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EXECUTIVE SESSION

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THURSDAY, MARCH 17, 1977

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

The Committee met, pursuant to recess, at 10:05 a.m. in room 2221, Dirksen Senate Office Building, Hon. Russell T. Long (Chairman of the Committee) presiding.

Present: Senators Long, Byrd, Ribicoff, Gravel, Bentsen, Hathaway, Haskell, Matsunaga, Moynihan, Curtis, Hansen, Dole, Roth, Laxalt, Danforth.

The Chairman. I hope we will have some Senators here in short order so we can get down to business and move ahead with this bill. I have here some correspondence addressed to me by Senator Talmadge involving the Hale Champion nomination as Under Secretary of Health, Education and Welfare. This matter will be discussed further, but I think that this can be made available so that people can judge for themselves what the question is all about.

So I would ask that that be released and be made a part of the record of the hearing.

(The material to be furnished follows:)

COMMITTEE INSERT

1           The Chairman. I would suggest to the Senators that if  
2 they have not seen Senator Talmadge's correspondence, they  
3 should take it home with them or put it in their pocket and  
4 read it when they can so they will be familiar with what  
5 Senator Talmadge's question is with regard to the nomination  
6 of Hale Champion. That matter will be discussed at a later  
7 date.

8           I suggest that we not get into it now.

9           I regret that thus far my Democratic colleagues are  
10 not on the scene. I guess they will be along shortly. If  
11 we could go on to another matter --

12           Senator Curtis. Senator, if I could raise a point about  
13 our procedure, I am sure what I am going to ask would be  
14 agreeable to the Chairman because it is the way he has  
15 handled other things.

16           The Minority are unanimous in opposition to the rebate.  
17 We will have probably a series of alternatives to the rebate.  
18 It will not take long to present them.

19           We do not want to rule one out because another substi-  
20 tute has been proposed. All I am asking is to preserve the  
21 right of each member who wants to have considered an  
22 alternative, that he will get a chance to state his propo-  
23 sition and get it voted on separately. That is the way we  
24 have always done it.

25           For the purposes of the record, I wanted to make that

1 clear and thank the Chairman for it.

2 The Chairman. I have this letter from Senator Talmadge.  
3 "Due to a death in the family, I am unable to attend today's  
4 Executive Session of the Committee on Finance. I thereby  
5 authorize you to vote my proxy."

6 Senator Talmadge, not being here, has asked that we  
7 hold up the nomination of Hale Champion until he could be  
8 here. I thought it would be today. He is not here. We  
9 will have to postpone it.

10 I know of no opposition to the nomination of Thomas  
11 D. Morris to be Inspector General. If there is no objection  
12 to Mr. Morris, why do we not confirm that nomination?

13 Without objection, he is confirmed.

14 The nomination of Arabella Martinez to be Under-secretary  
15 of Human Development to HEW, without objection, I suggest that  
16 be confirmed.

17 What is the fiscal year 1977 allocation?

18 Mr. Stern. That was a matter that you did take up  
19 the other day.

20 The Chairman. Have we disposed of it?

21 Mr. Stern. You have taken care of it.

22 The Chairman. Very well.

23 I wanted to get my Democratic colleagues over here.  
24 Senator Talmadge will not be here because of a death in his  
25 family. I have been notified that the others expect to be

1 here.

2 Is that Democratic Caucus still going on?

3 Senator Haskell. When I left, it still was not through,  
4 Mr. Chairman.

5 The Chairman. That is a problem. It may be we might  
6 talk about some of the other matters. I do not want Mr.  
7 Schultze to make his presentation without our Democrats here,  
8 for reasons that I think are fairly obvious.

9 I wonder if we might dispose of some of the other  
10 matters that we have been discussing, for example, I was  
11 just thinking, can you tell us the information we were  
12 thinking about in regard to what it would cost if we had  
13 this refundable tax credit apply to the railroads and to  
14 the airlines only?

15 Can you tell me what that would cost?

16 Mr. Shapiro. Yes, Mr. Chairman.

17 A 10 percent refundable investment tax credit for our  
18 railroads and airlines is \$220 million. At the level of  
19 12 percent it would be \$264 million.

20 The Chairman. How much?

21 Mr. Shapiro. For railroads and airlines, for both of  
22 them at the 10 percent level in present law, it would be  
23 \$220 million.

24 The Chairman. \$220 million?

25 Mr. Shapiro. Yes. If you had a 12 percent investment

1 and made that refundable for airlines and railroads, it  
2 would be \$264 million.

3 The Chairman. \$260 million. All right.

4 Senator Curtis. If we did that, that would take up  
5 yesterday's request that we have some language?

6 Mr. Woodworth. Yes, it would.

7 The Chairman. So far, I take it that what we are  
8 talking about doing, we would still appear to be within the  
9 figures of the Budget Resolution. If we did this, would we  
10 be within the budget figures?

11 Mr. Shapiro. This is for 1977. Yes, you would be.  
12 This is a full-year effect. Most all of it would be in  
13 fiscal '78, so that you would be within it for that time.

14 The Chairman. Do you think we ought to do that, Senator  
15 Curtis?

16 Mr. Shapiro. That is assuming the Budget Committee  
17 allows the additional billion dollars you requested. As of  
18 right now, you have sent your letter over; there has been no  
19 action on it.

20 The Chairman. The billion dollars we would like to have?

21 Mr. Shapiro. If they grant you that, you are all right  
22 in the spirit.

23 The Chairman. It would cost about \$264 million to make  
24 the investment tax credit a refundable tax credit for the  
25 railroads and the airlines, if you limit it to just those two.

1 Senator Curtis. I think it should be done.

2 Senator Packwood. I have a question.

3 The Chairman. Senator Packwood?

4 Senator Packwood. I have a question of equity and, in  
5 the spirit of openness, I have been contacted by a Portland  
6 company -- Evans Products. They make 40 percent of their  
7 profits by leasing railway cars to railroads.

8 They say it is unfair, if we give the investment tax  
9 refundable credit just to the railroads, then it is going to  
10 be a disincentive for the railroads to continue to lease  
11 their cars from this company, which is in a legitimate busi-  
12 ness, because they get no refundable credit.

13 The Chairman. My impression is, what has been happening  
14 is that airline companies and railroad companies that need  
15 rolling stock or airplanes, as the case may be, where they  
16 are not in the profit column, have had to give up, in effect  
17 to give up their investment tax credit in order to buy  
18 equipment.

19 They have had to borrow that money. The lender has  
20 made money.

21 The advantage of the tax credit for a company like  
22 Pan American Airlines has to be given away to the bank in  
23 order to get the bank to buy the equipment and lease it to  
24 them.

25 The idea of the tax credit was not to give it to some

1 outside group but to make it possible for these companies  
2 to buy the equipment that they were going to need.

3 Senator Packwood. To the extent that Evans Products  
4 makes money, they get the investment tax credit; to the  
5 extent that they lose -- and they have lost money in some  
6 years; they are a large company. They would like to have  
7 the same equality of treatment, so that when they build  
8 railway cars they would get a refundable tax investment  
9 credit for doing the same thing that we are encouraging the  
10 railways to do.

