

UNITED STATES SENATE

HEARINGS

BEFORE THE COMMITTEE

on
FINANCE

EXECUTIVE SESSION

Thursday, June 18, 1981

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EXECUTIVE SESSION

Thursday, June 18, 1981

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

The committee met, pursuant to notice, at 10:15 a.m.,
in room 2221, Dirksen Senate Office Building, Hon. Robert J.
Dole, (chairman), presiding.

Present: Senators Dole, Danforth, Chafee, Heinz,
Wallop, Armstrong, Symms, Grassley, Long, Byrd, Bentsen,
Matsunaga, Baucus, Boren, Bradley and Mitchell.

P R O C E E D I N G S

1
2 The Chairman. The committee will come to order.

3 I might say at the outset that we hope to begin today
4 making some decisions that will lead to the enactment of
5 major tax legislation in the weeks ahead and prior to the
6 August 1 recess date.

7 President Reagan announced his economic program in
8 February. He outlined his basic tax program as long ago
9 as last summer. Last summer, this committee considered and
10 reported out tax legislation dealing with many of the issues
11 we are examining again this year.

12 I think the members will find in the material handed
13 out this morning, that many of the items were in part in
14 the Senate bill last year.

15 So, I think based on the President's recent statement
16 and on statements of others, in both parties and the Congress,
17 it is time now that we move ahead.

18 There is some action now on the House side, quite
19 different from that recommended by the Administration.

20 We would hope that in this committee, we could report
21 out the President's program.

22 We concluded our hearings on May 21. So, it has been
23 some time since the last hearing was held. It is nearly a
24 month later now. I hope we can move ahead.

25 I would say we are not certain about the session

1 tomorrow, depending upon whether or not the Senate is in
2 session.

3 Starting next Tuesday, we would hope to meet in the
4 morning and afternoon, in an effort to report out a bill
5 next week.

6 I think there are sound reasons for that. Next
7 Friday starts a recess period. Then, we are back only for
8 about three weeks before at least a scheduled August recess.

9 It would seem to me, if we plan to meet that date,
10 and I think everyone wants to meet that date, if not it is
11 going to be difficult to provide any tax relief, for anybody
12 in 1981.

13 So, I would hope we could keep that in mind as we
14 proceed today and later on this next week.

15 I think the ground work has been laid. I hope every-
16 body has a copy of the -- what we refer to as the bipartisan
17 tax reduction program.

18 I would only take a minute to explain, on the first
19 page of the bipartisan tax reduction program there is an
20 index of items that we believe that will certainly find
21 their way into legislation that I will introduce today or
22 tomorrow or Monday.

23 There are about five items where there is still some
24 negotiation under way. We are not certain whether or not
25 they will be in a bill which will be introduced.

1 But, they are under active discussion, active con-
2 sideration with Administration officials. It would be my
3 hope that resolution of those five items can be accomplished.

4 Now, I don't suggest there aren't other meritorious
5 amendments that members have had for some time that they
6 would like to add to this proposal. But, I would also
7 indicate that the Administration has indicated to me that
8 they prefer not to load this bill up and that there will be
9 another opportunity.

10 I would hope that those who have amendments, and I
11 am certain there are many, would make that known to Mr.
12 Lighthizer, our Chief Counsel, as we make preparations to
13 see whether or not we can move on a second package.

14 There will be amendments offered. I do not see any
15 -- I certainly don't have any quarrel with that. But, we
16 would hope we have covered enough areas that are of
17 interest to members, that we might be able to report this
18 bill out, and hopefully, not later than next Thursday
19 afternoon, without any radical changes.

20 So, as we proceed today, I would hope we could have
21 votes on one or two items.

22 Before we do that, Senator Long, do you wish to make
23 a statement, and then we will ask Mr. Chapoton to sort of
24 go through very quickly, pretty much what you did the other
25 day.

1 Senator Long. Mr. Chairman, let me just say here is
2 the problem we will find. One will have an amendment that
3 will be said to be a good amendment. He will be told that
4 the budget or the Treasury can't stand that much Revenue
5 loss, and the reason it can't stand that much is because
6 someone else has his amendment in there already.

7 We started out on the assumption that we are going
8 to have a 10-10-10, and a 10-5-3, and therefore, the budget
9 could not contemplate further cuts.

10 Now my thought is that we really shouldn't judge any
11 of these items based on who got there first. It ought to
12 be based on which makes the most sense, which has the
13 higher priority and that would be true, I would think, of
14 some suggestions that have not found their way into this
15 memorandum you submitted to us.

16 I would hope we would do business on the basis that
17 those things we would like to suggest be a part of the
18 bill would be considered in connection with all of this,
19 and in the wrapping up process, we would simply release
20 whatever we have inside the bottle.

21 Otherwise, some suggestions people will make, and some
22 of us are committed to support will simply be left by the
23 wayside because something else we might think does not
24 claim that high a priority, that was agreed to prior to
25 that point.

1 Now, I would think we could agree that even the 14
2 items that you have listed here, have not at this point
3 been agreed to by the Committee. That is what the Chairman
4 thinks the committee would like to agree to.

5 The Chairman. Right.

6 Senator Long. It may very well be exactly what the
7 Committee wants to agree to. But, I would hope we would
8 think of other things we might want to do, that we think
9 of in the context that that does not necessarily increase
10 the cost of this bill to the Treasury, but in the context
11 that if we do this, we are going to have to put the whole
12 thing into the squeeze and find enough room to either put
13 some of it in or all of it in or leave all of it out,
14 because, just as you do in the budget process, you are
15 going to have to get down to a matter of priorities before
16 this is over with.

17 The Chairman. Well, I certainly share that view. I
18 think the one priority we have on our side, of course, is
19 trying to carry out the President's package. So the things
20 we have listed, items 1 through 14, the individual tax
21 rate reduction, the deduction for couples, accelerated
22 cost recovery system, individual retirement accounts,
23 retirement savings for self-employed, exclusion of a
24 portion of dividend and interest income, incentives for
25 research and experimentation, estate and gift taxation,

1 investment credit for rehabilitative buildings, crude oil
2 windfall tax, royalty owners credit, foreign earned income,
3 commodity tax straddles, incentive stock options, invest-
4 ment credit for property, are areas that I think there has
5 been either past actions by this Committee or indications
6 from the President that he believes he could accommodate
7 the desires of hopefully a large majority of this Committee
8 and support those areas.

9 There are five others, indexing individual taxes,
10 accelerated tax recovery system in a couple of areas,
11 additional savings incentives, estate tax special use and
12 technical changes, employee stock ownership plan tax credit,
13 employee stock ownership plans that are still under negot-
14 iation with the Administration, because there has been an
15 interest expressed by members of this Committee.

16 As I indicated, I know there are 60 some other
17 amendments floating around, I think by actual count, that
18 people would like to squeeze into this package.

19 If that can be done, with agreement, without squeezing
20 something of a higher priority out, we may be able to do
21 that.

22 But, I think we have taken a look at nearly every-
23 thing that has come to our attention. Therefore, I believe
24 we have a fairly firm priority list in the first 14 items,
25 plus two or three in the second category.

1 We certainly are not going to shut anyone off or
2 preclude anyone from offering amendments or having votes.

3 I would also indicate, it would seem to me, that we
4 could do all that by next Thursday and get a bill out of
5 the Committee, on to the Senate floor so that we can
6 indicate to the American people that the Senate, the House
7 never passed a tax bill, last year.

8 We have been waiting for the House to act on taxes
9 for a year and a half.

10 So, perhaps we can help speed that process along.

11 Senator Long. Well, may I say, Mr. Chairman, no one
12 can fairly criticize this Committee.

13 The Chairman. Right.

14 Senator Long. -- for failure to seek action on tax
15 reduction. If we had our way, the Nation would already
16 have had a big tax cut before the first of the year.

17 So, we are not behind anybody. We are way out front
18 as far as just passing on what we are seeking to do. I
19 hope that everyone will understand that in the negotiations
20 and voting we do here, we are just trying to write the
21 best bill we can write.

22 By just the ordinary standard, we are ahead of
23 schedule. Ordinarily we are expected to wait until the
24 House sends us a bill. We are voting here without having
25 seen what the House is going to send us.

1 I don't know that anyone is complaining at the
2 moment. But, I think this Committee can't be criticized
3 for failure to act. We are way ahead of time. I am one
4 of those who supported the Chairman of this Committee,
5 Mr. Dole, and others, when they tried to get a Senate
6 decision on the recommendation of this Committee last year.

7 The Chairman. I certainly agree with that.

8 Are there other members who would like to make an
9 opening comment?

10 Senator Bradley. Mr. Chairman.

11 The Chairman. Senator Bradley.

12 Senator Bradley. Mr. Chairman, I would like to
13 simply offer the following thought. This is clearly one
14 of the most important economic actions we are going to
15 take in this Congress.

16 The President has been urging us to act quickly.
17 The Secretary of Treasury has been calling us prima donnas.
18 We have a lot of things out there swirling.

19 I would hope that we have the opportunity to consider
20 this in an orderly fashion.

21 This is the first time I have seen this document,
22 when I came in today. I would hope that we wouldn't
23 preclude discussion about any of these matters or other
24 matters that would be of interest to a member of the
25 Committee.

1 Many of these items have changed back and forth,
2 different forms in the last couple of weeks. I would like
3 to have a chance to take a look at these and I hope we
4 wouldn't make any decisions very quickly on these matters
5 and would hope you would give each member the opportunity
6 to express his feelings about these and about other ideas
7 fully.

8 The Chairman. Right.

9 I do not think there is any desire to do anything
10 other than that. I guess the question might come on defin-
11 ition of moving it along. If we could do that by next week,
12 we can go full tilt. Maybe we can't do it. Maybe we will
13 find out it is not possible.

14 But, it seems to me that many of the items that are
15 before us, in fact, nearly every item has been before us in
16 one form or another for some period of time, and many things
17 that I have indicated were in the Senate Bill last year.

18 Some have been changed very little since that time.
19 But, certainly they should be discussed. There should be
20 opportunities for amendment, for modification, for add-ons,
21 for deletions, and we are going to do that.

22 I think maybe one way to start that process is to ask
23 Mr. Chapoton again, to go through it. We have made some
24 changes since we last met to go over the Administration's
25 proposal. There are certain changes that have been made in

1 the estate tax provisions. We added a provision on stock
2 options.

3 We recognize the need for some legislation in the
4 straddle area.

5 We worked with Senator Moynihan on that particular
6 provision, along with Senator Symms.

7 So, there has been a recognition that it is a fast
8 moving exercise. We have tried to accommodate. We have had
9 a number of members in little task force groups, but in the
10 final analysis, not everybody's amendments are going to be
11 adopted. Sooner or later we will have to make that choice.

12 Senator Bentsen. Would the Chairman explain what he
13 means by "next week."

14 The Chairman. Well, we would hope to report a bill
15 from this Committee, by next week, which would not even
16 approach the record set last year.

17 (Laughter.)

18 The Chairman. We did it in five days, last year.

19 That is why, since we agreed on so many of these
20 things before, there are different members on the Committee,
21 but I should think in many cases there may be refinements
22 offered, but I can't believe that the things we were for
23 last year, we would be opposed to this year.

