, too, on the
16 same basis, as a matter of fact, the Northwest Ordinance --
17 the Continental Congress passed the Northwest Ordinance which
18 set aside one plot in 64 or something like that for higher
19 education.

20 The State of New York acquired lands in the same way and
21 set aside certain shares which went to education. This went
22 to the schools that existed and subsequently came into
23 being. The only schools that existed and came into being
24 were denominational. There were no other schools. There
25 never had existed a nondenominational school. I can say with

1 some confidence, you go back in the western world, and there
2 was no such thing as an elementary or secondary school that
3 was not in some way denominational.

4 In the 1830's a dispute arose about the way some of the
5 state moneys were used and the schools that used the King
6 James Bible in New York City formed themselves into a group
7 called the Public School Society, and the other schools,
8 which shall be nameless, which used the Douay Bible, said we
9 will not join with the public schools.

10 That is where the word "public school" comes from in the
11 United States. There were none of any kind in the old states
12 of the Confederacy until after the War Between the States,
13 although in Senator Long's state the oldest Catholic
14 elementary school goes back to 1717.

15 Now, we all know the word "public school" in Britain
16 means private and we use "public school" for the opposite
17 meaning. It goes back just to the word chosen by a group of
18 schools that said, we will all come together and we will
19 accept public money. That is why in New York City -- I do
20 not know about other states -- we talk about PS-101; that
21 means Public School 101. It goes back to 1830.

22 Now, there is a sense in which -- and I will not say
23 another word -- these have always been, both the original
24 members of the public schools and those schools that did not
25 join them, were all public institutions. They were parochial

1 institutions. They were where the people in neighborhoods
2 went to school and always had for 180 years. These are not
3 new.

4 And with respect to the minority enrollments, these
5 schools are in the greatest main parochial schools, and they
6 enroll the people who live in the neighborhood, and the
7 neighborhoods of New York are now in large measure minority
8 neighborhoods. And that is why in Manhattan, for instance,
9 the largest number of students are what we call minority
10 students. I do not know why they are called minority
11 students, since they are the majority, but they are.

12 Senator Chafee: Well, Mr. Chairman, Senator Moynihan has
13 touched on this historic reference in the past, and if I
14 follow him correctly his point is that there is an historical
15 justification for government support for so-called private
16 schools because that was the origination of schools in this
17 nation. And indeed, in my state there were the private
18 academies which were where children went to school in the
19 early part of the nineteenth century. That may be.

20 But we have seen great changes in our society since then,
21 and if you follow his historic analogy then presumably the
22 integration of schools would not be proper because originally
23 the schools were entirely segregated, if indeed there were
24 any schools at all for minorities.

25 Now, I do not think we want to return to everything that

1 was in the past. For well over 130 years there have existed
2 public schools as we know them. That has been an obligation
3 for society, to support these schools. And we have not
4 dedicated public funds for the support of those attending
5 institutions in the elementary and secondary level that were
6 not controlled by the populace who paid the taxes.

7 And what is being proposed here is a radical departure
8 from anything we were used to in this nation.

9 Senator Moynihan: Would you allow me to say I was not
10 making a justification; I was just making the historical
11 statement that we do not want to get the idea that we are
12 starting up a new school system here. We are proposing to
13 support at the federal level schools that have been there for
14 nearly two centuries.

15 And you may think this a good idea or a very bad idea,
16 but it is not a radically new one.

17 Senator Chafee: I think that is irrelevant. On that
18 basis we might say, let us go back to segregated schools. It
19 is historic for the country. That was the origination. That
20 means nothing in today's society. Obviously, we would not do
21 that, and I do not think we want to hang our hat on something
22 that may have started in the early part of the nation's
23 founding, but is improper to continue in the views of many
24 today.

25 The Chairman: I wonder if I might. I think this is

1 interesting --

2 [Laughter.]

3 The Chairman: -- but I might suggest that this amendment
4 will be pending when we meet again tomorrow morning at 10:00
5 o'clock. And I would hope maybe Senator Boren would offer
6 his en bloc. I understand he has several.

7 Senator Boren: I think they deserve individual
8 consideration and further philosophical discussion, perhaps.

9 The Chairman: I am certain they do. And I know Senator
10 Grassley has an amendment, Senator Danforth does. There are
11 a number of amendments.