11 I am sure we could work out some sort of harmonious  
12 arrangement, that we could extend it to them or companies  
13 like them.

14 Senator Haskell. If I could comment, I think that since  
15 the investment tax credit is, in fact, a subsidy, there is  
16 a very good argument that the people who need it the most,  
17 the people who do not make money, should get it. I think  
18 that it is a very good argument; I think that it is logical.

19 I do not think it is logical to single out a couple of  
20 industries. I think that compounds inequity.

21 Perhaps there is some way of making a partial refundable  
22 across the board that would have the principles of equity  
23 behind it and still stay within the budget.

24 The Chairman. It may meet your objections if we said  
25 all right -- Mr. Woodworth, maybe you have some suggestions --

1 to say, this applies to railroad rolling stock; it applies  
2 to the laying of rails -- I guess you would want to apply  
3 it for that, would you not? If they are trying to repair  
4 their rails to get them in shape, would that be subject to the  
5 investment tax credit?

6 Mr. Shapiro. Yes.

7 Mr. Woodworth. Yes, it is.

8 The Chairman. If you say it applies to railroad rolling  
9 stock, it applies to airplanes, what else would we need to  
10 apply it to?

11 Mr. Shapiro. You are talking about leasing companies?

12 The Chairman. What I was thinking of, if you say you  
13 get a refundable tax credit if you are buying the following  
14 items.

15 Senator Haskell. Mr. Chairman, you misunderstand me.  
16 What I am saying to apply to just a couple of industries  
17 does not seem fair. For example, it would be a new business  
18 that would be started up in some other line of endeavor. If  
19 you are going to subsidize plant and equipment, we ought to  
20 do it across the board. The new business is probably not  
21 making money.

22 What I was suggesting was that possibly there be some  
23 way of giving partial refundability to everybody entitled  
24 to it in a given year. Maybe in succeeding years, give the  
25 balance.



1 Senator Curtis. I realize that there are many businesses  
2 that are in need. The argument for the transportation  
3 industries, most of the transportation industries of the  
4 world are government owned. Ours are not. When they make  
5 money, they do pay taxes, and they pay a lot.

6 Our airlines are in very tough competition with the  
7 foreign government-owned airlines. Our railroads are needed  
8 right now.

9 It is so related to the energy crisis. The additional  
10 freight, particularly coal, that is needed to be hauled --  
11 it is in the public interest that tracks and cars and  
12 trains and the whole service be improved in order to meet  
13 the real national need.

14 I am not degrading the fact that other industries are  
15 in distress, but that is a particular logic.

16 Transportation companies are in distress. A lot of  
17 them, unless they have other properties other than railroads,  
18 and there is a peculiar situation with our airlines.

19 The Chairman. Senator Kennedy made a pitch, and he made  
20 a fine statement, saying that we ought to make the tax credit  
21 refundable for all people. If we did that, it would cost  
22 about \$3.5 billion.

23 Some of the beneficiaries would be people who never pay  
24 income taxes, like churches, universities, foundations and  
25 various other nonprofit organizations, so that it raises a

1 broad question that one of these days we ought to legislate in  
2 this regard one way or the other. As much as I favor the  
3 concept of a refundable tax credit, the investment tax  
4 credit for example, looking at the budget figures, if we put  
5 a \$3.5 billion in here, we have to strike out the 2 percent  
6 additional investment tax credit they want to provide for  
7 everybody else.

8 What you are confronted with is trying to do the best  
9 you can with what you have to work with.

10 Here are two industries where some of their members are  
11 very much distressed, need the benefit of it. We could  
12 provide it for them in those two industries and put more  
13 people to work.

14 I do not know if you had seen that letter ConRail sent  
15 over here. I think they have tried to provide a copy to all  
16 Senators. I would like it asked to be made a part of the  
17 record.

18 (The material referred to follows:)

19 COMMITTEE INSERT  
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1           The Chairman. They make a very appealing case. They  
2 would like to put more people to work. If they could get  
3 the investment tax credit, every nickel of it will be used  
4 to put more people to work.

5           The same thing is true, in one respect or the other,  
6 with regard to some of the airline companies that just do  
7 not get the benefit of the investment tax credit because to  
8 buy an airplane company, a company like Pan American has  
9 to go out here and ask the bank to buy the airplane, they  
10 lease it from the bank in order to get the airplane to provide  
11 the service. That means they do not get the investment  
12 tax credit; the bank makes that money, because the bank can  
13 get it by virtue of the fact it is in a profit position.

14           If you simply take the view that we will try to extend  
15 this principle in some areas where it is needed the most, if  
16 you extend it to the airlines and to the railroads, I think  
17 it would be all right with me to take care of the situation  
18 you are talking about, Senator Packwood, where you are talking  
19 about leasing companies that lease that kind of equipment.  
20 If the amendment could be drafted to take care of that  
21 limited situation, I would not have any objection to that.

22           They are leasing it, and if they fall on bad times, they  
23 would get the investment tax credit as well. But if you try  
24 to go beyond the type thing that these airlines and railroads  
25 use, then you are in for a huge cost factor.

1           What is your thought, Mr. Woodworth?

2           Mr. Woodworth. I would just like to say, if you did it  
3 with respect to the equipment, you in fact would be allowing  
4 the refundable credit to banks. I am not sure that that is  
5 what your intention is.

6           Senator Packwood. Only if they have a loss.

7           The Chairman. If they are losing money.

8           Mr. Woodworth. That is correct. But they are probably  
9 one of the biggest owners of aircraft in the United States.

10          The Chairman. Is that not why they are the biggest  
11 owners, if the credit is not refundable?

12          Mr. Woodworth. That is correct.

13          The Chairman. It is a business they do not particularly  
14 want to go into. They are accomodate their customers -- they  
15 are making money at it, by the way.

16          Senator Packwood is talking about people who make that  
17 their regular business. I suppose if you are going to do it  
18 for the leasing people, if the banks are losing money, they  
19 would get the benefit too. I do not think it would make  
20 any difference.

21          Is it not a fact that the banks who do this kind of  
22 thing for their customers are not in a loss position?

23          Mr. Woodworth. I am not sure. There may be some of  
24 them that are in a loss position because of tax purposes,  
25 even though making money for their shareholders.

1           The Chairman. If it appeals, why do we not take care  
2 of it in regards to the people who are in the airline business  
3 and those who are in the airlines leasing business exclusively,  
4 or in the leasing business exclusively, and then if the banks  
5 think they ought to be considered, we can consider that  
6 later on.

7           Can you draft it that way? I am sure you can.

8           Senator Byrd. Mr. Chairman?

9           The Chairman. Senator Byrd.

10          Senator Byrd. As one who originally opposed the  
11 investment tax credit, I have come to be a supporter of it.  
12 I think it has done good. I am willing to vote to increase  
13 it from 10 to 12 percent, but I think there has to be a  
14 limit as to what we do in regard to the investment tax  
15 credit.

16          I think Senator Haskell makes a good point. If we are  
17 going to the refundable principle, we should go to it across  
18 the board and not single out two or three industries for  
19 that reason. I would be inclined to oppose singling out a  
20 couple of industries.