24 Senator Bradley. Mr. Chairman, last year we were
25 approving a one-year tax cut. So, on that ratio, this should

1 take 15 days.

2 (Laughter.)

3 Senator Long. Let me just make this suggestion. When
4 we reported last year, we reported by a vote of 19 to 1.
5 Even the one vote that was voting opposed to it, was not
6 against the bill. The one vote was simply a protest against
7 a tax cut at all at that point, expressing the concern of
8 a great number of people that perhaps it was premature to
9 have a tax cut.

10 I would think, Mr. Chairman, that if you can persuade
11 your members to be as satisfied with the package that has
12 been put together as the 20 Senators were on the bill that
13 was reported, you won't have any problem reporting it in a
14 week.

15 Nobody is opposed to going in a hurry, providing that
16 they are in favor of what you are doing.

17 So, we will just have to see how well it goes on these
18 matters.

19 The Chairman. I would just say there is one marked
20 difference between last year and this year. Last year we
21 had a President who didn't want any tax cut. We were just
22 sort of free agents. We just kept adding things on until
23 everybody was on board.

24 This year, we have a President who wants a tax cut.
25 He has his own ideas where or how it should be structured.

1 So this Chairman may find himself in the position of having
2 to resist some of those great things that I supported last
3 year. I understand that.

4 So, I am not -- last year, I think the Chairman was
5 sort of in the position of being Santa Claus. This year, I
6 may not be able to do that this early in the year.

7 Well, if Mr. Chapoton, would again, I am happy to
8 have you here. You can explain these items very quickly
9 so that everybody supports them, it would be appreciated.

10 Mr. Chapoton. I would be happy to, Mr. Chairman.

11 Would you like me to go through the ACRS changes and
12 the individual tax cut changes, as well, very briefly?

13 The Chairman. Yes.

14 Mr. Chapoton. As you know, the President's original
15 proposal was only two pronged, the individual rate cuts,
16 10-10-10 over three, 30 percent over three years, beginning
17 July 1, of this year, a ten percent cut, another ten percent
18 cut in '82, and another 10 percent in '83, and the final
19 full 30 percent would be effective January 1, '84, and
20 beyond.

21 On the business side, the original ACRS proposal
22 would have put all assets in either 10, 5 -- equipment in
23 a 10-5-3 class, and would have dealt with real estate,
24 either a 10 year class, 15 year class or an 18 year class.

25 The original proposal has been modified and is now

1 introduced in the House as H. R. 3949.

2 It would modify the individual rate cuts by cutting
3 back and deferring slightly the individual rate cuts so
4 that as now proposed we would have individual rate cuts of
5 5 percent, beginning October 1, of this year, and additional
6 10 percent beginning July, 1981, and the final cut of
7 another 10 percent, beginning July, 1983.

8 The ACRS proposal, the cost recovery proposal would
9 also be amended in four significant ways.

10 First, the acceleration of recovery, all equipment
11 would be left in the same periods, as in the original
12 proposal; that is, either 10, 5 or 3 year class.

13 But the acceleration of the recovery would be
14 reduced from approximately 200 percent, declining balance,
15 to 150 percent declining balance through the years --
16 through 1984 and then, in 1985, the acceleration would
17 increase to 175 percent declining balance and in 1986,
18 would go back to the original 200 percent declining balance
19 and stay that way in 1986 and beyond.

20 The second change in the ACRS proposal dealt with
21 real estate. We removed the distinction between various
22 kinds of structures, put all structures in a 15 year class,
23 allowed a 200 percent declining balance depreciation, and
24 provided for 1245 recapture, if the accelerated depreciation
25 is elected, except for housing, which would have 1250

1 recapture, giving a slight benefit to housing.

2 All taxpayers would be entitled to elect, rather than
3 the 200 percent declining balance on structures, straight
4 line depreciation on structures, in which event, they would
5 avoid recapture altogether on the disposition of the real
6 estate.

7 The third change was the elimination of the deduction
8 for qualified progress expenditures.

9 The fourth change was a liberalization of the present
10 law rules applicable to leasing, whereby, under present
11 law, taxpayers do, who cannot for one reason or another
12 use the benefits of depreciation or the investment tax
13 credit, they enter into leasing transactions and receive
14 the benefits of these -- receive these tax benefits
15 through lower rentals.

16 We propose liberalization of those rules to some
17 extent to allow taxpayers who cannot use the deductions
18 currently, to obtain the benefits of them through greater
19 leasing transactions, which is basically a financing
20 method, whereby the benefits are received.

21 In addition, we propose adding certain personal
22 tax items that were not on our original proposal. I would
23 go through those very quickly, and then I will come back,
24 Mr. Chairman, and go through, as I understand the proposal,
25 how it differs, the bipartisan proposal before you this

1 morning.

2 In H. R. 3849, the additional items would have been,
3 first, lowering the top rate on unearned income from 70
4 percent to 50 percent, effective January 1, 1982.

5 We would have provided marriage penalty relief phased
6 in over two years.

7 Our proposal would have provided a ten percent credit
8 against -- a ten percent deduction from the income of the
9 lower earning spouse, limited to a cap of \$3,000. That would
10 be phased in beginning in '82 and fully effective in 1983.

11 We would have increased -- in the estate and gift
12 tax, we would have increased the unified estate and gift
13 tax credit to an exclusion equivalent of \$600,000, from
14 the present law, \$175,000. That would be phased in over
15 four years, fully effective in 1985.

16 We would also increase the annual gift tax exclusion
17 from \$3,000 to \$10,000.

18 We would increase the marital deduction on both gifts
19 and bequests from the present 50 percent limit on marital
20 deduction to 100 percent, so that the decedent could pass
21 property to his spouse or could give property to his spouse
22 during his lifetime, free of any transfer tax whatsoever.

23 We would propose increasing the individual retirement
24 account limits --

25 Senator Symms. Excuse me, Mr. Chairman. Did you want

1 us to ask any questions as we go along?

2 The Chairman. Just let him run through it first, and
3 then we can come back.

4 Senator Symms. Thank you.

5 Mr. Chapoton. Increase the individual retirement
6 account limits from the present law, \$100 to \$2,000 and
7 increase the spousal IRA or add the spousal IRA to that
8 so the total would be \$2,250 in the case of a spouse who
9 was not employed.

10 It would increase the IRA eligibility to individuals
11 who are not -- who are covered by an employer sponsored
12 plan. They could put \$1,000 in an individual retirement
13 account and in the case of a spouse who is not employed,
14 the total amount put in by husband and wife could be
15 \$1,125.

16 We would propose increasing the Keogh Plan limits
17 from the \$7,500, present law, to \$15,000. All of these
18 changes would be effective January 1, 1982.

19 We would have made permanent the present law, \$200-
20 \$400 interest and dividend exclusion. We would have made
21 that permanent for future years.

22 Finally, on the personal side, would have extended
23 and increased the Windfall Profit Tax Credit for royalty
24 owners from the present -- from the \$1,000 limit, in 1980.

25 We would extend that to the future and increase it

1 from \$1,000 to \$2,500, effective for 1981.

2 Then, three additional changes related to business.

3 We proposed a 25 percent incremental credit for
4 direct wages, or 25 percent of incremental increases in
5 direct wages for research and development, effective July
6 1, 1981.

7 We would have amended the Section 911 provisions
8 relating to taxation of Americans abroad to increase the
9 present -- change the present law rules to allow an
10 exclusion of the first \$50,000 of income earned abroad,
11 plus 50 percent of the next \$50,000 income earned abroad
12 and plus a housing allowance.

13 Finally, in the business area, we propose an invest-
14 ment tax credit for rehabilitation expenditures. The present
15 law provides a 10 percent credit for rehabilitation
16 expenditures on buildings that are at least 20 years old.

17 We would delete that and replace it with a 15 percent
18 credit for buildings that are 30 years old, a 20 percent
19 credit for buildings that are 40 years old, and a 25 percent
20 credit for buildings, including residences, rental
21 residential property, which qualifies as an historic
22 structure.

23 Now, Mr Chairman, the package before the Committee,
24 as I understand it, would change these proposals in the
25 following respects.

1 The exclusion for dividends and interest, the \$200
2 and \$400 exclusion would not be extended beyond existing
3 law. So, we would go back to the present law, \$100-\$200
4 exclusion for dividends only.

5 This package would add some provision dealing with
6 commodity tax straddles which would be of course, a revenue
7 raiser. It would add an incentive stock option package
8 which would basically, as I understand it, be the incentive
9 stock option rules that existed in the '70's, and it would
10 provide investment credit for used property at the same
11 time so that persons buying used property would receive a
12 full 10 percent or 6 percent investment credit, depending
13 upon the class the property falls into, and at the same
14 time, the seller of the property would have a recapture
15 of the investment credit of a like amount.

16 Now, those basically are our proposal, and as I
17 understand the changes in those proposals that would be
18 before the Committee this morning.

19 The Chairman. Are there any other changes made in the
20 -- other than those he recited. There was some change made
21 in the estate tax provision.

22 Mr. Lighthizer. There was a carryover basis rule
23 included, or something like a carryover basis rule included
24 in the Administration's or in the Conable Bill's estate
25 tax provision. We dropped that out.

1 Basically, the provision said that if a decedent
2 receives a gift within three years of his death, the --
3 his beneficiaries would receive the same basis that he had.
4 There would not be a stepped up basis. That was removed.

5 Mr. DeArment. Also, in the royalty owner credit, the
6 Secretary was authorized to set up a procedure for -- a
7 certification procedure for exempting royalty owners.

8 The Chairman. Would you explain that again? There
9 may be some interest in it.

10 Mr. DeArment. In the provision dealing with the
11 royalty owner credit, there is a provision that would be
12 inserted that would authorize the Secretary of the Treasury,
13 under regulations, to have an exemption certificate
14 procedure for royalty owners.

15 The Chairman. Most of these royalty owners can't
16 afford to wait a year or a year and a half. They shouldn't
17 be paying any tax in the first place. That is the purpose
18 of that amendment.

19 Are there any other changes that were made. The
20 point I would make, there were some minor changes made.
21 There are some others I have indicated are still under
22 discussion.

23 Senator Wallop, Senator Boren, in the estate tax
24 area. I think Senator Danforth and Senator Matsunaga on
25 the savings area. Senator Armstrong on indexing.

1 What have we done insofar as the straddle is
2 concerned in our proposal?

3 Mr. Lighthizer. Mr. Chairman, the information that
4 we have distributed to the Committee merely says we are
5 going to deal with that problem. There have been negot-
6 iations between a variety of the staffs of the members and
7 the Treasury and the Joint Committee and our staff, and
8 the minority staff on the Finance Committee.

9 There seems to be movement towards a bill not unlike
10 the bill that Mr. Moynihan introduced last week. There has
11 not been agreement on a tax rate for traders in the
12 commodity -- who get involved in commodity straddles.

13 But, it would clearly cut off the straddle for
14 people who use it for tax purposes. But, the details of
15 that provision have not been completely agreed to yet.

16 The Chairman. Now, if anybody has a question of Mr.
17 Chapoton.

18 Senator Symms. Mr. Chairman.

19 The Chairman. Senator Symms.

20 Senator Symms. On your estate and gift tax, I was
21 concerned, you make no mention of the special use valuation
22 for farms and forests and so forth. Are you trying to
23 leave that out of the whole thing?