12 Senator Durenberger: I have three, Mr. Chairman.

13 The Chairman: So I doubt that we can conclude this
14 before 1:00 o'clock. So let us just adjourn until tomorrow
15 at 10:00 o'clock, to come back on tuition tax credits and
16 maybe finish it tomorrow some time, or the next day.

17 [Whereupon, at 12:50 p.m., the Committee adjourned, to
18 reconvene at 10:00 a.m. on Wednesday, May 18, 1983.]

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SUMMARY DESCRIPTION OF S. 528
(THE EDUCATIONAL OPPORTUNITY AND EQUITY ACT OF 1983)
RELATING TO
TAX CREDITS FOR TUITION EXPENSES

SCHEDULED FOR A MARKUP
ON
MAY 17, 1983
BY THE
SENATE COMMITTEE ON FINANCE

Prepared by the Staff
of the
Joint Committee on Taxation

May 13, 1983

JCX-12-83

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INTRODUCTION

This document provides a description of the provisions of S. 528, the Educational Opportunity and Equity Act of 1983 (introduced by Senators Dole, Packwood, Moynihan, Roth, and D'Amato). S. 528, which has been proposed by the Administration, would provide a nonrefundable tax credit for certain tuition paid to private elementary and secondary schools that have racially nondiscriminatory policies.

The Senate Committee on Finance has scheduled a markup of S. 528 for May 17, 1983. The Committee on Finance held a public hearing on the bill on April 28, 1983.¹

In the 97th Congress, the Senate Committee on Finance reported H.R. 1635, with amendments, a bill that was very similar to S. 528.²

The first part of this document is a summary description of present law. This is followed, in the second part, by a summary description of S. 528. The third part is a brief description of the differences between S. 528 and H.R. 1635 (97th Cong.).

¹ For a more detailed description of the provisions of S. 528, see "Description of S. 528 (the Educational Opportunity and Equity Act of 1983) Relating to Tax Credit for Tuition Expenses" (JCS 8-83, April 26, 1983).

² See, S. Rep. No. 97-576, 97th Cong., 2d. Sess (1982).

I. PRESENT LAW

Tax Benefits for Educational Expenses

Present law does not provide any tax credit or deduction for personal educational expenses. However, in certain cases, taxpayers are entitled to a personal exemption for a dependent, which they could not claim otherwise, because the dependent is a student. Moreover, individuals generally may exclude from gross income certain amounts received as scholarships and fellowships, or amounts received under qualified educational assistance programs. Finally, certain types of "job-related" educational expenses may be deducted.

Other Tax Provisions of Benefit to Education

Some provisions that benefit education, in general, and sometimes students, in particular, include the exclusion from income of gifts, which may comprise a large portion of a student's educational expenses, and the charitable contribution deduction, which allows a deduction for charitable contributions (not tuition payments) to educational institutions. Other provisions, such as the exclusion of interest on State and municipal bonds and the deduction for State and local taxes, indirectly assist publicly supported educational institutions by easing the financial burden of State and local governments.

Effect of Racial Discrimination on the Tax-Exempt Status of Private Schools

The Internal Revenue Service issued a revenue ruling and a revenue procedure in 1971 and 1972, respectively, which state that private schools with racially discriminatory policies as to students will not be recognized as organizations exempt from Federal income tax. These documents also set forth guidelines and recordkeeping requirements for determining whether private schools have adequately publicized their racially nondiscriminatory

³The Congressional Research Service has estimated that school districts benefit from roughly 58 percent of the subsidy associated with the deductibility of property taxes on owner-occupied homes (i.e., \$5,083 million of the \$8,765 million projected revenue loss for FY 83); 29 percent of the subsidy associated with the deductibility of all other nonbusiness State and local taxes (i.e., \$5,817 million of the \$20,060 million projected revenue loss for FY 83); 35 percent of the subsidy associated with the exclusion of interest paid on State and local general obligation bonds (i.e., \$2,800 million of the \$8,000 million projected revenue loss for FY 83); and none of the subsidy associated with the exclusion of interest paid on revenue bonds sponsored by State and local governments.

policies so as to enable them to qualify for tax-exempt status. ⁴

Revenue Procedure 75-50, 1975-2 C.B. 587, sets forth guidelines and recordkeeping requirements for determining whether private schools have racially nondiscriminatory policies. A school's failure to comply with these guidelines ordinarily results in the proposed revocation of the tax-exempt status of the school.