21          Also, Counsel answered your question a little while  
22 ago in the affirmative that this would be within the budget,  
23 but as Counsel continued on, as I understand it, it will  
24 only be within the budget limits if the Budget Committee  
25 approves the letter that has just gone to it, and they have

1 not yet acted on it.

2 So we will be going above the budget if we approve this  
3 proposal, as I understand it.

4 The Chairman. Let us understand this, that we are not  
5 bound by the First Budget Resolution. The First Budget  
6 Resolution is a pious hope. It is the Second Budget  
7 Resolution that is binding.

8 Whether the Budget Committee approves this or not for  
9 fiscal 1978, we are not bound by that. We are free to do  
10 whatever we want to do about it.

11 Is that not right?

12 Mr. Stern. If you take up a revenue bill in the upcom-  
13 ing fiscal year before May 15th of the year, you do have to  
14 get a waiver from the Budget Committee. That was done on  
15 the House side; I expect that we would do it here.

16 The point is that there is not really a First Budget  
17 Resolution yet. At this time, the only revenue estimate for  
18 purposes of the First Budget Resolution is this Committee's  
19 ~~recommendation~~ to the Budget Committee, and that is \$1 billion  
20 higher than the House bill.

21 So far you have not added to the cost of the House bill  
22 in 1978.

23 The Chairman. For 1978, we do not need any Resolution  
24 from them up until the Second Budget Resolution.

25 Mr. Stern. You will need a waiver from the Budget

1 Committee in order to take up a revenue bill before May  
2 15th that affects the upcoming fiscal year.

3 Mr. Shapiro. The way you have it on the House side,  
4 the Ways and Means Committee needs; to go to the Budget  
5 Committee for a waiver with respect to the extention of the  
6 1977 costs, because that was something in fiscal '78 alone,  
7 as I understand it. Any provision that has a fiscal '77  
8 impact, no matter how small, a fiscal '77 impact, it does  
9 not need a waiver as long as it has a fiscal '77 impact  
10 that is within the budget limit.

11 The only reason the Ways and Means Committee had to go  
12 to the Budget Committee is because one portion of its bill,  
13 only the portion that dealt with the extension of the 1977  
14 tax cuts, had no 1977 effect. Purely a fiscal '78 effect.  
15 That was the only provision they needed a waiver on.

16 If I understand that correctly, and if that is consistent  
17 here, if you make any provision that would have a fiscal  
18 '77 effect, no matter how small, you would not need a waiver  
19 from the Budget Committee with respect to that provision.

20 It would only be if there was no fiscal '77 effect.  
21 The only effect, if there is an effect in fiscal '78, that  
22 is a case where you would need a waiver.

23 These refunds, it would have some effect in '77, which  
24 is small, you would not need a waiver with respect to those  
25 refundable credits.

1 The Chairman. Would these affect '77?

2 Mr. Shapiro. Yes, it would.

3 The Chairman. Then we do not need a waiver.

4 Now, Senator Byrd, in regard to these two industries,  
5 we voted in the Tax Reform Act last year, we selected these  
6 two industries to say that they could have 100 percent, they  
7 could take the investment tax credit against 100 percent of  
8 earnings rather than only 50 percent of earnings.

9 As far as selecting out two industries, we have already  
10 done that; that is the law now. The law in effect this  
11 year -- for how far in the future?

12 Mr. Shapiro. They have the 100 percent ceiling for  
13 two years, 1977 and 1978. Then that ceiling is reduced 10  
14 percentage points each year until it comes back to the 50  
15 percent ceiling generally applicable.

16 The Chairman. We have already established a principle  
17 as far as these two industries are concerned. They would  
18 receive a more favorable tax consideration, but the point is  
19 that, having done that, those needing it the most are still  
20 not going to get the benefit of it. They really do not have  
21 a profit.

22 If you let them take 100 percent, if you want to let  
23 them have some benefit of it, ConRail and the railroads are  
24 not making enough money to claim the investment tax credit.  
25 And you are talking about airlines in that situation, if you



1 want to let them have the benefit of it, you really should  
2 make it a refundable credit.

3 Senator Hansen. Mr. Chairman, I am not a bit unsympa-  
4 thetic to the problems of the airlines and railroads. I  
5 agree in respect to my friends from Colorado and Virginia.  
6 If we look at the problems that farmers and ranchers are  
7 facing today, they are mighty critical. I do not know the  
8 situation in Colorado, but in Wyoming I have talked to  
9 representatives of the bankers. They tell me that maybe  
10 10 percent of the ranchers are going to use their outfits  
11 this year.

12 Let me tell you what happened from '73 to '75. In  
13 1973, the total net ranch and farm income in Wyoming was  
14 \$122 million; in 1974, it dropped down to \$62 million; in  
15 1975, it dropped down to \$14 million.

16 Last year, the average farm and ranch income in  
17 Wyoming was \$1725. That does not pay the rancher a dime for  
18 his whole year's efforts. He gets paid only when everything  
19 else has been paid.

20 If you want to help somebody -- and I repeat again, I  
21 am not unsympathetic to the airlines and the railroads, but  
22 by gosh, these people are losing their outfits. They have  
23 a drought on top of everything else, and that is going to  
24 exacerbate the livestock situation, because they are just  
25 going to have to sell their herds and their flocks simply

1 because they are completely out of grass.

2 If we want to give a refundable investment tax credit  
3 to somebody here, I appeal to you, is a place where we can  
4 be mighty charitable. It might not keep their noses above  
5 water.

6 I do not think that there is a single segment of our  
7 economy more distressed today that I know of than farming and  
8 ranching. Is that your opinion?

9 Senator Haskell. I would agree with you. There is no  
10 question that there are people in Colorado who have been in  
11 business for thirty years who are going broke.

12 The Chairman. If you do not want to do anything for  
13 anybody, that is all right with me; just forget about the  
14 whole matter.

15 Senator Haskell. I have a suggestion, Mr. Chairman, and  
16 that is that we do do something in the investment tax credit  
17 refundability. I happen to agree if we are going to give  
18 subsidies to people we should give it to the folks that  
19 need them and those are the people who are not making money.

20 Maybe the staff could work out some percentage formula  
21 that would apply across the board, and we could roll it in  
22 year after year. All I have is the general idea -- maybe  
23 the staff could work out some percentage formula that would  
24 be within the budget, a certain percentage this year, a  
25 certain percentage next year, a certain percentage the

1 following year until you have eaten it up.

2 Mr. Shapiro. Let me make a few observations.

3 Senator Hathaway has asked about a refund on the first  
4 \$25,000, the first ceiling that we referred to. At the 10  
5 percent level, the present 10 percent investment credit, we  
6 do not have a firm estimate, but it is in the range of  
7 \$500 million to \$1 billion, probably closer to the other, and  
8 maybe \$800 million.

9 If you made refundable only the additional 2 percent, not  
10 the entire 12 percent but the additional 2 percent, it is  
11 in the neighborhood of \$100 to \$200 million.

12 There are several other alternatives that the Committee  
13 could consider. You could refund 1 percent of the additional  
14 2 percent credit. That would be in the neighborhood of  
15 \$500 million. Or you could have a flat dollar ceiling, for  
16 example, \$10,000 or \$20,000 could be refundable.