24 Mr. Chapoton. It is not -- as you know, Senator
25 Symms, it is not in our original package. As I understand

1 it, it is not in the list before the Committee, though there
2 has been discussion of putting it in in 1985 or 1986, some
3 special use amendments.

4 Mr. DeArment. Senator Symms, if you look at the index
5 page, item number 18 there lists that as one of the items
6 that is still under negotiation, estate tax, special use
7 and --

8 Senator Wallop. I might add that it is under heavy
9 negotiation. The revenue effect of it is inconsequential
10 in terms of overall things. It just seems absurd, a slap in
11 the face to American agriculture, especially to leave that
12 out.

13 Senator Boren. Mr. Chairman, I want to agree with that.
14 I think that something all of us have worked on very hard
15 and we feel very strongly about it.

16 It was my understanding, when we were talking about
17 putting the estate and gift tax provision in, that that was
18 a very important part of it and it would definitely be
19 included.

20 So, negotiations can go on, but as far as I am concern-
21 ed, it is not negotiable. I just think it has to be in there
22 and has to be in there and must be for me to support it.

23 Senator Baucus. Mr. Chairman, I agree. I want to
24 ask Senator Wallop or Mr. Chapoton when will these negotiations
25 result in something we could --

1 Senator Wallop. I think their side of it is over. I
2 am not sure.

3 Senator Boren. They don't have a vote though, do they?

4 The Chairman. Maybe I could, without putting Mr.
5 Chapoton on the spot, he is here in a technical role this
6 morning, there is -- we are negotiating that question,
7 hopefully successfully.

8 But, I think the indicate from at least four members
9 here would be some indication, if anyone from Treasury is
10 here, of the feeling of the members.

11 Mr. Chapoton. We note that, Mr. Chairman.

12 Senator Baucus. Mr. Chairman, I would hope a lot of
13 other items would be negotiated, too.

14 The Chairman. If you have any you would like to raise
15 at this point.

16 Senator Baucus. The curious point strikes me as these
17 items are being negotiated, not in this Committee, but other
18 rooms and other places.

19 The Chairman. No, they have been negotiated. We have
20 a task force at staff level for the past several days that
21 has been trying to come up with recommendations. They were
22 only recommendations we agreed to make for the Administration.

23 But, I think in this case, there may have been some
24 statements made to certain members, at least I understand
25 that to be the case, that this would be done.

1 We had negotiations on savings, recommendations on
2 estate and gift tax, recommendations on indexing, re-
3 commendations on ACRS and recommendations on small business.

4 We have submitted those to Mr. Regan, the Treasury
5 Secretary. Some were approved, most were rejected. It
6 did happen, as far as I know, it all happened in this build-
7 ing, didn't it, Mr. Lighthizer?

8 Mr. Lighthizer. Yes, sir, in this room, in fact.

9 Senator Grassley. Mr. Chairman.

10 The Chairman. Senator Grassley.

11 Senator Grassley. Mr. Chairman, I support what has
12 been said about special use, but I do think I need to
13 compliment the Administration and Assistant Secretary
14 Chapoton, because we did have some hearings in IRS Oversight
15 on some of the technical problems with special use, and
16 certain people qualifying.

17 They have been able to make some technical corrections.
18 There has to be a change in statute, but I do think we need
19 to recognize that the Administration has been working to
20 some degree on this problem.

21 Senator Wallop. I agree with that. I certainly don't
22 cast any aspersions on Mr. Chapoton. But, that is one thing
23 that is of major import to those of us who have been pushing
24 this.

25 The Chairman. I think a rather generous package was

1 submitted to us. Maybe if it hadn't been so generous and
2 we fought for a few changes, we would think today this is
3 fantastic.

4 But, I guess we are like everyone else. They say
5 you can say you can have this and they immediately indicate
6 that is not enough.

7 So, you understand that.

8 Mr. Chapoton. Yes, sir. I understand. I would echo
9 that comment. We did put together a package we thought had
10 broad support and was still consistent with the President's
11 overall program.

12 Senator Bentsen. I would like to know where we are
13 on the savings incentive. Has that been pretty well resolved
14 or not?

15 The Chairman. Not resolved. That is why it is in that
16 category.

17 Senator Bentsen. Well, as the Chairman knows, I am
18 very interested in that. I have one piece of legislation
19 with some 33 co-sponsors in the Senate.

20 The Chairman. I would like to say on that one, Senator
21 Bentsen, you have a proposal. I think Senator Borén has a
22 proposal. Senator Danforth has had a proposal. Senator
23 Matsunaga has talked to me about a proposal.

24 So, I would say that it is still open.

25 Senator Bentsen. On the small business, I have a

1 proposal there that is tantamount to what we passed through
2 this Committee last year, very similar to it.

3 Where are we on that?

4 Mr. Chapoton. You are talking about increasing the
5 surtax exemption?

6 Senator Bentsen. Yes.

7 Mr. Chapoton. That is not in this package, Senator.
8 We do feel like there is an awful lot in this package for
9 small business, particularly if the investment credit on
10 used property is added.

11 Senator Bentsen. All right. Let me ask another one
12 then. On the liberalizing of the leasing, I would like to
13 know what the cost is of that. I would like to know to what
14 extent you are changing the at risk provisions on leasing
15 and to what extent that precludes individuals from parti-
16 cipating as limited partners, in a general partner deal?

17 Mr. Chapoton. The cost of -- to answer your first
18 question, the liberalized leasing rules cost is specified
19 in the fact sheet we released.

20 It would be \$.5 billion, in 1981.

21 It would be \$2.7 billion, in 1982.

22 \$3.8 billion, in 1983.

23 \$5.4 billion in 1984.

24 Senator Bentsen. Is this in effect a way to do a
25 refundable tax credit?

1 Mr. Chapoton. It moves in the direction of allowing
2 taxpayers who cannot utilize deductions and credits, to
3 obtain the benefits of them by passing them along through
4 leasing, to other taxpayers who can.

5 That is what is done currently. This would --

6 Senator Bentsen. This would expand it very substantially
7 to the extent of at least how many billion?

8 Mr. Chapoton. Well, \$5.4 billion, in 1984, which is
9 very substantial; yes sir.

10 It would be limited to the corporate sector. So that
11 individual leasing under these expanded rules would not be
12 allowed.

13 Senator Bentsen. Now as to the question on limited
14 partners and the at risk provisions on the investment tax
15 credit. Is that a part of this legislation?

16 Mr. Chapoton. That rule was modified from the original
17 proposal. It would have applied the at risk rules directly
18 to the investment tax credit.

19 In H. R. 3849, that proposal was modified so that the
20 limitations would apply only to financing. You would be
21 considered at risk from -- with respect to financing, if
22 it was from a traditional financing institution.

23 Senator Bentsen. That would then preclude the
24 individual; is that correct?

25 Mr. Chapoton. That would be available to the

1 individual, yes sir.

2 Senator Bentsen. Would not be available.

3 Mr. Chapoton. Would be available to the individual.

4 As under present law, individuals are entitled to use the
5 investment tax credit through a limited partnership
6 mechanism, for example.

7 Senator Bentsen. That's correct.

8 Mr. Chapoton. Without respect -- without regard to
9 the at risk rule.

10 Senator Bentsen. That's right.

11 What is the change?

12 Mr. Chapoton. Our proposal, in February, would have
13 extended the at risk rule to the investment credit, very
14 simply.

15 As modified, our proposal would extend the at risk
16 rule to the investment tax credit, but would say that
17 taxpayers are considered to be at risk with respect to
18 debt, that is loans, made by traditional financial insti-
19 tutions.

20 It would stop the problem that has existed with
21 respect to non-recourse loans from non-financial institutions
22 which has been a significant problem in the tax shelter
23 area.

24 Senator Bentsen. Thank you.

25 The Chairman. Senator Armstrong.

1 Senator Armstrong. Mr. Chairman, I have three matters
2 that I would like to just raise briefly.

3 One may I report to the Chairman and the Committee
4 that I have met with Mr. Chapoton on the question of family
5 rental tax issue, which really has nothing to do with this
6 broad tax relief bill we have before us, and for which, by
7 the way, I compliment you, Mr. Chapoton and Secretary Regan,
8 and others for putting together a good package.

9 Mr. Chapoton. Thank you.

10 Senator Armstrong. I will tell you this. I do not
11 for a second share the view that some have expressed, we
12 ought to slow down the conclusion on this. The American
13 public thinks it is already five years too late.

14 I would like to get moving on it. I forgot who said
15 it, whether it was the President or Speaker O'Neill or who
16 it was, but someone suggested that we ought to be here
17 through the August recess, around the clock, until we get
18 action on this bill.

19 I share that feeling.

20 On the family rental tax which is really not related
21 to this, I am advised by Mr. Chapoton that they can solve
22 part of the problem that was addressed in that bill, which
23 I think is sponsored by most of the members of this
24 Committee, but there is one aspect of it that cannot be
25 addressed by regulation.

1 That is the provision of law which limits renters in
2 the amount of income they can receive, from family members.

3 The effect of it, as I understand it Mr. Chapoton,
4 unless there is a statutory change, the Treasury Department
5 will be required in effect to treat property which is rented
6 to family members, different in the deduction of expenses
7 than it is treated if the same property is rented to a
8 stranger.

9 Mr. Chapoton. That is correct. That is required by
10 the legislation. I think obviously the concern of the
11 legislation was that you don't know whether, when you rent
12 to a family member, whether you are receiving fair market
13 value.

14 So, if you change the rule, I think you would have to
15 say it would be for fair market value. The Internal
16 Revenue Service would be required to make that determination.

17 Senator Armstrong. That is exactly the nature of
18 change that I think we must make. I would leave it to
19 a later decision as to whether or not we want to incorporate
20 that as an amendment to this bill.

21 I assume that would not be controversial. The only
22 reason that it is timely is this. At the end of the last
23 session, I suggested I would offer an amendment on a then
24 pending bill, Treasury did agree by letter, to withhold
25 until July 1, action on this matter.

1 The July 1 deadline is coming up, and while Mr.
2 Chapoton has agreed that he will insure us on two of the
3 three points that were contained in that bill, on this last
4 one, he doesn't feel he is in a position to do so.

5 We have a time deadline and in one way or another,
6 we need to resolve that problem.

7 Second, Mr. Chairman, I just want to raise and note
8 in passing that so far as I can tell, this package does
9 not contain original Administration proposal on qualified
10 progress, permitting those companies that have a construction
11 project that extend over several years, to benefit from the
12 more generous depreciation rules that are proposed.

13 Since this affects a large number of companies, in a
14 very significant way, including some in my state, I think
15 particularly the synfuels industry where it takes five or
16 ten years to build a plant, depletion of that from the
17 Administration proposal is the source of real concern to
18 me, particularly at a time when there is an enormous
19 national effort to increase the synfuel production.

20 I was a little surprised that was taken out of the
21 package during the course of the negotiation.

22 Mr. Chapoton. Well, Senator, the qualified progress
23 expenditure, the overall, the changes were within budgetary
24 constraints.