Through provisions enacted as part of annual appropriations' legislation, the Congress has, at various times in the past, forbidden the Internal Revenue Service from developing or carrying out any rulings, procedures, or other provisions concerning tax exemptions for racially discriminatory private schools beyond those that were in effect prior to August 22, 1978.⁵

The issue of whether schools with racially discriminatory policies may qualify for tax-exempt status currently is pending before the Supreme Court of the United States in the cases of Goldsboro Christian Schools, Inc. v. United States (No. 81-1), and Bob Jones University v. United States (No. 81-3). These cases have been argued before the court, but a decision has not yet been announced.

⁴ Rev. Rul. 71-447, 1971-2 C.B. 230 and Rev. Proc. 72-54, 1972-2 C.B. 834. These documents were issued in response to Green v. Connally, 330 F. Supp. 1150 (D.D.C.), aff'd per curiam sub nom. Coit v. Green, 404 U.S. 997 (1971), which held that racially discriminatory private schools are not entitled to the Federal tax exemptions provided for educational organizations and that gifts to such schools are not deductible as charitable contributions by the donors.

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Under the bill, an individual would be allowed to claim a nonrefundable tax credit for 50 percent of the tuition expenses paid during the taxable year to one or more educational institutions for certain dependents who are under age 20 at the close of the taxable year in which the expenses are paid and with respect to whom the individual is permitted to claim dependency exemptions.

Eligible Educational Institutions

The credit would be available only with respect to tuition paid to an institution which:

- (1) provides a full-time program of elementary or secondary education;
- (2) is a privately operated, not-for-profit, day or residential school; and
- (3) is a section 501(c)(3) organization.

Maximum Credit Amount

The maximum credit allowable to a taxpayer with respect to tuition expenses paid on behalf of each dependent would be:

- (1) \$100 in the case of tuition expenses paid or incurred after July 31, 1983, in taxable years beginning in 1983;
- (2) \$200 in the case of tuition expenses paid or incurred in taxable years beginning in 1984; and
- (3) \$300 in the case of tuition expenses paid or incurred in taxable years beginning in 1985 or later.

A special rule would provide that any tuition tax credits available to any taxpayer could not be taken into account in determining the estimated tax of a taxpayer for any taxable year beginning before January 1, 1984, or in determining the number of withholding exemptions to which any taxpayer would be entitled with respect to remuneration paid before January 1, 1984.

Adjusted Gross Income Phaseout

The maximum credit amount would be reduced by a specified percentage of the amount by which the taxpayer's adjusted gross income exceeds \$40,000 (\$20,000 in the case of a married individual filing a separate return). A taxpayer with adjusted gross income of \$60,000 or more (\$30,000 in the case of a married

individual filing separately) could not claim any credit.⁶

Disallowance of Credit with Respect to Amounts Paid to Racially Discriminatory Institutions

No tax credit would be permitted for tuition payments to schools that have racially discriminatory policies.

Under the bill, an educational institution would be considered to have a racially discriminatory policy if it refuses, on account of race (1) to admit applicants as students; (2) to admit students to the rights, privileges, programs, and activities generally made available to students by the educational institution; or (3) to allow students to participate in its scholarship, loan, athletic, or other programs. A racially discriminatory policy would not include failure to pursue or achieve any racial quota, proportion, or representation in the student body. The term "race" would include color or national origin.

A school would be required to file annually with the Internal Revenue Service a statement declaring that it had not followed a racially discriminatory policy and also would have to indicate whether the Attorney General has brought a declaratory judgment action against it during the current or any of the two preceding calendar years. The nondiscrimination statement would be furnished to each person who paid tuition to the school, and a taxpayer claiming the credit would have to attach a copy to his return.

Enforcement Proceedings

Under the bill, the Attorney General would be responsible for determining whether a school followed a racially discriminatory policy.

The Attorney General would be authorized and directed to seek a declaratory judgment against a school after receiving a written allegation of discrimination filed by a complainant against the school and finding good cause. This written allegation would be required to allege with specificity that (1) the school had committed a racially discriminatory act against a student applicant or student within one year preceding the date on which the allegation was made, or (2) that the school had made a

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If the Attorney General decided not to seek a declaratory judgment against the school, he would be required to make available to the complainant the information on which he based his decision, including any relevant information submitted by the school. He would not be required or authorized, however, to make available any information the disclosure of which would violate any Federal or State law protecting personal privacy or confidentiality.