17 There are various alternatives. If you want to put a  
18 ceiling where everybody could get a 1 percent or a dollar  
19 ceiling, no matter how large a business, he would get no more  
20 than \$5,000, \$10,000 or \$15,000. These are the various  
21 ranges that would keep your revenue costs low.

22 One of the main concerns is not having too much of a  
23 revenue cost.

24 The question is, do you want to give to all businesses,  
25 whereby you could say that 1 percent would be refundable

1 across the board to everybody, or if you wanted to have a  
2 higher amount, \$10,000 or \$15,000 refundable, that would  
3 mean that the larger businesses would not get as much, but  
4 the smaller businesses would get more.

5 The Chairman. When you move on the theory you are  
6 talking about, you are going to be -- you drastically reduce  
7 the help you would give to those whom you know need it very  
8 much and in doing so, defy the principle of tax uniformity.  
9 You are providing it for a lot of people who do not need it  
10 as badly, who have no need of it at all.

11 The people who are in here asking for it are, for the  
12 most part, companies that have not been able to use their  
13 credits for years, and they are having to pay interest on  
14 the money, hoping some day in the future they will be able  
15 to use it.

16 If you do the kind of thing you are talking about doing,  
17 there are a whole lot of people who are not able to use  
18 their credit this year, let us say. This is the first year  
19 they were not able to use it. Later on, they have every  
20 anticipation of using it, carrying it forward, using the  
21 unused credit in the following year.

22 That is not true for those that came in here that they  
23 very much need some help.

24 I wanted Mr. Schultze to make his statement. Let Mr.  
25 Schultze speak with regard to the Administration's view with

1 regard to this refund of the \$50 which is the big item in  
2 this bill and explain why he feels that we need to do this  
3 at this time.

4 Go ahead.

5 Mr. Schultze. Thank you, Mr. Chairman. I will try to  
6 be brief, if I can.

7 I want to make three points about the rebate. Do we  
8 need economic stimulus provided by the rebate currently in  
9 the economy?

10 If we provide it, will it be inflationary?

11 Thirdly, if we are going to apply it, why a rebate; why  
12 not something else.

13 Let me speak briefly on each of those three points.  
14 Do we need that kind of economic stimulus in this country?

15 First, the Gross National Product of the economy, after  
16 seven quarters of recovery is only 3 percent above where it  
17 was three-and-a-half years ago when the recession began.  
18 Output in the American economy now, after two years of  
19 recovery, is about 3 percent above where it was three-and-a-  
20 half years ago.

21 The Chairman. Constant dollars?

22 Mr. Schultze. Constant dollars, that is correct, compared  
23 to an average, in other post-War recoveries at this time, of  
24 8 percent above. We had the worst recession in forty years.  
25 We have had a recovery partially from it.

1 Even after that, we are far below relative to that  
2 prior peak than we have been in the past.

3 Secondly, because of that factor, at the present time  
4 the unemployment rate -- while it is falling -- is still  
5 7.5 percent which, with one minor exception, is higher than  
6 it was at the trough, the very bottom of all the other post-  
7 War recessions. After seven quarters of recovery with  
8 respect to unemployment, we are still worse off than when we  
9 were at the very bottom.

10 It is not that we are saying that the economy will not  
11 grow at all; it will grow. What we are saying is that it  
12 will grow too slowly to make a really significant dent on  
13 unemployment, starting from a period where we are worse off  
14 than we have ever been in the post-War period with respect  
15 to economic recovery.

16 Let us look at some of the recent economic statistics  
17 that some people have said, things are looking pretty good;  
18 you do not need the rebate.

19 The economy was not disrupted as much as most people  
20 thought by the cold weather. In terms of the overall economy,  
21 it has come back pretty well, not having gone down quite  
22 so far, and it has come back pretty well.

23 Nevertheless, let us look where we are.

24 In February, industrial production was only 12 percent  
25 higher than it was in December. Where auto sales have been

1 pretty strong, total retail sales in February were still  
2 below December. This is not even adjusted for prices.

3 Not only that, in the absence of something to stimulate  
4 consumer spending, nothing in this world is positive. It is  
5 fairly clear that consumer spending will grow rather weakly  
6 in the year ahead.

7 In the last quarter of 1976, consumers were spending  
8 a higher fraction of their income than at any time since  
9 1969. It is unlikely, even though consumers in general are  
10 fairly confident, that they are going to retain that high  
11 spending fraction.

12 Over the year ahead, as income rises, consumption is not  
13 going to rise very probably in the absence of a rebate. Let  
14 me say that again.

15 In the last quarter of 1976, consumers were spending an  
16 abnormally high fraction of their income. It is likely that  
17 they will restore their savings to the normal rate. There-  
18 fore, consumption will not rise as fast as income.

19 During the cold weather, consumers spent \$2 to \$3  
20 billion extra for fuel. That is not a huge amount, but it  
21 does mean another slight dampening effect on consumption for  
22 other things because they had to spend that amount extra on  
23 fuel.

24 Residential construction, another area of the economy,  
25 recovered fairly significantly in 1976, but it has been

1 on a plateau since then. Residential construction has been  
2 running at a level of \$1.7 million to \$1.8 million every  
3 month except for January when it dropped down, due to the  
4 cold weather. It has been on a plateau. Although you are  
5 not going to get out of it a major rise, pushing the economy,  
6 it will rise some.

7 Business plant and equipment investment has got to rise  
8 strongly, not only this year but next year to assure meaning-  
9 ful progress in reducing unemployment. What do we have?

10 The latest survey of business intentions to invest  
11 showed an increase of about 12 percent over last year. This  
12 is slightly less than we had been counting on in our economic  
13 forecast.

14 Exports over the nonagricultural exports, quarter by  
15 quarter over the last four quarters, have been about flat  
16 after you adjust for price increases. Recoveries in other  
17 parts of the world are weaker than ours, in some cases, not  
18 occurring at all. You cannot look for a big bulge in exports.

19 On balance, what do we have? On balance, we have an  
20 economy that has recovered some, but because the recession  
21 is so deep, it is still well below performance in every other  
22 post-War recovery.

23 We are faced with an economic growth this year, without  
24 stimulus -- an economic growth when you look at what the  
25 situation is with consumption, business investment, exports



1 and housing will not be strong enough to make a significant  
2 contain unemployment. It will go down.

3 Without this rebate as an economic stimulus, it will go  
4 down too slowly.

5 With the rebate in, with economic stimulus, is it likely  
6 to be inflationary?

7 Let me start with the fact with the rebate, on best  
8 judgment, real output in the economy will grow between the  
9 last quarter of last year and the last quarter of this year,  
10 over the twelve months ahead, something in the neighborhood  
11 of 6 percent real, adjusted for inflation, it will grow 6  
12 percent.

13 Nobody can be that precise, but that is what it looks  
14 like with the rebate.

15 Growth rates of 6 percent, not just this year, but  
16 continued into next year, are not going to put upward  
17 inflationary pressure in the economy. Let us look at why  
18 not.

19 Right now, we are clearly performing well below the  
20 nation's economic potential or the nation's economic capacity.