25 It was felt that that was one we could delete in favor

1 of some improvements in the overall package.

2 Let me say that the qualified progress expenditure
3 provision, as originally proposed, benefited principally the
4 utilities, who in some cases, weren't particularly interested
5 to have it, because the rate-making bodies would require
6 them to flow it through, would have required them to take
7 it into account and flow the benefit through.

8 Other than that, a lot of buildings.

9 So, we thought overall it was probably desirable to
10 not have it.

11 Senator Armstrong. I think your point is well taken.
12 I would at least to flag it for the attention of the
13 Committee, the possibility we might restore that in a
14 limited form with respect to certain kinds of projects. I
15 am thinking of synfuels projects where the lead times are
16 very long and the national priority to encourage construction
17 of such projects is very clearly defined, where the revenue
18 loss would not be very great.

19 I understand that is a matter that is of interest to
20 several around the table.

21 Third, Mr. Chairman, I want to note at least in
22 passing, I have no proposal to make today on this matter,
23 but I think it is something we must give attention to, that
24 there is no relief from Windfall Profit Tax Bills.

25 I am one of those who -- I have forgotten what I said

1 last year when we passed that, whether I said that it was
2 the worst piece of legislation of the decade or whether I
3 merely said it was the most hurtful legislation enacted by
4 any.

5 But, I continue to believe that the Windfall Profit
6 Tax is counterproductive, antisocial, unwise tax policy,
7 against the best interest of the country.

8 Having said that at the time and having voted against
9 it at the time, I noted with pleasure the President's
10 questions along the same line.

11 So, I am eager to get some relief for that tax.

12 Of course, I appreciate the royalty owners portion of
13 it, but that is a modest part of the exemption. I under-
14 stand there may be proposals to be suggested at the right
15 time.

16 I don't know whether I can support that, because I
17 am, like the Treasury Department, I am concerned about the
18 revenue implications here.

19 So, I don't know whether that gets in the package or
20 not or whether I would vote to do it would depend upon a
21 lot of other things.

22 Senator Bentsen. If I might say to the Senator, I will
23 be proposing my 1,000 barrel exemption again, this year.

24 Senator Armstrong. I wondered if you had that in mind.

25 I would say to the Senator from Texas, that I am

1 interested in the problem. I don't know whether I can
2 support you on that or not. But, I think that if there is
3 integrity and meaning in this process, we ought not forget
4 the promises we made last year.

5 Finally, Mr. Chairman, I would like to just give a
6 brief report from the tax indexing caucus. If there was
7 ever an idea which has become timely, this is it. I am sure
8 that members of the Committee and Treasury recall what
9 Victor Hugo said about an idea whose time has come.

10 I want to remind my friend from Montana, who was
11 talking about some proposals that are pending, I noted with
12 interest what the voters of Montana said about tax indexing
13 in the last election. I think that passed by about 70 to
14 30, in your state.

15 We put tax indexing in in Colorado. It has been very
16 popular. When it was offered in the Senate, in the last
17 biennium, there were 38 Senators who voted for it and I
18 believe some of the new members of this Committee and new
19 members of the Senate have expressed themselves in favor of
20 it.

21 I recall vividly the President's stirring endorsement
22 of tax indexing last September.

23 I also want to report that since this Committee last
24 met, I have been conferring with our colleagues in the House.
25 I am advised that the tax indexing proposal over there is

1 now co-sponored than no less than 211 members of the U. S.
2 House of Representatives.

3 Tax indexing has been endorsed by the American Bar
4 Association, Congressional Black Caucus, American Institute
5 of Certified Public Accountants, National Taxpayers Union
6 and the Advisory Commission on Intergovernment Relations
7 and some other groups that maybe we should not invoke at
8 this moment.

9 But, the purpose of my mentioning this, Mr. Chairman,
10 is just to indicate that there is a continuing effort to
11 raise this issue, because it is fundamentally just.

12 If we are really serious about giving the taxpayers of
13 this country a tax break, a permanent tax break, we must
14 index the tax system. If we don't there is real possibility
15 they will be simply inflated back into higher brackets.

16 So, I don't want to argue the issue at this time, but
17 I would like to ask the staff to distribute for the members,
18 a paper we have prepared just outlining some of the main
19 issues.

20 At the right time, when you are ready to consider it
21 further, I would like to be recognized again next week,
22 whenever it is.

23 Thank you.

24 The Chairman. If there are no other questions, we
25 could probably adopt the first 14 items.

1 (Laughter.)

2 The Chairman. But, if there are questions, why of
3 course -- Senator Grassley.

4 Senator Grassley. We are hopeful you were being
5 facetious.

6 The Chairman. Either way, we could adopt them.

7 (Laughter.)

8 Senator Grassley. Let me say I understand that I have
9 a lot to learn yet about how the Committee operates.

10 The Chairman. So have I.

11 (Laughter.)

12 Senator Bentsen. Apparently so do we.

13 Senator Grassley. Thank God, then there is hope for
14 all of us.

15 Well, Mr. Chairman, I wanted to ask the Administration
16 as a co-sponsor of 10-5-3, in the first hearings we had on
17 this bill, it was brought out that businesses would benefit
18 more than beyond expensing, in 10-5-3.

19 Then, there was some talk at one time about putting
20 a cap on that. That was when you included the investment
21 tax credit with it.

22 Then, there was some readjustment in 10-5-3, in the
23 Administration's original proposal, and then there was some
24 adjustment later on to encourage the support of the business
25 community towards the whole tax package.

1 So, it is my understanding that in '85, and '86, there
2 is some benefit to the business sector beyond expensing in
3 the changes that were made for '85 and '86.

4 So, I want to know, first of all, is that true for
5 -- my understanding of the bill, and if it is true, for an
6 explanation as to the economic rationale for that.

7 Obviously, I support accelerated depreciation, because
8 I think we have to encourage investment.

9 Is that additional -- if what I understand is true for
10 '85 and '86, is that necessary to encourage that business
11 investment?

12 Mr. Chapoton. Senator Grassley, this question of
13 faster than expensing has, as you well know, been discussed
14 a great deal.

15 Senator Grassley. First of all, can I ask you, has it
16 been discussed this morning?

17 Mr. Chapoton. No, it has not been discussed this
18 morning.

19 Just so we know what we are talking about. The
20 question is what is the present value of the future tax
21 benefits from both the investment tax credit and the
22 depreciation or cost recovery.

23 If you have a deduction, let's say from an asset that
24 will be placed in service in 1981, a deduction that will be
25 received in 1984, of \$100, so that it will offset tax

1 liability in 1984, and therefore, is a 46 percent tax rate,
2 it would offset, you would save \$46 in tax, because of that
3 cost recovery deduction, in 1984.

4 If you didn't take that \$46 and you discount it at
5 present value at some discount rate. You also make that
6 same calculation as to every other deduction in the years
7 over which the property is held and cost of that property
8 is recovered.

9 You make the same calculation with respect to invest-
10 ment tax credit, which, of course, is received in year one,
11 but is not a benefit until you have a tax liability that
12 would otherwise be due.

13 If you assume that the taxpayer is in a 46 percent
14 bracket, and if you assume the taxpayer a 46 percent
15 marginal bracket, and can use all the deductions and credits,
16 can fully utilize all the deductions and credits available
17 to him, then you can use a discount rate to determine the
18 present value of those future benefits.

19 If the discount rate you use is 12 percent, the
20 present value of the deductions in 1981 through 1984 is
21 approximately equal to present law expensing.

22 If you take both a credit and a deduction.

23 I would point out that -- well, the discount rate,
24 the question of what discount rate you use is a much dis-
25 cussed issue. And 12 percent is certainly lower than many

1 companies use for their internal rate of return.

2 I think the feeling is that something between 12 and
3 18 percent is correct. It depends on the inflation rate and
4 it depends on the internal rate of return the particular
5 company expects from investments it makes.

6 If you use 12 percent, as I said, we are about equal
7 to expensing, '81 to '84.

8 If you use 12 percent when the accelerated cost goes
9 up in '85 and '86, you are slightly, very slightly better
10 than a current deduction.

11 It does not mean for making an investment though, you
12 get more dollars back than you invest.

13 But, I would emphasize that we do not know, none of
14 us know what is the correct discount rate. Indeed, we
15 certainly don't know what the correct discount rate will
16 be in 1985 and 1986.

17 As we look at the history of cost recovery, when the
18 Investment Tax Credit came in, it came in in 1962.
19 Originally, the taxpayers were required to reduce basis
20 by the amount of the credit. Therefore, reducing the
21 cost recovery from an asset in later years.

22 In 1964 or 1965, the law was changed so that the
23 investment tax credit did not reduce basis, making it
24 clear that the taxpayer got the investment tax credit,
25 plus 100 percent recovery of basis.

1 You trace through what might be an appropriate discount
2 rate through those years, because the inflation rate is a
3 factor. You come in some cases where the combined benefit
4 then, in some classes of assets, work faster than expensing.

5 So, I think this question has been discussed to a
6 point that we have not necessarily understood the significance
7 of it.

8 But, a direct answer to your question, we like this
9 proposal. We think it gives the benefit. We are trying to
10 give significant benefit to cost, to cost recovery so the
11 taxpayers will make investment in plant and equipment.

12 It gives it in these early years, we think, and it
13 gives it slightly more in '85 and '86. We think that is
14 desirable to keep business making these investments.

15 Senator Bradley. Mr. Chairman.

16 Would the Senator yield for a point related to the
17 question you asked?

18 Senator Grassley. But I am not done with my question-
19 ing, but I will yield to you. Go ahead.

20 Senator Bradley. Thank you, Senator Grassley.

21 Just for a comment. I think in Mr. Chapoton's explan-
22 ation that the answer he gave is that yes, there will be a
23 negative effective tax rate in 1985 and 1986, for certain
24 categories of assets.

25 Now, related to that is what is your assumption for

1 inflation figured into the discount rate in order for there
2 not to be a negative effective tax rate?

3 Mr. Chapoton. Senator Bradley, the assumption, as we
4 went through last week, our assumption on the inflation rate
5 is about six and a half percent, I believe, out in those
6 years.

7 Senator Bradley. That is the budgetary assumption.

8 Mr. Chapoton. Right.

9 Senator Bradley. But in order for the -- for it to
10 be no negative tax rate what would inflation have to be?

11 Mr. Chapoton. You have to take inflation plus real
12 rate of return.

13 The answer to your question is you have to have a
14 discount rate of approximately 17, 17.5 percent, to come
15 to about zero, about equal to expensing in 1986, under this
16 proposal.

17 Senator Bradley. So what would be the -- the real rate
18 of return is simply mathematical calculation.

19 Mr. Chapoton. No, the real rate of return is what a
20 taxpayer will have to assume or have to assume he will yield
21 on an investment before he will make the investment, and it
22 will vary.

23 Senator Bradley. So, if you recall our exchange last
24 week, when I asked you this question, you said that the
25 inflation rate would have to be 12 percent.

1 Mr. Chapoton. If you assume the real reate of return
2 should be no more than five and a half percent.

3 No, you have to decide in a particular taxpayer's
4 case, what rate of return will induce him to make the in-
5 vestment.