Instead of seeking a declaratory judgment, the Attorney General could, in his discretion, enter into a settlement agreement with a school against which an allegation of discrimination had been made. However, before doing so, the Attorney General would be required to find that the school had been acting in good faith and had abandoned its racially discriminatory policy. A copy of any settlement agreement would be required to be furnished to the complainant whose allegations resulted in the Attorney General's investigation. If the school violated the settlement agreement, then no subsequent allegation would need to be filed before the Attorney General could initiate a declaratory judgment proceeding or commence a proceeding to enforce the terms of the settlement.

Attorney's Fees

The bill would authorize the district court to award costs and reasonable attorneys' fees to a school prevailing in a declaratory judgment proceeding brought by the Attorney General.

Discontinuance of Racially Discriminatory Policy

The bill provides that a school against which a declaratory judgment had been rendered could, at any time after one year from the date of the judgment, file with the district court a motion to modify the judgment to include a declaration that the school no longer followed a racially discriminatory policy. The motion by the school would be granted, and tuition paid to the school that is otherwise qualified would again become eligible for tax credits, unless the Attorney General established that the declaration by the school was false, or that the school had, within the preceding year, (1) committed a racially discriminatory act against a student or applicant, (2) communicated that it followed a discriminatory policy, or (3) engaged in a pattern of conduct to implement such a racially discriminatory policy.

Period of Disallowance of Tax Credits

No credits would be allowed for amounts paid to a school during the period in which a declaratory judgment against the school was in effect. Generally, a declaratory judgment would be effective beginning with the calendar year in which it was entered by the district court, whether or not it was appealed. The period of disallowance would end only if a motion to reinstate credits was granted by the district court. In that event, credits would again be allowed beginning with the year the motion was granted by the district court, whether or not that motion was appealed.

Annual Report by Attorney General

The bill would require the Attorney General to make an annual report to the Congress on his activities regarding enforcement of the anti-discrimination provisions.

Credit Not to be Considered as Federal Assistance

The bill provides that tuition tax credits would not constitute Federal financial assistance to educational institutions or the recipients thereof.

Effective Date

The bill generally would be effective for tuition payments made after July 31, 1983. However, no credits would be allowable until either a final decision of the Supreme Court of the United States or an Act of Congress prohibits the granting of a tax exemption under Code section 501(a) by reason of section 501(c)(3) to private educational institutions maintaining a racially discriminatory policy or practice as to students.

Revenue Effect

It is estimated that the bill would reduce budget receipts by \$245 million in fiscal year 1984, \$526 million in fiscal year 1985, \$753 million in fiscal year 1986, \$779 million in fiscal year 1987, and \$763 million in fiscal year 1988. (Last year, a committee amendment to H.R. 1635 would have made the credit provided by that bill refundable. If S. 528 provided a refundable credit, then the bill would reduce fiscal year budget receipts by \$253 million in 1984, \$548 million in 1985, \$786 million in 1986, \$812 million in 1987, and \$792 million in 1988.)

**III. DIFFERENCES BETWEEN S. 528
AND H.R. 1635 (97TH CONGRESS)**

There are three differences between S. 528 and H.R. 1635 (as reported by the Senate Committee on Finance in the 97th Congress).

Under H.R. 1635:

(1) Credit would not have been allowed for tuition paid to a school having an admissions policy that discriminated against handicapped children;

(2) Credit would not have been allowed for tuition paid to a school attendance at which does not satisfy State compulsory attendance laws; and

(3) No credit would have been allowed for taxpayers with adjusted gross incomes of \$50,000 or more (rather than \$60,000 or more). (S. 1137, introduced by Senator Grassley, contains this adjusted gross income phaseout. S. 1137 would reduce fiscal year budget receipts by \$229 million in 1984, \$491 million in 1985, \$703 million in 1986, \$716 million in 1987, and \$723 million in 1988.)

COMMITTEE ON FINANCE

Executive Session

Tuesday, May 17, 1983

Room SD-215

10:00 a.m.