21 For example, based on some fairly conservative estimates  
22 of the outgoing Ford Council of Economic Advisors, the output  
23 last year was \$135 billion below its potential. With the  
24 kind of economic growth we would get with the stimulus, in  
25 1977, that gap would shrink, but still be \$100 billion.

1 In 1978, continuing the 6 percent, the gap will shrink,  
2 but it still will be about \$75 billion.

3 Labor markets are not tight -- not that we are putting  
4 upward pressure on labor markets. There are 7 million  
5 Americans out of work. There are some of those who are  
6 structurally unemployed, people who have a hard time finding  
7 jobs even in good times. There are millions of people who  
8 are people who, normally in good times, are experienced wage  
9 and salaries workers holding normal, average paying jobs  
10 who are out of work and now looking for work. There is a  
11 sizable pool of experienced, unemployed labor available to be  
12 put to work to produce the output which this economy and  
13 economic stimulus would produce.

14 We would not, by putting the stimulus in, be putting  
15 real tight labor markets in.

16 What about capacity? In 1973, part of the upsurge in  
17 inflation in '73 did result from bottlenecks and scarcities of  
18 raw materials, but today the overall capacity utilization  
19 among firms producing industrial materials is about 80  
20 percent.

21 We tried to make a calculation of where that would be  
22 if the recovery, with the stimulus, over the next two years  
23 recedes as we think it might, 5 to 6 percent a year. At the  
24 end of two years capacity utilization in those critical  
25 industrial materials would be 85 to 87 percent, well below

1 the 93 percent peak that gave us trouble in 1973.

2 Obviously none of these capacity utilization methods  
3 are perfect, but this is based on the Federal Reserve Board  
4 index, recently extensively revised last year, and fairly  
5 conservatively measured. There is a recognition that these  
6 numbers had not been too good, so the Federal Reserve spent  
7 a long time revising, and these numbers are based on the  
8 revision.

9 There is ample productive capacity worldwide. In 1973,  
10 when we were experiencing inflation, the rest of the world  
11 was drawn tight. That is no longer true. That gives us  
12 additional leeway.

13 So measuring output compared to its potential, as done  
14 by the outgoing Council of Economic Advisors, measuring the  
15 availability of labor, measuring raw material availability  
16 and economic recovery of the moderate but good magnitude  
17 that we foresee with this economic stimulus which we will not  
18 get without the stimulus, it will not put inflationary  
19 pressure on the economy.

20 That does not mean inflation is going to stop. It is  
21 5 to 6 percent a year. We got some bad news last month,  
22 we will get some bad news in the next few months due to  
23 food and fuel prices and due to the cold weather.

24 I am not suggesting inflation will stop, but I am  
25 suggesting this will not add to it. We could not keep doing this

1 for three, four, five, six years in a row. Given where this  
2 economy now is, we cannot afford to grow too slowly.

3 Let me give you one reason. It is tempting to say that  
4 we should be extremely cautious about stimulating the  
5 economy, because we are in an inflationary age. A danger  
6 with doing that is, what happens in a relatively slowly  
7 growing economy?

8 What has happened to ours recently, you do not get much  
9 investment. If you do not get much investment, you do not  
10 add capacity. Then you go down the road three years from now  
11 and you say, aha, now we can afford to stimulate again.

12 All of a sudden, you are going to find that you cannot  
13 stimulate because you have not been investing, have not  
14 been building capacity.

15 Now you start to reach bottlenecks when the rate of  
16 employment is 6.5 to 7 percent. There is a long run infla-  
17 tionary danger of not pursuing at least a moderate economic  
18 stimulus, because if you let that investment continue to  
19 stagnate -- which it will do if the economy continues to  
20 stagnate -- you have problems three years down the road, from  
21 a real shortage of capacity.

22 A final point. Assuming for the moment that you agree  
23 with me that you need some economic stimulus and it will not  
24 be inflationary, why the rebate, why not something else?

25 There are two kinds of something else. One kind of

1 something else is to substantially increase public works,  
2 public jobs and other programs. That is one way to do  
3 something else.

4 What happens if you do that? Number one, it will not  
5 be effective right now, because you cannot get it started  
6 fast enough. Number two, you are building yourself in, if  
7 you overdo that, some very large spending down the road  
8 three or four years from now.

9 I would be very careful in doing that.

10 There is no way on the spending side that I know of where  
11 you could responsibly put that stimulus in.

12 The second point, why not have a permanent tax cut  
13 instead of a rebate? It gives you an economic stimulus with  
14 the tax cut, I have to agree, it clearly does. Why should we  
15 not do that instead of the rebate?

16 I would say for two big reasons. Number one, the  
17 beauty of the rebate is that it does not mortgage a very  
18 large amount of revenues into the future. It does not take  
19 that \$11 billion which is a one-shot increase in the deficit  
20 and then disappear. It gets the economy ticking. It mort-  
21 gages that \$11 billion and then it grows down into the  
22 future.

23 In the long run, even though we consider that it is  
24 appropriate to increase the deficit this year, we also say  
25 that to deal with inflation in the longrun, you also have a

1 budget that is in a position that is able to be balanced in  
2 1980-81. In order to stimulate the economy in 1978, we do  
3 not want to mortgage all those future revenues.

4 Secondly, if you come in now, and for purposes of a  
5 quick economic stimulus, which we do need, mortgage those  
6 future revenues, I think you will then substantially reduce  
7 the possibility, in my judgment, of significant tax reform  
8 and tax reduction, worked out very carefully at a later  
9 stage.

10 I think that we ought not to confuse what may be very  
11 needed, a longterm set of structural reforms in our economy  
12 and dealing both with questions of equity on the one hand  
13 and questions of business taxation on the other, we ought not  
14 to mortgage that possibility in order to do something that  
15 we can do with the rebate, still leaving that flexibility  
16 open in the future.

17 On three grounds, therefore, it seems to me that this  
18 tax rebate makes sense.

19 One, we need stimulus.

20 Two, the stimulus will help the economy without being  
21 inflationary.

22 Three, in my judgment there is no way to get that kind  
23 of appropriate moderate stimulus on either the spending side  
24 or on the permanent tax cut side without mortgaging the  
25 future too soon.

1 The Chairman. Thank you very much, Mr. Schultze. I am  
2 not going to suggest any questions because that would just  
3 drag out these proceedings.

4 I chose this procedure because I think that, while it  
5 would have been easy enough to have Mr. Schultze tell this  
6 to the Democrats in a caucus, I thought that it be more  
7 appropriate that the presentation be made so everybody can  
8 hear it and make their own decisions.

9 I appreciate your stating it, Mr. Schultze. I am not  
10 going to ask any questions or invite others to because that  
11 could take the whole morning. I appreciate very much your  
12 being here. I think you have another appointment.

13 Thank you very much.

14 Mr. Schultze. Thank you, gentlemen.

15 The Chairman. I would suggest that if we want to vote  
16 on this matter that we go ahead and vote, for the substitutes  
17 or whatever you want to do about this.

18 Senator Roth. Mr. Chairman, I appreciate the fact that  
19 Mr. Schultze has an appointment, but before he leaves I think  
20 there ought to be a chance for some statement to be made on  
21 the other side.