6 If he can get Treasury bills at five and a half to
7 six percent, he is not likely to make a risk investment at
8 that same real rate of return.

9 Senator Bradley. Well, either you will have to concede
10 that the inflation rate will be in the 12 to 13 percent
11 range, or you will have to concede that you have a negative
12 effective tax rate.

13 Mr. Chapoton. I will have to concede that if you make
14 the assumption --

15 Senator Bradley. One of the two.

16 Explain to me under what circumstances would you not
17 have to do either one or the other?

18 Tell me why it would not have to be an inflation rate
19 of 13 percent or a negative effective tax rate?

20 Mr. Chapoton. It wouldn't have to be 13 percent, but
21 at some point, if inflation dropped to six or below, you
22 would have a negative tax rate out in 1986, under this
23 proposal.

24 Senator Bradley. If it didn't drop -- it would have to
25 drop to 6 or below in order for you not to have it?

1 Mr. Chapoton. I repeat, you cannot make a general
2 statement, because it depends upon what the taxpayer's rate
3 of return.

4 Senator Bradley. Maybe I don't understand the concept.
5 Could you explain a little more, so that I could
6 understand it?

7 Mr. Chapoton. The appropriate discount rate is the
8 sum of the inflation rate and the real rate of return.

9 So the question is, if you assume an inflation rate
10 of let's say 6 percent, then you have to decide what real
11 rate of return would induce the taxpayer to make this
12 investment.

13 If you tell me that a six percent rate would induce
14 him to make the investment so that the sum of the two is 12
15 percent, then in 1986, you do have slightly better than the
16 present value of the future deductions to that taxpayer
17 will be slightly better than expensing.

18 Senator Bradley. What is the real rate of -- normal
19 real rate of return?

20 Mr. Chapoton. Well, that is the subject much debated,
21 you know.

22 Senator Bradley. Just the range, you know.

23 Mr. Chapoton. I think in the range of 5, 6, to 8
24 percent; in that range.

25 Senator Bradley. What has it been on assets,

1 generally, in the last year?

2 Mr. Chapoton. Six percent.

3 Senator Bradley. Six percent. So you are saying
4 you have to have a real rate of return at greater than
5 6 percent?

6 Mr. Chapoton. That's correct, but I would emphasize
7 that you have to look at the particular taxpayer and he may
8 indeed demand a higher rate of return, and therefore, would
9 use a higher discount rate.

10 In fact, if you ask companies what is their internal
11 rate of return on investment, many of them now will say 18
12 to 20 percent.

13 What they are telling you then, they need that type
14 of -- that amount of return to induce them to make an
15 additional dollar investment.

16 Senator Bradley. I think that this blunts or blurs the
17 issue sufficiently here. But, I think that you have to keep
18 in mind again, and I say this to the Senator, that you
19 cannot assume that you are going to have no negative
20 effective tax rate.

21 In other words, a real subsidy for investment. Not
22 zero tax, but a real subsidy, unless you assume a rather
23 high inflation rate.

24 Unless you have done as Mr. Chapoton, just assume a
25 much bigger real rate of return than we have consistently

1 thought possible.

2 Senator Grassley. Senator Bradley, could I recapture
3 my time?

4 Senator Bradley. Thank you.

5 Senator Grassley. Thank you.

6 I still -- the point of my question was probably a
7 little more philosophical than it was related to the direct
8 impact, the philosophy of the Administration on a cost of
9 \$2.5 billion beyond expensing for 1985, and I think \$14
10 billion beyond expensing for 1986.

11 The extent to which that sort of cost to the Treasury
12 is necessary to encourage investment in '85 and '86, when I
13 hope by that period of time, we have the economy turned
14 around where -- to a point where just expensing and
15 accelerated depreciation more closely related to replacement
16 costs is adequate incentive.

17 Mr. Chapoton. Well, we certainly hope the economy
18 is turned around and inflation is down and that these cost
19 recovery allowances do spur the investment that we need.

20 Senator Grassley. There has to be a feeling in the
21 Administration in those out years of '85 and '86 that there
22 is going to have to be further incentive at that point to
23 encourage the investment; right?

24 Mr. Chapoton. There are budgetary constraints in the
25 original proposal in the years -- well budgetary constraints

1 in the years '81 through '84 and that is why we couldn't
2 go immediately to the higher cost recovery.

3 Senator Grassley. So then your explanation for --
4 Mr. Chapoton. We prefer to have it in place immediate-
5 ly.

6 Senator Grassley. So you are saying then that the '85
7 and '86 is necessary to have the added cost at that time,
8 to even encourage investment in '81, '82, '83 and '84; right?

9 Mr. Chapoton. This as proposed, the lower level, will
10 encourage investment, will encourage it significantly. We
11 would prefer to have a higher degree of encouragement and
12 would put it in place immediately, but for the budget
13 constraints. That is why I --

14 Senator Grassley. Am I right, those costs are \$2.5
15 billion?

16 Mr. Chapoton. Senator, I don't -- I am not sure I
17 can break those costs out for you from the figures I have
18 before me.

19 Senator Grassley. Is there anybody else on the panel
20 who can?

21 (Pause.)

22 Mr. Chapoton. Well, I am advised it is approximately
23 fiscal year, \$1.4, '85; \$9.2, '86.

24 Senator Grassley. Senator Symms had questioning along
25 this line, Mr. Chairman.

1 Senator Symms. Did we get this -- did I understand
2 you correctly now about the difference between '82 and
3 '83 and '84 and '85? Are you convinced that you are not
4 going to have decisions put off because of more attractive --

5 Mr. Chapoton. The question you are going to, the
6 benefits will increase in '85 and '86. You have to examine
7 when you have a phase in or step up in benefits as to
8 whether the investment will be deferred as you approach that
9 period, particularly in '84.

10 Senator Symms. How about right now?

11 Mr. Chapoton. No, clearly there would be no deferral
12 that far in advance. The deferral question would really
13 arise as you get much closer to the period. That is why
14 it is phased in over two years so that the deferral will
15 not occur, in our opinion.

16 In other words, if you stepped immediately from 150
17 percent, in 1984, to 200 percent, in 1985, we would be
18 concerned that some deferral of investment would occur.

19 We do not think it will when you phase it in over
20 two years.

21 The Chairman. Could I ask? Have you had a chance
22 to review the House action of yesterday?

23 Mr. Chapoton. Yes, Senator, in a preliminary basis.
24 The House action yesterday would phase in expensing over a
25 ten year period.

1 The principal problem with that is the phase in, the
2 -- in 1981, for example, 20 percent of investment would be
3 expensed, and 80 percent of investment would be recovered
4 under the present ADR rules, and in 1982 would jump to 40
5 percent, under expensed, and 60 percent under the present
6 ADR rules.

7 So that the present value of the deductions in the
8 first few years, '81 through '83, would be significantly
9 below the present value of the deductions under our ACRS
10 proposal.

11 The Chairman. I guess my question was, do you feel
12 your product is superior?

13 Mr. Chapoton. For that reason, that is the principal
14 benefit we see in our proposal over that.

15 The Chairman. The corporate rate reduction.

16 Mr. Chapoton. Even taking the corporate rate -- we
17 think corporate rate reduction might well be considered at
18 some point, but we now are after benefits that will give the
19 tax benefits to investment in new plant and equipment,
20 increased productivity directly in that manner.

21 Of course, the House bill would spread that, dilute
22 that benefit somewhat by putting part of the benefit through
23 corporate rate reduction.

24 The Chairman. Well, I want to ask one question. I
25 think there will be some votes here I understand in about

1 ten minutes. I would like to have the Committee go on
2 record at least in one area today and that is on the --
3 make certain we don't exceed the revenue loss estimates for
4 the Administration's revised bill.

5 I understand that you have those figures. In fiscal
6 year '81, it is \$2.1 billion; fiscal year '82, \$38 billion;
7 fiscal year '83, \$93.4 billion and fiscal year '84, \$149.6
8 billion.

9 Mr. Chapoton. That's correct.

10 The Chairman. Are those accurate figures?

11 Mr. Chapoton. Yes, sir.

12 Senator Bradley. Mr. Chairman, where are these
13 numbers? In our paper?

14 The Chairman. They are not in the paper. I just
15 wanted to verify if -- they are in --

16 Mr. Chapoton. They are in the fact sheet we handed
17 out last week, Senator.

18 The Chairman. They are also printed. They are in the
19 printed material.

20 Mr. DeArment. They aren't precisely the same because
21 there is some netting.

22 Senator Bradley. They are not the same numbers?

23 Mr. Lighthizer. The only difference, Senator, is that
24 in the proposal we handed out this morning, there is -- we
25 did not include the continuation or making the \$200 or \$400

1 which is about \$2.4 billion. The reason was that the
2 savings item is still under negotiation.

3 Senator Bradley. Mr. Chairman, this is what I was
4 talking about earlier.

5 Mr. Lighthizer. They are the same in '81 and '82 and
6 they are \$2.4 billion.

7 Senator Bradley. You know, if we could have had these
8 some time in advance to look at them, we could be asked to
9 vote on them.

10 The Chairman. We are going to be asked to vote on them.
11 That is why I wanted to verify that these are the numbers.
12 The Administration's loss estimates are the numbers I just
13 read; is that correct?

14 Mr. Chapoton. That is correct, Mr. Chairman.

15 The Chairman. All that I am suggesting is that we need
16 some parameters so that when we start digging out additional
17 amendments, we know that we would hope that the Committee's
18 action on the loss estimate would not be -- the Administra-
19 tions loss estimates would not be exceeded.

20 Senator Danforth. Mr. Chairman.

21 The Chairman. Senator Danforth.

22 Senator Danforth. Thank you, Mr. Chairman.

23 I think this makes sense. This is the procedure that
24 we followed, as I recall, last September, when we figured out
25 how much revenue we could afford to lose before we started

1 addressing the question of the tax bill.

2 The Administration's -- the figures we are voting do
3 assume the extension of the \$200 and \$400; is that correct?

4 Mr. Lighthizer. That's correct.

5 The Chairman. Right.

6 That is the only difference.

7 Mr. Lighthizer. Yes, sir.

8 The Chairman. That is still under negotiation, that
9 is why it is different from ours.

10 Senator Long. When we agree on this, we are leaving
11 ourselves the option of doing it the way we did in the
12 Committee last year or doing it the way we have done it
13 when we were loaded down on the floor, on occasion. That
14 is, we have those two options available to us where we could
15 go to conference with a bill that say we come back within
16 these figures, although we are taking a bill that exceeds
17 them to conference.

18 Incidentally, up to now that has always been the first
19 amendment the House agreed to, without any debate. They say,
20 "Now here is something in your bill we will agree to right
21 off," and that is what comes from conference should not
22 exceed what the budget would permit. That is basically what
23 you are talking about.

24 Where we took to conference a bill that did exceed
25 that, but we had that amendment that said it should not

1 exceed those figures when it came back.

2 Just reserving us, what in effect we would mean by
3 this, whenever we agree to something that increases the
4 cost, that means that before this thing is over with, before
5 the legislative process has been concluded, we have to be
6 within the figures the Chairman is referring to.