AGENDA

1. S. 863, The Enterprise Zone Tax Act of 1983 (materials provided previously)
2. S. 528, The Educational Opportunity and Equity Act of 1983 (Attachment A)
3. Increase in the Public Debt; Long Bond Authority (Attachment B)

Tuition Tax Credits

Prepared by the Staff of the Committee on Finance

Present law generally provides no tax credit or deduction for personal educational expenses.

S. 528 would provide a nonrefundable credit for 50 percent of tuition expenses paid to private elementary and secondary schools for certain qualified dependents of the taxpayer. The maximum credit per dependent would be \$100 in 1983, \$200 in 1984, and \$300 in 1985 and subsequent years. The maximum credit amount would be phased down for taxpayers with adjusted gross incomes of greater than \$40,000 and no credit would be allowed for taxpayers with adjusted gross incomes of \$60,000 or more.

For tuition expenses to be creditable, a school could not follow a racially discriminatory policy. An eligible school (i.e., a school that is exempt from taxation under Code section 501(a) as an organization described in Code section 501(c)(3)) would be required to include a statement of its nondiscriminatory policy in any published by-laws, admissions materials, and advertising, and to file annually with the Treasury Department a statement that it has not followed a racially discriminatory policy. Generally, a copy of this statement also would have to be furnished to each individual who pays tuition to the school and be attached to any return on which credits are claimed. In addition, the bill would disallow credits for payments to any school found to be following a racially discriminatory policy in an action brought by the Attorney General under the bill's declaratory judgment provisions.

The bill generally would apply to tuition paid or incurred after July 31, 1983, for taxable years beginning after December 31, 1982. However, no credits would be allowed until either a final decision by the Supreme Court of the United States or an Act of Congress prohibits the granting of a tax exemption under section 501(a) of the Internal Revenue Code by reason of section 501(c)(3) to private educational institutions that maintain a racially discriminatory policy or practice as to students.

SUMMARY DESCRIPTION OF S. 528
(THE EDUCATIONAL OPPORTUNITY AND EQUITY ACT OF 1983)
RELATING TO
TAX CREDITS FOR TUITION EXPENSES

SCHEDULED FOR A MARKUP
ON
MAY 17, 1983
BY THE
SENATE COMMITTEE ON FINANCE

Prepared by the Staff
of the
Joint Committee on Taxation

May 13, 1983

JCX-12-83

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INTRODUCTION

This document provides a description of the provisions of S. 528, the Educational Opportunity and Equity Act of 1983 (introduced by Senators Dole, Packwood, Moynihan, Roth, and D'Amato). S. 528, which has been proposed by the Administration, would provide a nonrefundable tax credit for certain tuition paid to private elementary and secondary schools that have racially nondiscriminatory policies.

The Senate Committee on Finance has scheduled a markup of S. 528 for May 17, 1983. The Committee on Finance held a public hearing on the bill on April 28, 1983.¹

In the 97th Congress, the Senate Committee on Finance reported H.R. 1635, with amendments, a bill that was very similar to S. 528.²

The first part of this document is a summary description of present law. This is followed, in the second part, by a summary description of S. 528. The third part is a brief description of the differences between S. 528 and H.R. 1635 (97th Cong.).

¹ For a more detailed description of the provisions of S. 528, see "Description of S. 528 (the Educational Opportunity and Equity Act of 1983) Relating to Tax Credit for Tuition Expenses" (JCS 8-83, April 26, 1983).

² See, S. Rep. No. 97-576, 97th Cong., 2d. Sess (1982).

I. PRESENT LAW

Tax Benefits for Educational Expenses

Present law does not provide any tax credit or deduction for personal educational expenses. However, in certain cases, taxpayers are entitled to a personal exemption for a dependent, which they could not claim otherwise, because the dependent is a student. Moreover, individuals generally may exclude from gross income certain amounts received as scholarships and fellowships, or amounts received under qualified educational assistance programs. Finally, certain types of "job-related" educational expenses may be deducted.

Other Tax Provisions of Benefit to Education

Some provisions that benefit education, in general, and sometimes students, in particular, include the exclusion from income of gifts, which may comprise a large portion of a student's educational expenses, and the charitable contribution deduction, which allows a deduction for charitable contributions (not tuition payments) to educational institutions. Other provisions, such as the exclusion of interest on State and municipal bonds and the deduction for State and local taxes, indirectly assist publicly supported educational institutions by easing the financial burden of State and local governments.