22 The Chairman. Of course.

23 Senator Roth. I am not an economist; perhaps I am not  
24 the proper one to speak, but I would just like to point out  
25 to Mr. Schultze that I think that many of us agree that there

1 is need of some kind of stimulus, that something needs to be  
2 done to get the economy moving.

3 I think our concern is that we did not want to move it  
4 just in the short run. What we are interested in is a long-  
5 term movement upward that will provide meaningful jobs in  
6 the private sector. That is what it is all about.

7 What concerns me, as you know, having worked with me  
8 for many years at Brookings, I have great respect for you.  
9 One of the things going for the rebate, to be honest, is we  
10 have a fine new President supporting it, but we have  
11 authority after authority saying it is not the answer to the  
12 economic problems today.

13 That includes not only Republicans nor conservative-  
14 type philosophers or economists, but the liberals and  
15 Democrats as well.

16 I would just like to read a few things here about what  
17 people are saying about rebates. For example, the Joint  
18 Economic Committee, or Congressional Budget Committee, said  
19 "that a one-time refund will only have a temporary effect  
20 in stimulating the economy. After the refund has been spent  
21 and the multiplier effect has worked itself out, the economy  
22 will return to the same path on which it would have been  
23 without the refund."

24 Let me read what the Joint Economic Committee said.  
25 It has a report that states: "A rebate would have only a



1 temporary impact on the rate of economic growth with most  
2 of the effect petering out in a twelve-month period."

3 Otto Eckstein, former economic advisor to President  
4 Johnson, argues that because inflation is pushing tax  
5 payers into higher tax brackets, a temporary tax rebate  
6 will have little economic impact.

7 Paul McFadden, a former economic advisor, he says, "A  
8 \$50 tax rebate is a Rube Goldberg contrivance that will do  
9 little to help economic expansion." What we need to do today  
10 is build confidence into the economy, confidence into the  
11 picture. That will get the economy moving up longrange.  
12 I do not think we can delay that.

13 If I can understand what you are saying, let us do  
14 this today. Somewhere down the road, we will have tax reform  
15 that this Finance Committee is already committed to. Last  
16 year, we adopted legislation -- it was my legislation -- that  
17 the Joint Committee would come up with recommendations in  
18 six months. We all agree with you that there has to be  
19 tax reform, tax simplification, no question about that.

20 What we need right now if we are going to create these  
21 jobs is something that the people know are going to be here  
22 for awhile. They have to know what the picture is going  
23 to be.

24 The \$50 rebate is not going to end up with any  
25 substantial longterm purchasing. The only way you are going

1 to get done what you want done is a permanent tax credit.

2 Let me point out, it does not mean less revenue. The  
3 Kennedy experience in the 60's showed just the opposite. It  
4 means more revenue for the Federal government.

5 There is a very basic difference in philosophy.

6 Mr. Chairman, at a later date I intend to offer a  
7 proposal for an across-the-board tax cut.

8 Mr. Schultze. } One comment, maybe two comments.

9 First, if we were coming up with only a tax rebate and  
10 nothing else, either in economic stimulus or in the rest of  
11 the three years of this, he might be right. The tax rebate  
12 is the first stage of a two-year program. That is number  
13 one.

14 The tax rebate phases out; some of the other measures  
15 phase in.

16 Secondly, this is a resilient, private economy and it  
17 is not necessary to keep on pumping in stimulus. Why are  
18 we not getting more investment, which is critical in the  
19 Longrun?

20 There are a lot of reasons. I do not pretend that this  
21 answers all of them.

22 One of the reasons is precisely what I said earlier,  
23 that right now this economy has sales, markets only 3 percent  
24 above what it was three-and-a-half years ago.

25 Who is going to build new capacity; compared to the  
normal situation of being 8 percent above where you can put

1 some need for capacity into people?

2 A point about a two-year stimulus program is to build  
3 up those sales and markets, get you closer to where we have  
4 been in past periods of recovery and start taking over some  
5 self-generating investment in capacity.

6 I do not want to stop there and say that that is the  
7 only thing that needs to be done. I agree on confidence. I  
8 agree on the need for major tax reform.

9 What I am suggesting is that even though the one-shot  
10 rebate looked at in and of itself is temporary, but it is  
11 part of a longer strategy. It is effective in that context.

12 It is also effective in a way that does not mortgage --  
13 and I think it might -- some of the chances of this  
14 Committee doing something serious in tax reform.

15 Thank you.

16 The Chairman. Let me lay out the groundrules which I  
17 think are obvious in the present situation. We have an  
18 even number of Senators on this Committee, therefore we have  
19 the potential of tie votes.

20 The \$50 credit is something that is in the House bill.  
21 It takes a majority of the Senators to vote to take it out,  
22 so a tie in effect goes to those of us who support the  
23 House position.

24 Senator Packwood. It takes a majority of the Committee  
25 to send the House bill out, does it not?

1 The Chairman. That is right.

2 Sure, absolutely. We will worry about that when we come  
3 to it.

4 Shall we vote on it? If you want to offer substitutes,  
5 you can offer substitutes.

6 Senator Curtis. Mr. Chairman, we would like, and I am  
7 sure my colleagues will be brief, we would like to offer a  
8 substitute or two first.

9 The Chairman. Go ahead.

10 Senator Roth. Mr. Chairman, I would like to propose  
11 a substitute to the rebate, a 10 percent reduction in all  
12 individual tax rates effective May 1, 1977.

13 Let me say in starting out, I would just like to read,  
14 if I could, a statement in the State of the Union address  
15 by President Kennedy in 1963 where he proposed a very sub-  
16 stantial permanent reduction in tax rates which included  
17 lowering the rate from 20 to 91 percent to what he said  
18 was a more sensible rate of 14 to 65 percent.

19 I think this is particularly pertinent. I hope all of  
20 my colleagues will listen to this with great care. He said:  
21 "I do not say that a measure for tax reduction reform is  
22 the only way to achieve these goals. No doubt a massive  
23 increase in Federal spending could also create jobs and  
24 growth. In today's setting, private consumers and  
25 employers and investors should be given the full opportunity

1 first.

2 "No doubt, a temporary tax cut" -- that is, of course,  
3 what the rebate is -- "could provide a spur to our economy,  
4 but a longrun problem compels a longrun solution?" I would  
5 like to emphasize that.

6 Senator Kennedy in '63 said "A longrun problem compels  
7 a longrun solution," and that is what we are proposing here  
8 today by a permanent tax cut reduction of 10 percent.  
9 It would provide a longterm reduction that would create some  
10 buoyancy in our economy.

11 As I said a few moments ago, the most important thing  
12 today to get the economy moving again is to get some confi-  
13 dence both in the business world and the consumer. The only  
14 way you are going to get the consumer to go out and start  
15 buying things is to make sure he has a permanent tax cut.

16 I passed out -- I think it has been passed out to you --  
17 some papers of what would happen with a 10 percent cut  
18 across-the-board. When you combine it with a standard tax  
19 reduction of the House, whatever we adopt here, it does  
20 mean that very substantially the tax cut benefits those at  
21 the lower end of the scale.