7 I think that on that basis, I could agree to it. I
8 would believe that everybody here could. I certainly hope
9 so.

10 Senator Bentsen. Mr. Chairman, I could too, with that
11 kind of a proviso in it. Senator Long stated we are talking
12 about staying within the budget. As I recall, the budget
13 -- we are talking about different figures there. That was
14 \$55 billion, for 1982.

15 Here we are talking about something that approximates
16 \$38 billion. I am not quarreling over that. I am just
17 stating that when we are talking about the budget provisions
18 itself, that that is a \$55 billion figure.

19 The Chairman. Right. These are based on the revised
20 proposal. It is my view though, that we need to have some
21 parameters. It is easy to push things into the bill if we
22 don't have to worry about the final figure. The Adminis-
23 tration is concerned. We have other of our colleagues, on
24 both sides, who are concerned. Senator Hollings and Senator
25 Domenici are already saying the tax cut is too large.

1 If we could establish that would be the guidelines
2 when we take final action on this proposal, that they will
3 not exceed the revenue loss estimates of the Administration's
4 revised bill. I think that would be at least one step that
5 we could take today.

6 That would be \$38 billion in 1982; \$2.1 billion, in
7 '81; \$93.4 in '83 and \$149.6, in '84.

8 Senator Long. Might we understand, Mr. Chairman, that
9 that might entail coming out of Committee with something
10 that goes above the \$38 billion, but which has an amendment
11 to it that says the final product cannot exceed that.

12 The Chairman. I just said the final product.

13 Senator Long. Yes.

14 On the floor we had the experience there, not in the
15 Committee, but on the floor we have had the experience, by
16 the time the bill is loaded down with amendments, we had
17 something that looked like an irresponsible bill.

18 On behalf of the Committee, I would offer the amendment
19 to say this bill came back from conference it should not
20 exceed the following figure. So far there has never been
21 a vote against it. The Senate, having indulged itself the
22 pleasure of voting for all those amendments, are then happy
23 to vote to say that it shouldn't break the budget.

24 I think that on that basis, I believe we can all agree
25 with the Chairman.

1 Senator Danforth. In what amount would it leave the
2 Committee? I think all of us recognize that something can
3 happen on the floor. Are we just going to look forward to
4 what comes out of conference or is this figure also
5 supposed to be a limitation on what we do in this committee?

6 The Chairman. I hope it will be some guide to the
7 Committee for consideration.

8 I don't anticipate exceeding these limits in the
9 Committee, but I haven't counted the votes on various
10 amendments.

11 If a number of amendments are probably meritorious
12 and they are under consideration by different members, we
13 might have to accede to that. I hope that is not the case.

14 I think again, we should commend the Administration
15 for presenting a package that I think is an exceptional
16 package in many ways. I don't see much reason to exceed
17 it. But, there may be 11 on this committee who have a
18 different view. That would make the vote 11 to 9.

19 Senator Danforth. As I recall last year, we did use
20 this as a discipline within the Committee itself. It seems
21 to me that that is what we should be looking forward to,
22 recognizing that anything can happen on the floor of the
23 Senate. We can't control that. We will hope to come back
24 to it in conference.

25 Senator Long. As I recall last year, though, when we

1 had more freedom to do what we on the Committee wanted to
2 do. We first agreed to the discipline and then we proceeded
3 to overshoot it. I see some of the staff laughing who
4 recall what happened.

5 Now, it wasn't that we overshoot it badly, it is just
6 that we went over the target.

7 All I am saying is, I think in good faith and in
8 fairness to those who have amendments to offer of this bill,
9 that we ought to understand, if we can we would like to
10 squeeze it inside these estimates before we leave here.
11 But, we would like to reserve the right that if we go out
12 to the floor over that, we would still be willing to support
13 an amendment and to bring it out in the bill. Say that this
14 is where we expect to end up and where we expect the Senate
15 to expect us to end up.

16 Senator Wallop. Mr. Chairman, could we ask the staff
17 to do one thing for the benefit of the Committee and the
18 public, in addition to talking of these things as revenue
19 losses, could we also see the revenue forecasts that it
20 would raise, because theoretically, a taxing committee isn't
21 running around taxing for losses. We are trying to raise
22 revenue to support the Government.

23 I just think that is an important figure. The public
24 starts looking at a figure like \$92 billion, in '84, and it
25 sounds like there won't be any raised.

1 As a matter of actual fact, there will be a substantial
2 amount of revenue raised.

3 The Chairman. I think that is accurate.

4 Let's just call the roll on the motion.

5 Senator Matsunaga. Mr. Chairman, what is the motion?

6 The Chairman. Before final action on the tax
7 reduction bill, we agree that we will not exceed the revenue
8 loss estimate of the Administration's revised bill. The
9 revenue loss estimates are those just referred to of \$2.1
10 billion, in '81; \$38 billion, in '81; \$93.4 billion, in
11 '83, \$149.6 billion, in '84.

12 Senator Boren. Mr. Chairman, I do understand we will
13 be able to offer amendments, even though at that particular
14 point in time they might appear to exceed, subject later to
15 a later reconciliation of all the figures.

16 The Chairman. That is correct.

17 I hope that doesn't happen, but that is an escape
18 hatch that will be available.

19 Senator Grassley, Then, also, a further clarification,
20 it would not preclude the subject of indexing which every
21 suggestion at this point has had it starting in 1985, from
22 being offered as well.

23 The Chairman. No, we figure '84, if we get that far,
24 we will be in good shape.

25 Senator Grassley. There are some of us who think if we

1 can get beyond '85, it will be better for the business and
2 working climate in America as well.

3 The Chairman. Right.

4 Senator Chafee. Mr. Chairman, what is the effect if
5 we make the changes in the straddles? What does that do to
6 us? These figures?

7 The Chairman. Well, it depends on the changes made in
8 the straddles. The estimates I think have been increased.
9 It was about \$1.3 billion. Is that still the same estimate?

10 Mr. Lighthizer. \$1.3 billion in the first year and
11 then \$.7 in subsequent years is what the number we have
12 been assuming.

13 Senator Chafee. So, does that give us -- if we make
14 that change, does that give us more leeway?

15 The Chairman. Well, hopefully, but we haven't made
16 that change. We would like to have, if we have a little
17 surplus, we hope that we don't rush in to spend it, but
18 based on precedents, there is probably likelihood that will
19 be suggested.

20 Senator Bradley. Mr. Chairman, could I just ask one
21 last question?

22 What is the rationale if the budget has a tax cut of
23 \$55 billion, for the Committee at this time saying, even
24 with the escape hatch that they have offered each of us,
25 that will not exceed \$38 billion?

1 The Chairman. Well, I think that there has been a
2 great deal of concern expressed by the Administration and
3 by many in both parties about deficits in '82, '83 and '84.
4 For that and other reasons, that figure has been reduced.

5 I don't know if Mr. Chapoton could expand on that.

6 Mr. Chapoton. That's correct. One desirable feature
7 of this modified package is it would reduce the deficit in
8 fiscal '82.

9 The Chairman. Of course, we are hoping for a balanced
10 budget in '84. There is a very delicate balance there now.
11 I think under these figures you would have about \$2 billion?

12 Mr. Chapoton. About \$2 billion surplus in 1984.

13 The Chairman. There isn't much leeway.

14 Senator Bradley. Does that assume there is a second
15 tax cut?

16 A second bill?

17 The Chairman. The second bill will depend, in addition
18 to those things that will cost money, some that might save
19 money. There are some of those under review by Treasury
20 now.

21 Senator Matsunaga. Mr. Chairman, one question.

22 Relative to emergency measures, and I think there is
23 one emergency measure pending before this Committee and that
24 is the All Savers Saving Certificates to help a very much
25 ailing industry.

1 if we could have the staff determine what the impact
2 would be on the adoption of that amendment, and if there is
3 no real impact, we could include that as an amendment.

4 The Chairman. Right. I appreciate it. I mentioned
5 earlier that you discussed that with me yesterday and of
6 your interest in that provision.

7 I think the question of whether it really has any
8 impact at all. If it does that which it is advertised to do.

9 There has been a search, I think, by many on this
10 Committee to find a better way, a better provision beyond
11 1982.

12 So, the answer is yes, we are certainly willing to do
13 that.

14 Mr. Lighthizer. Mr. Packwood.

15 The Chairman. Aye.

16 Mr. Lighthizer. Mr. Roth.

17 The Chairman. Aye.

18 Mr. Lighthizer. Mr. Danforth.

19 Senator Danforth. Aye.

20 Mr. Lighthizer. Mr. Chafee.

21 Senator Chafee. Aye.

22 Mr. Lighthizer. Mr. Heinz.

23 Senator Heinz. Aye.

24 Mr. Lighthizer. Mr. Wallop.

25 Senator Wallop. Aye.

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

1 Senator Mitchell. Aye.

2 Mr. Lighthizer. Mr. Chairman.

3 The Chairman. Aye.

4 I didn't mean to interrupt Senator Grassley, but I
5 wanted to have this vote.

6 Did you have any questions on that one area?

7 Senator Grassley. No. I was just asking that point
8 for clarification purposes.

9 The Chairman. On this vote the aye's are 17. The
10 nay's are zero. Absentee members will be permitted to
11 register their vote.

12 Senator Long. Could I just ask Mr. Chapoton a
13 question about this depreciation matter?

14 Mr. Chapoton, it is my understanding of this whole
15 situation on depreciation that what the business community,
16 small business as well as big business would prefer would
17 be first year expensing. They fail to ask for first year
18 expensing only because they doubted they could pass it
19 through the Congress.

20 That first year expensing is so much simpler that
21 anybody, anybody in this room can understand it and handle
22 it very easily.

23 The accounting cost savings alone would run into
24 hundreds of millions, maybe billions of dollars. That is
25 really where we ought to be headed.

1 Now, for the same number of dollars, in other words,
2 if you think in terms of what system, where we ought to be
3 going and thinking in terms of what the revenue loss would
4 be one way or the other, it seems to me that everybody
5 would prefer, that every businessman in American who has
6 the problem, would prefer to go the expensing route rather
7 than to go the 10-5-3 and any other route where he has to
8 keep a vintage account and keep a record of when he bought
9 the piece of equipment and take so much off each year and
10 hire himself an accountant to do something he can do for
11 himself under expensing.

12 That is where we ought to be going, if we can. I
13 had the impression and we had the witnesses before us,
14 this gentleman from Harvard, Professor Jorgensen, we had
15 him on the one hand and we had these other people on the
16 panel who apparently were there to differ with Dr. Jorgensen
17 they all wind up agreeing.

18 For the same number of dollars, expensing is the
19 better answer. My thought about it is that regardless of
20 whether you want to have an investment tax credit as a
21 subsidy or do not want to have an investment tax subsidy,
22 tax credit subsidy, regardless of whether you want to have
23 a negative tax rate or do not want to have a negative tax
24 rate. In either event, for the same number of dollars,
25 expensing is the better answer.

1 Now if that is the case, why don't we do it?

2 Mr. Chapoton. Senator Long, expensing has a lot of
3 desirable features. You are perfectly correct.

4 Senator Long. Compared to the alternative, it has all
5 the desirable features.

6 (Laughter.)

7 Mr. Chapoton. Of course, it is correct that in whatever
8 you do in the tax system businesses are required to keep
9 books on their assets, are required to compute book
10 depreciations, so the bookkeeping might be simplified,
11 doesn't go away.