Effect of Racial Discrimination on the Tax-Exempt Status of Private Schools

The Internal Revenue Service issued a revenue ruling and a revenue procedure in 1971 and 1972, respectively, which state that private schools with racially discriminatory policies as to students will not be recognized as organizations exempt from Federal income tax. These documents also set forth guidelines and recordkeeping requirements for determining whether private schools have adequately publicized their racially nondiscriminatory

³The Congressional Research Service has estimated that school districts benefit from roughly 58 percent of the subsidy associated with the deductibility of property taxes on owner-occupied homes (i.e., \$5,083 million of the \$8,765 million projected revenue loss for FY 83); 29 percent of the subsidy associated with the deductibility of all other nonbusiness State and local taxes (i.e., \$5,817 million of the \$20,060 million projected revenue loss for FY 83); 35 percent of the subsidy associated with the exclusion of interest paid on State and local general obligation bonds (i.e., \$2,800 million of the \$8,000 million projected revenue loss for FY 83); and none of the subsidy associated with the exclusion of interest paid on revenue bonds sponsored by State and local governments.

policies so as to enable them to qualify for tax-exempt status. ⁴

Revenue Procedure 75-50, 1975-2 C.B. 587, sets forth guidelines and recordkeeping requirements for determining whether private schools have racially nondiscriminatory policies. A school's failure to comply with these guidelines ordinarily results in the proposed revocation of the tax-exempt status of the school.

Through provisions enacted as part of annual appropriations' legislation, the Congress has, at various times in the past, forbidden the Internal Revenue Service from developing or carrying out any rulings, procedures, or other provisions concerning tax exemptions for racially discriminatory private schools beyond those that were in effect prior to August 22, 1978.⁵

The issue of whether schools with racially discriminatory policies may qualify for tax-exempt status currently is pending before the Supreme Court of the United States in the cases of Goldsboro Christian Schools, Inc. v. United States (No. 81-1), and Bob Jones University v. United States (No. 81-3). These cases have been argued before the court, but a decision has not yet been announced.

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Revenue Effect

It is estimated that the bill would reduce budget receipts by \$245 million in fiscal year 1984, \$526 million in fiscal year 1985, \$753 million in fiscal year 1986, \$779 million in fiscal year 1987, and \$763 million in fiscal year 1988. (Last year, a committee amendment to H.R. 1635 would have made the credit provided by that bill refundable. If S. 528 provided a refundable credit, then the bill would reduce fiscal year budget receipts by \$253 million in 1984, \$548 million in 1985, \$786 million in 1986, \$812 million in 1987, and \$792 million in 1988.)

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Increase in the Public Debt Limit

Prepared by the Staff of the Committee on Finance

The Reagan administration has requested an increase in the public debt ceiling to cover anticipated financing needs of the Federal Government through September 30, 1983. The present ceiling on the public debt is \$1,290.2 billion and is comprised of the permanent debt ceiling of \$400 billion plus a temporary ceiling of \$890.2 billion. The temporary ceiling expires September 30, 1983. However, the administration anticipates that the present ceiling on the public debt will be exceeded by the end of May.

The Treasury Department has testified that an increase of \$99 billion in the debt ceiling would be sufficient to cover the Government's financing needs through the end of fiscal year 1983. This would raise the debt ceiling to \$1,389.2 billion. The same figure is recommended as appropriate for fiscal year 1983 in H. Con. Res. 91, the House-passed budget resolution.

Long Bond Authority

The Treasury Department also has recommended an increase in the amount of bonds that may be issued without regard to the statutory limit of 4-1/4 percent on the interest rate such bonds may bear. Currently up to \$110 billion may be issued without regard to the 4-1/4 percent limit, and Treasury estimates that the present limit will be reached early in 1984. Treasury projects that an increase of \$40 billion in the exception from the 4-1/4 percent limit will be adequate through 1984.

Ways and Means Committee Action

On May 12, 1983, the Committee on Ways and Means agreed to report legislation to raise the ceiling on the public debt to \$1,389.0 billion. This is a permanent increase in the debt ceiling, designed to carry through to the end of fiscal year 1983, but without specifying an expiration date of September 30, as is usually the case. The Committee also agreed to a \$40 billion increase in the exception to the 4-1/4 percent limit on the interest rate that may be paid on bonds.