22 For example, the guy who makes \$3,000 between the  
23 two cuts would get something like a 100 percent cut. He  
24 now pays \$43; he would pay no taxes.

25 The guy who makes \$6,000 would get a 33 percent tax cut,

1 or \$179.

2 One of the important things I think to recognize in this  
3 context in this across-the-board tax cut, it is about time  
4 we quit gutting the middle class, seeking the middle class.  
5 It is about time that we give them some breaks. Inflation  
6 has hit them hard.

7 I would just like to point out "The New Republic," a  
8 liberal magazine -- I mentioned this the other day -- said  
9 for the first time in our history, modern history, the middle  
10 class is faced with downward mobility. As it looks ahead, it  
11 cannot afford houses, it cannot afford to send its child  
12 to school.

13 They said, we had better do something about that or there  
14 is going to be a rebellion. They said, we are talking about  
15 tax cuts. Sure, it is fine to help the \$17,000. They need  
16 it, no question about it. What is wrong with helping the  
17 \$20,000 guy or the \$30,000 guy or even the \$40,000 guy?

18 They are the ones who are going to go out, if they have  
19 a permanent tax cut, and put a down payment on a house which  
20 will create jobs in the private sector, will buy TVs, will  
21 buy refrigerators, will create jobs in the private sector.

22 As a matter of fact, my proposal shows that by the end  
23 of 1978 it would create permanently 920,000 jobs in the  
24 private sector. This rebate is going to have no longterm  
25 effect. Next year, we are going to be right back where we

19 000000 67

1 started from.

2 The JEC says that many of our leading economists have  
3 said that, as I have already read. So I am proposing, as  
4 I said, this 10 percent cut across the board.

5 I know a lot of you say we should not do it, for some  
6 people, we should not help those over \$20,000 or \$30,000.  
7 I would like to point out that this Congress did not turn  
8 down a \$13,000 pay cut for themselves because they said they  
9 needed it. If they needed it, so does the guy or gal in the  
10 private sector.

11 The only other point that I want to make at this time  
12 is that this will cost less, its longrange effect will  
13 be beneficial, and the Kennedy experience showed that it  
14 ultimately will create -- actually create -- more income for  
15 the Federal government. So we are not mortgaging the  
16 future. We are taking a chance on the private sector. It is  
17 about time that we quit doing what we have done in the past,  
18 have a little bit of something for everybody, which has not  
19 worked.

20 That is the reason we are in the mess we are in today.

21 We ought to start in on a simple, dramatic new front.

22 Senator Curtis. I commend the Senator.

23 I would like to point out this. There may be some on  
24 the Committee who feel revenue should not be reduced at all.  
25 If so, they will have a chance to vote against it. Reporting

1 out the bill, there may be several votes. I do not know.

2 As I see it, the vote on the Senator's proposal is a  
3 clear-cut one of a tax cut or the rebate.

4 If anybody feels we should have neither, they will have  
5 the opportunity to say so. It would be my hope that we would  
6 have a substantial majority for your proposal.

7 Senator Byrd. Mr. Chairman?

8 The Chairman. Senator Byrd.

9 Senator Byrd. I associate with the remarks made by  
10 the Senator from Delaware. If there is to be a tax reduction  
11 legislation in this session that the proposal by Senator  
12 Roth is far sounder in my opinion than is the Carter Adminis-  
13 tration's proposal and also, I think it will do a great deal  
14 more to inspire confidence on the part of the people of our  
15 country than will a \$50 rebate. I shall support the Roth  
16 proposal.

17 The Chairman. Gentlemen, I would hope that we could  
18 get on with the voting on these matters. We respect the  
19 fact that those who offer amendments ordinarily are entitled  
20 to the right to speak for their proposal. We have had a  
21 good presentation of both sides of an argument, and I would  
22 hope that we could just call the roll and vote for the  
23 Roth proposal.

24 Senator Roth. That is fine.

25 Mr. Stern. Senator Talmadge?



1 The Chairman. No.

2 Mr. Stern. Senator Ribicoff?

3 The Chairman. No.

4 Mr. Stern. Senator Byrd?

5 Senator Byrd. Aye.

6 Mr. Stern. Senator Nelson?

7 Senator Haskell. No.

8 Mr. Stern. Senator Gravel?

9 (No response)

10 Mr. Stern. Senator Bentsen?

11 Senator Bentsen. No.

12 Mr. Stern. Senator Hathaway?

13 Senator Hathaway. No.

14 Mr. Stern. Senator Haskell?

15 Senator Haskell. No.

16 Mr. Stern. Senator Matsunaga?

17 Senator Matsunaga. No.

18 Mr. Stern. Senator Moynihan?

19 Senator Moynihan. No.

20 Mr. Stern. Senator Curtis?

21 Senator Curtis. Aye.

22 Mr. Stern. Senator Hansen?

23 Senator Hansen. Aye.

24 Mr. Stern. Senator Dole?

25 Senator Curtis. Aye.

1 Mr. Stern. Senator Packwood?

2 Senator Packwood. Aye.

3 Mr. Stern. Senator Roth?

4 Senator Roth. Aye.

5 Mr. Stern. Senator Laxalt?

6 Senator Laxalt. Aye.

7 Mr. Stern. Senator Danforth?

8 Senator Danforth. Aye.

9 Mr. Stern. Mr. Chairman?

10 The Chairman. No.

11 Senator Curtis. May the absentees be recorded?

12 The Chairman. Yes, they can.

13 I ask that Senator Gravel be called. The vote is eight  
14 yeas and nine nays. At this moment, it would not make any  
15 difference.

16 Senator Danforth?

17 Senator Danforth. I have a proposal to offer as  
18 contained in Senate bill 730, which is in front of you,  
19 which provides for an 18 percent reduction in rates for  
20 taxpayers with adjusted gross incomes of \$18,000 or less.  
21 I am sorry, a 14 percent reduction in rates for taxpayers  
22 with \$18,000 gross income or less.

23 The basic proposition behind this proposal is that  
24 it will provide more jobs than the rebate will provide.  
25 The jobs will be longer lasting, and the effect will be half

1 as inflationary as the rebate.

2 Under the Carter proposal, the rebate proposal, in 1977  
3 350,000 jobs, it has been estimated, would be produced whereas  
4 in 1978, 150,000 jobs would be produced. Under this proposal,  
5 in 1977, the figure would be 200,000 estimated; in 1978, an  
6 estimated \$525,000.

7 I would dispute the Carter figures because the analysis  
8 of the effect of the rebate and the whole theory of the  
9 rebate was made before the Harris poll results came out which  
10 showed, in fact, that a substantial portion of the amount to  
11 be paid out in the rebate would not be used by the recipients  
12 to purchase consumer items.

13 Senator Curtis. Would the Senator yield for a  
14 correction?

15 I think you have understated your bill. It would give  
16 some tax reduction to everybody, because it would lower the  
17 rates on the first \$18,000 of income for all the brackets,  
18 rather than confining it.

19 Senator Danforth. You are absolutely correct. I  
20 appreciate the correction. My reduction would go to the  
21 first \$18,000 of adjusted gross income. It would benefit  
22 all taxpayers, but it would benefit them because it would  
23 benefit the first \$18,000 of adjusted gross income, which  
24 would cover everybody.