12 The difficulty, as we see in the proposal, in the
13 Ways and Means Committee, we are trying to get expensing,
14 is it takes a very long time to get there. In doing so
15 you keep a system that nobody seems to be satisfied with
16 now.

17 In doing so, you do not give as much present value to
18 the cost recovery benefits as you can do by a system such
19 as we have proposed.

20 Senator Long. Well, you say it takes a very long
21 time. But my thought is, you know, you don't get there in
22 a day, going with your 10-5-3.

23 So, my thought is that if you -- even if you look at
24 that problem, by the compromises that have been made, you
25 still have several years to do it.

1 My thought is that if for some reason you can't afford
2 to go to full expensing, you can go to 90 percent expensing
3 or 95 percent expensing or whatever it takes and go to that
4 as the interim step, which is a very simple way of doing
5 business rather than to one go from the 10-5-3, with the
6 complexities that that involves, and then have to eventually
7 have to wind up going to expensing anyway.

8 It seems to me that the logic of expensing makes so
9 much more sense in terms of what you are trying to achieve
10 than it does to get there by arbitrary assumptions and the
11 complexities that are involved and the rest of it.

12 Rather than have the change over twice, we ought to
13 do it just one time and take dead aim on where we want to
14 go and head there directly.

15 Mr. Chapoton. Well, the problem, I agree with some
16 of your statements. The problem is the House Bill, the
17 Ways and Means Bill, as proposed, costs about the same in
18 dollar revenues, '81, '82, '83 and '84 as the Administration's
19 proposal.

20 But, you have to realize they allow only expensing of
21 20 percent in the first year and then jumping to 40 and 60.

22 When you do that, you are spending the same amount of
23 money, because the Federal Government operates on a cash
24 basis of accounting, dollars in, dollars out, but you are
25 not giving as much present value benefit as our proposal.

1 So, you are having present value benefit to a business
2 that is deciding whether or not to make an investment and
3 you are keeping a system in place that we don't like.

4 Now, there are alternatives of getting to expensing
5 as you suggest, as you would know. You could go to our
6 system and you could kick over to expensing later.

7 There are all sorts of varieties. But, to get the
8 incentive effect we need in these next few years, we do not
9 think a phase in of expensing can do it.

10 Senator Long. But, you are saying, if I understand
11 your answer though, I believe you are agreeing with me that
12 expensing is the better answer to the problem. Just leaving
13 out the phase-in period. Leave that out for the moment.
14 Between what the objective is you are trying to achieve,
15 expensing is a better answer to the problem.

16 Mr. Chapoton. Senator, I wouldn't necessarily say it
17 is the better answer to the problem. I would say it is a
18 very good system.

19 You do have -- and we looked last night in some detail
20 over when you make the assumption you are now making, that
21 you ignore the phase-in period, which is a very difficult
22 part of it.

23 But if you ignore that, the problems you might have
24 and benefits you would have from expensing. I can tell you
25 expensing is a good system.

1 Senator Long. It just seems to me that if that is the
2 answer, and I believe if we go back and take all the witnesses
3 that came before this Committee, testifying for 10-5-3, and
4 a lot of them, if they tell you what they honestly and
5 sincerely believe about this matter, aside from the expedi-
6 ency of the moment, they would all tell you that expensing
7 is a better answer.

8 That being the case and I know small business would
9 say beyond any doubt. I read what Mr. Greenspan said about
10 expensing. For small business, expensing would just make
11 them think, where did these wonderful people come from that
12 came up with this expensing as the answer.

13 Now, if we think that is really the answer, I would
14 think that we might be well advised, and you would be well
15 advised to work with us and see if we can't better meet the
16 problem that you find standing in the way, that is the phase
17 in aspects of it, to see if we can't find a better way to
18 get from here to there.

19 Because, if what you are trying to get to is a better
20 mousetrap, I don't see why we shouldn't work to that rather
21 than work to something that still is not as good as where we
22 ought to be.

23 Mr. Chapoton. Senator, we have indeed looked at expensing
24 earlier and we confronted the very problem that the Ways and
25 Means Committee has confronting and that is the phase-in

1 period.

2 The Chairman. Senator Heinz.

3 Senator Heinz. Mr. Chairman, regardless of whether
4 we go Senator Long's way or whether we go the Treasury way
5 on appreciation or expensing of plant and equipment, 5 and
6 3, we have no other problem I hope the Committee is attentive
7 to.

8 We have some very, very critical industries that
9 because of provisions in the Tax Code over the last several
10 years and also because of the way previous Administrations
11 have administered such laws as the antidumping law, the
12 countervailing duty law, that have a very large backlog of
13 unused tax credits.

14 Now, they include such industries as mining, steel,
15 airlines, paper, railroads, automobiles, probably everybody
16 familiar with the case of Chrysler and or Ford Motor Company
17 which we would like to see every single business stand on its
18 own two feet, you have the very peculiar situation that here
19 is the second largest automobile company in the United States
20 Ford, probably the second largest in the world, and the way
21 the law is going to operate, General Motors is going to get
22 tens, maybe hundreds of millions of dollars of tax credits
23 because they are still making some money.

24 Ford, which is a major competitor to General Motors,
25 is kind of in difficulty, some would say teetering on the

1 edge, and they are not going to get any advantage from tax
2 credits at all, because they don't have any taxes, having
3 no income, having losses, to offset those tax credits against.

4 The result is that the rich get richer and the poor get
5 poorer. It is going to be pretty poor for all the auto
6 workers of Ford and all the other places like that if they
7 go out of business.

8 I think we need to find a means of addressing this
9 very, very serious problem.

10 Now it turns up the Administration is attempting to
11 address this by attempting to be liberalizing, leasing. As
12 I understand the Administration's proposal on leasing, they
13 are trying to bring about a situation where in effect, at
14 least prospectively, there will be the opportunity for these
15 capital intensive industries, is what they mainly are, to
16 find a way to get value out of their tax credit, even if they
17 have to go in effect to another party, leasing.

18 Now, I think in theory, leasing may have a lot of
19 advantages. In practice, there are a lot of real problems
20 as a means of achieving the Administration's and mine, and
21 I think other Senators' objectives.

22 The two practical problems are that there are many
23 industries that are -- need to modernize. You can't very
24 practically lease half of a continuous process steel mill that
25 has already been built. Maybe some magic magician might be

1 able to do it, but it is pretty difficult to get some of
2 these industries into a position where they can lease a
3 part of an integral operation.

4 Secondly, there is no guarantee that the leasing
5 provisions aren't going to make a lot of leasing companies
6 awfully rich. There is no guarantee that all these supposed
7 benefits in leasing are going to go to the companies, the
8 people who need and use and operate plant and equipment we
9 are talking about, that the benefits are really going to get
10 to them. They are going to be at the mercy of people with
11 money.

12 Leasing companies somehow or another get money and
13 then they buy or build something for you and then you pay a
14 rent on it.

15 Well, you know, we all know that ownership is nine-
16 tenths of the law, and maybe it is going to end up with
17 nine-tenths of the benefit, the investment tax credit, and
18 that is the leasing company that is going to get it.

19 I am not against leasing companies, per se, but I
20 think we don't want to claim that they are the solution to
21 the problems of these industries that I have mentioned.

22 So, one of the things that I want to ask for my
23 colleagues' attention to is the addressing of this problem.

24 I am working on a proposal. I am not going to present
25 it now. It is not the right time to present it, and it is

1 not fully scoped out at this point, but basically, I think we
2 ought to permit these kinds of companies, these kinds of
3 industries to at least carry back their tax credit for ten
4 years and be able to take advantage of it.

5 One of the rationales for doing that is that we had
6 some restrictions, very, very serious restrictions on the
7 utilization of tax credits in previous years where only 25
8 percent on point of net income could be offset by investment
9 tax credits and it rose to 50 percent and so forth and it
10 will rise eventually I guess to 90 percent, this year or
11 next.

12 But, the result of those provisions in the previous
13 law was to take away from our most capital intensive in-
14 dustries that which we said we were giving them with the
15 other hand.

16 It remains therefore, a real inequity. It may in fact
17 be one of the causes why we are not as competitive as we
18 would like to be internationally.

19 It is something that has been ignored. I think it is
20 time to stop ignoring the problem, unless we want a lot more
21 unemployment on our hands. Unless we want a lot more business
22 failures on our hands.

23 So, I think we have the opportunity here to structure
24 something that will work within what the Administration is
25 doing.

1 Let me say, I think we have the opportunity here to
2 structure something that will work within what the Adminis-
3 tration is doing.

4 Let me say to the Administration that claims much
5 for their \$29 billion, over five year leasing provision,
6 that if in fact your leasing provision works the way that
7 you say it will, there is really not much, there should not
8 be any net revenue loss by allowing what I am proposing as
9 an election for people.

10 You believe that leasing will allow the unused in-
11 vestment tax credit to be transferred. I believe that in
12 fact that is impractical, even though you do not, then there
13 shouldn't be any net cost to Treasury under what I propose.

14 So, Mr. Chairman, I wanted to put myself on record
15 as being concerned about this problem. I know many of my
16 colleagues expressed a great deal of concern about this.
17 Senator Bentsen is concerned about it. Senator Long is
18 concerned about it. I have talked to Senators Danforth,
19 Chafee and Symms. I know Senator Grassley is concerned about
20 it. Senator Armstrong is, too.

21 There may be other people who are concerned too. I
22 think Senator Matsunaga has expressed concerns.

23 I don't know if that is all Senators or not, but it is
24 getting pretty close.

25 The Chairman. Eleven concerns.

1 Senator Heinz. We have a lot of -- a majority of
2 concern.

3 The Chairman. I wonder how many votes that would be.
4 (Laughter.)

5 The Chairman. Put me down as being concerned.

6 (Laughter.)

7 The Chairman. But, I would say, in answer to the
8 Senator's statement, that we did recognize there was that
9 problem and it is listed in the index. You probably noted it
10 as under negotiation.

11 I might --

12 Senator Heinz. Does Mr. Chapoton have anything he would
13 like to say?

14 The Chairman. Probably not.

15 (Laughter.)

16 Mr. Chapoton. Senator, as you probably know, we are
17 concerned.

18 Senator Heinz. You can't vote, but we can listen to you
19 anyway.

20 Mr. Chapoton. We are concerned about this problem.

21 The Chairman. There are 12 concerns right there.

22 (Laughter.)

23 Mr. Chapoton. We do think our leasing proposals move
24 in that direction. We do not know and have not seen another
25 proposal that is workable, that would allow some suggest, free

1 transferability of deductions and credits.

2 We would be happy to look at such a proposal. I
3 would say though, if you have absolute free transferability
4 of deductions and credits, you would have a significant
5 revenue cost above what our leasing proposal is shown to
6 be because there are constraints under leasing rules now.
7 The lessor does have to have an investment, a 10 percent
8 investment in the property. That in itself is a constraint.

9 You also have to assume, there is no end of technical
10 problems if you try to rewrite the Internal Revenue Code to
11 allow for greater transferability, what you do about re-
12 capture and what you do about business acquisitions.

13 All these rules, all these problems are addressed under
14 present law with respect to leasing rules. We think a
15 liberalization of the leasing rules is by far the best way
16 to address these problems.

17 Senator Heinz. But you are persuaded.

18 Mr. Chapoton. I am persuaded it is a problem.

19 Senator Heinz. Mr. Chairman, it reminds me of Senator
20 Long having had discussions with previous Treasury people
21 and I remember Senator Long sitting back and saying one
22 day, "Your lips say, no, no, no, but your eyes say yes, yes,
23 yes."

24 (Laughter.)

25 Mr. Chapoton. In that event, maybe I better add that

1 I am thinking "No, no, no, beyond our leasing proposals,
2 as well."

3 (Laughter.)

4 Senator Long. Might I just correct the Senator. That
5 old song goes like this.

6 (Laughter.)

7 Senator Long. "Your lips may say no, no, but there is
8 yes, yes, in your eyes."

9 (Laughter.)

10 The Chairman. I want to recognize Senator Mitchell.
11 But, I wonder if there would be any objection to -- you
12 know the corner stone of the President's program has been
13 across the board cuts. That has now been modified so it is
14 5 percent effective October 1, '81, additional 10 percent
15 effective July 1, '82, and a final 10 percent effective
16 July 1, '83, across the board.

17 I would hope we might have some resolution of that.
18 I don't know of any objection to that. If there is, we
19 could have a roll call.

20 Senator Mitchell. Mr. Chairman, I wasn't a member of
21 the Committee last year. I noted with interest the Committee's
22 actions. It included a number of provisions affecting small
23 business.

24 I just, along with the other members of the Committee,
25 have just received this package this morning which we are

1 now discussing.

2 I don't see on the list many of the items that were
3 included in the Committee's action last year.

4 I, myself, have introduced legislation involving
5 inventory accounting for small business. I am very much
6 concerned about special needs and requirements for small
7 business.

8 I wonder if we could get any explanation perhaps, of
9 why there are no such comparable provisions in the proposed
10 legislation.

11 Mr. Chapoton. Senator, the small business benefit
12 under this bill has arisen frequently, that question has
13 arisen frequently.

14 We think there are very substantial benefit for small
15 business, not only obviously to the extent that small
16 business makes capital investment, they enjoy the benefits
17 with all other business.

18 In addition, the individual rate cuts will significant-
19 ly benefit small business, because the great preponderance
20 of small business is operated in non-corporate form, either
21 through partnerships or sole proprietorships.

22 So that you are talking about significant rate cuts
23 for those small businesses.

24 In addition, in the proposal, the so-called add on in
25 these proposals, estate and gift tax relief is added, which

1 has been number one or number two on the list of most small
2 business groups. They are strong supporters of estate and
3 gift tax relief. That was a consideration in adding that
4 to this bill.

5 Senator Mitchell. Well, of course, all of the
6 general benefits, I am not sure about the estate and gift
7 tax, the other general benefits suggested for small business
8 as well as for others, were present in some form in last
9 year's bill.

10 Yet, the Committee saw fit at that time to add a
11 number of additional provisions for small business.

12 So the rationale suggests it doesn't apply at least
13 in comparison to what this Committee did last year.

14 Mr. Chapoton. I understand that. I am simply explain-
15 ing our proposal and why we do think it has significant
16 benefit for small business.

17 Finally, let me mention that the added on the list
18 before the Committee today, is the used property investment
19 tax credit, which of course, as you well know, is a small
20 business -- has been strongly supported by small business
21 groups.

22 The Chairman. And the incentive stock option.

23 Mr. Lighthizer. Senator Mitchell, the estate and
24 gift tax provision that is in here was not in last year's
25 bill.

1 The Chairman. I might say further, this is another
2 matter that we have been discussing, because there has been,
3 just as you have expressed interest, others have expressed
4 interest.

5 There were a number of suggestions made in the task
6 force, headed by Senator Durenberger. We did make a
7 recommendation to the Administration on changing the rates.
8 That was not approved.

9 They did approve the used equipment change.

10 I am not certain they have approved the stock option
11 change, but at least that provision will be added to the
12 bill I hope to introduce.

13 Senator Mitchell. I just want to say that it is clear
14 that at least insofar as this Committee last year felt that
15 small business was deserving of some special provision, that
16 concern is far less significant in the present proposal
17 than it was last year.

18 One can argue that it wasn't appropriate last year,
19 but I don't think you would dispute that, would you, Mr.
20 Chapoton.

21 Clearly, comparing the benefits to small business of
22 last year's bill with this year's bill, those benefits were
23 substantially greater last year.

24 The present proposal does much less for them.

25 Mr. Chapoton. Senator, I might dispute that, and I

1 would have to look and compare them side-by-side, but the
2 estate and gift tax provision is so significant to small
3 business, that that alone might outweigh --

4 The Chairman. Plus, we have a much larger individual
5 rate.

6 Mr. Chapoton. And much larger individual rate cuts,
7 of course help.

8 The Chairman. It is now 12:00 o'clock. I would like
9 to get an expression from the Committee on the 5-10-10
10 proposal.

11 Senator Bradley.

12 Senator Bradley. Mr. Chairman, on this matter, I will
13 have at least two amendments, on the 5-10-10 proposal.

14 So, I would ask of you, I would refrain from moving
15 with the 5-10-10 until we could at least have the opportunity
16 to discuss the two amendments I would offer.

17 One deals with targeting the individual income tax
18 relief much more directly to middle and lower income people.
19 That is, since I support the reduction of the investment
20 income rate from 70 to 50, I have talked with quite a few
21 individuals who say that is enough of a break for people
22 with more than \$50,000.

23 These are people with more than \$50,000, telling me
24 this. Therefore, rather than bunch the bulk of the individual
25 rate cut at the top of the income scale, I would like to

1 target it to under 50. I have an amendment to do that.

2 Then I also have an amendment that relates to the
3 third year of the tax cut, and its relation to economic
4 performance.

5 I think that all of us, given what present interest
6 rates are would argue that a tax cut next year might be the
7 needed remedy for the kind of a slow down we are headed for.
8 The concern is further out. I would like to have the oppor-
9 tunity to discuss that and submit the amendment.

10 Senator Danforth. Mr. Chairman, I don't know what you
11 intend to do at this point on this. But, again, tax bills,
12 they have always been subject to further amendment until
13 they are actually reported out.

14 Therefore, a consensus vote right now, it would seem to
15 me would be appropriate.

16 It is your idea. I think it is in fact the right time
17 to get a general sense of the Finance Committee.

18 The Chairman. I certainly don't want to preclude any
19 amendments being offered and action on this amendment would
20 be subject, as it has been over the years, to reconsideration,
21 amendment, modification.

22 I would like to have some expression today on the
23 general principle. You may modify it successfully, or you
24 may trigger the third year.

25 When I make the motion, it is not to deprive you of any

1 rights you have in this regard.

2 Senator Bradley. So, it is your view that this is
3 simply a sense of the Committee.

4 The Chairman. Right.

5 Senator Bradley. It is not an approval of the specific
6 5-10-10 cuts, since we haven't even seen the material.

7 It is just basically an approval of that direction.

8 The Chairman. I think we have -- I say we deal in
9 concepts much of the time here. This has been rather spelled
10 out rather precisely by the President a number of times.

11 If we agree on this, it is certainly subject to change,
12 but if it is not changed, then it would be the decision of
13 the Committee.

14 Senator Bradley. So that the vote you would be taking
15 would be the final vote of the Committee on the 5-10-10 cut?

16 The Chairman. You may offer substitutes, amendments,
17 modifications. All it would be would be a tentative decision
18 by this Committee that that is the position we adopt. It
19 can be changed to 4-9-9, or you can make it 10-10-10, if
20 you want to go all out. We are not advocating at this point.

21 Is that all right?

22 Senator Bradley. Well, I will offer those amendments.
23 I don't know about my other colleagues here, but that is fine.

24 The Chairman. Senator Matsunaga.

25 Senator Matsunaga. Mr. Chairman, I have no objection

1 to the concept.

2 One question. Under your proposal, will the acceler-
3 ated depreciation apply --

4 Mr. Chapoton. Under the bill, it does apply, 15 year
5 life, 200 percent declining balance depreciation for rental
6 real estate.

7 The Chairman. Let us just call the roll on this.

8 Senator Mitchell. Could I just say one thing. We are
9 apparently now voting on whether we favor an individual cut
10 of 5-10-10.

11 The Chairman. Right.

12 Senator Mitchell. I intend to vote against it, not
13 because I am opposed to a tax cut, but because, like Senator
14 Bradley, I feel it should be weighted more heavily toward
15 middle income taxpayers.

16 I just want to make that clear that those of us, I
17 can't speak for Senator Bradley --

18 Senator Bradley. You may speak for me.

19 Senator Mitchell. -- those of us who are voting against
20 a 5-10-10 tax cut are not voting against a tax cut. We are
21 voting against this precise form.

22 The Chairman. I understand.

23 Senator Bradley. Also, it should be made clear that
24 my intention to offer the targeted individual rate reduction
25 amendment is made because I support the reduction from 70 to

1 50 of investment income.

2 Therefore, I feel that is taking care of the upper
3 income individual.

4 The Chairman. I certainly understand that. I can
5 assure any member that they are not going to be shut off,
6 amendments to be considered, reconsideration.

7 I would like, as we have done in the past, to show
8 some progress, at least on concepts of tentative decisions.

9 Mr. Lighthizer. Mr. Packwood.

10 (No response.)

11 Mr. Lighthizer. Mr. Roth.

12 The Chairman. Aye.

13 Mr. Lighthizer. Mr. Danforth.

14 Senator Danforth. Aye.

15 Mr. Lighthizer. Mr. Chafee.

16 Senator Chafee. Aye.

17 Mr. Lighthizer. Mr. Heinz.

18 (No response.)

19 Mr. Lighthizer. Mr. Wallop.

20 The Chairman. Aye.

21 Mr. Lighthizer. Mr. Durenberger.

22 The Chairman. Aye.

23 Mr. Lighthizer. Mr. Armstrong.

24 The Chairman. Aye.

25 Mr. Lighthizer. Mr. Symms.

1 Senator Symms. Aye.

2 Mr. Lighthizer. Mr. Grassley.

3 Senator Grassley. Aye.

4 Mr. Lighthizer. Mr. Long.

5 (No response.)

6 Mr. Lighthizer. Mr. Byrd.

7 (No response.)

8 Mr. Lighthizer. Mr. Bentsen.

9 Senator Bentsen. Aye.

10 Mr. Lighthizer. Mr. Matsunaga.

11 Senator Matsunaga. Aye.

12 Mr. Lighthizer. Mr. Moynihan.

13 (No response.)

14 Mr. Lighthizer. Mr. Baucus.

15 (No response.)

16 Mr. Lighthizer. Mr. Boren.

17 Senator Boren. Aye.

18 Mr. Lighthizer. Mr. Bradley.

19 Senator Bradley. No.

20 Mr. Lighthizer. Mr. Mitchell.

21 Senator Mitchell. No.

22 Mr. Lighthizer. Mr. Chairman.

23 The Chairman. Aye.

24 Those who are not present will be permitted to record
25 their vote.