25 It would target, as Senator Roth's proposal did not do,

1 it would target the low income and the middle income  
2 taxpayers.

3 The Harris poll on January 27, 1977 indicated that only  
4 21 percent of the people who would receive the rebate would  
5 use the rebate to buy things that they need, whereas 33  
6 percent would put the money in the bank and 29 percent would  
7 pay off old debts, and 15 percent would use the money for  
8 a combination of things.

9 So that well over half of the recipients, over 60  
10 percent of the recipients of the rebate would not, in fact,  
11 use it to buy consumer items. Insofar as they would use it  
12 to buy consumer items, it would be a sudden rush of cash into  
13 the marketplace.

14 For this reason, Chase Econometrics predicts that a  
15 permanent tax cut would be half as inflationary as the  
16 rebate.

17 Obviously with the projections made with the Carter  
18 rebate proposal, together with the testimony of Mr. Schultze  
19 last week or the week before when he came before us that this  
20 would be about a two quarters' effect, the job effect of the  
21 rebate would fall off very, very rapidly, after the rebate is,  
22 in fact, paid.

23 A further reason, I think, for a permanent tax cut as  
24 opposed to a rebate has to do with the credibility of what  
25 we are doing here in Washington. I think that the rebate is

1 something that does not have credibility with the general  
2 public. It would not build confidence. In fact, my  
3 experience with it, in my trips back to the state of Missouri,  
4 is that the rebate is a subject of jokes.

5 I do not think that we should do something that is a  
6 laughing matter for the people of this country. I pointed  
7 out yesterday that yesterday morning I met with a group of  
8 approximately 50 4-H leaders from Missouri, adult leaders  
9 of 4-H groups scattered throughout the state. I asked them  
10 in what I hoped was an impartial way whether they preferred  
11 to have a one-shot rebate or a permanent tax cut and they  
12 stated that they favored a permanent tax cut.

13 Finally I would like to address myself to the reasons  
14 given by Dr. Schultze for not wanting a permanent tax cut.  
15 He says that this would mortgage the future, yet the  
16 experience in the past has been that a permanent tax cut  
17 does not reduce Federal revenues. In fact, when you stimulate  
18 the economy, when you increase, in effect, the tax base,  
19 the government produces more revenues than it did before the  
20 tax cut was made.

21 So that I reject the notion that we would have fewer  
22 tax dollars that are raised.

23 Really, the question is, what percent of the Gross  
24 National Product is to be eaten up by government and what  
25 percent of the Gross National Product down the road is going

1 to be in the hands of people, in this case, lower income  
2 and middle-income taxpayers.

3 Secondly, he says that somehow this would affect  
4 the possibility of meaningful tax reform. There are a couple  
5 of problems with that. First, what tax reform is he talking  
6 about?

7 Are we to make a decision based on no specific proposal  
8 for what reforms are called for and also, as I understand  
9 the argument, it is as follows: the way we are going to get  
10 tax reform is not on the merits of tax reform. The way we  
11 are going to get tax reform is holding hostage middle income  
12 and lower income taxpayers by making them hurt even more  
13 than they do now on the theory that if they hurt enough  
14 they will cry out and then something can be done and we  
15 will have tax reform and offer them the salve of lower tax  
16 rates at that time.

17 I think that it is absolutely wrong to hold hostage  
18 people who are having, really, the worst time in this  
19 country.

20 Senator Hathaway. If the Senator would yield at that  
21 point, the Administration has indicated that it will have  
22 a tax reform package to us the 1st of September. There is  
23 some chance of having tax reform later this year or next  
24 year.

25 Senator Danforth. I would say two things to that. First,

1 we are buying a pig in a poke. We do not know what kind of  
2 tax reform they want. There was some argument whether the  
3 last tax reform bill, 1500 pages long, was a tax reform or  
4 not.

5 Some would say it was a complication of the tax laws  
6 rather than a simplification. I do not think that right now,  
7 on the theory that maybe we will have a tax reform, maybe  
8 there will be good reforms and bad reforms, is the basis  
9 now for making that kind of a guess.

10 Also, it should be borne in mind that that tax reform  
11 bill takes three years to pass. Are we going to wait three  
12 years for an unknown?

13 Senator Hathaway. Last year's took three years to pass?

14 Senator Danforth. That is correct.

15 Senator Hathaway. It just seemed that way.

16 Senator Curtis. It will take a lot longer for the  
17 country to recover from it.

18 Senator Danforth. Therefore, what I offer as a substi-  
19 tute for the rebate is the proposal contained in Senate  
20 bill 730.

21 Senator Byrd. May I ask the Chairman --

22 The Chairman. Senator Byrd?

23 Senator Byrd. -- what would be the revenue impact?

24 Mr. Shapiro. Senator, the revenue impact we have is at  
25 an annual rate. The revenue effect would be \$9.9 billion at

1 1977 income levels. Most of that, however, would be in  
2 fiscal '78. It will be probably a little under \$5 billion  
3 for fiscal '77. The full year effect would be beginning  
4 fiscal '78.

5 Senator Byrd. One question for clarification.

6 Does your proposal -- you say it goes from \$18,000 down-  
7 ward, is that it?

8 Senator Danforth. Yes. It is on the first \$18,000 of  
9 adjusted gross income, so if somebody had an adjusted gross  
10 income of \$50,000 it would benefit him.

11 If you had an across-the-board tax reduction of, say,  
12 10 percent, it would have a much greater dollar effect of  
13 somebody who is in an upper income bracket. 10 percent to him  
14 is more of a benefit than 10 percent to somebody who is in a  
15 \$15,000 bracket.

16 What this does is have a cut-off and it targets for the  
17 greatest benefit, taxpayers with \$18,000 adjusted income.

18 Senator Byrd. Thank you.

19 The Chairman. Let me ask this question, Mr. Woodworth.

20 In the planning down there in the Treasury, I assume that  
21 you are recognizing when we look at a tax reform proposal  
22 such as you are working on, that these tax reform bills usually  
23 wind up being revenue losers on balance, do they not?

24 Mr. Woodworth. They have in the past, in virtually all  
25 cases.



1 The Chairman. The average being a loser by \$7 billion?

2 Mr. Woodworth. Yes.

3 The Chairman. So that this bill is already a longterm  
4 tax cut on the simplification side for the low income people  
5 to begin with, is that not right?

6 Mr. Woodworth. That is correct.

7 The Chairman. If you are ever going to move towards  
8 a balanced budget, which I understand is an ultimate objective  
9 of the four-year term of this Administration, are you not  
10 going to be needing the tax rates that you have in the  
11 lower and middle income brackets with relatively full employ-  
12 ment to ever get to a balanced budget?

13 Mr. Woodworth. If you make this kind of reduction that  
14 you are talking about now, I think that it makes it extremely  
15 difficult to come with a tax reform and simplification  
16 measure later on.

17 As you suggested just a moment ago, Senator Long, in  
18 effect it takes the tax reduction and uses it up right there  
19 and then. It leaves you with a complicated system and a  
20 very difficult job to get out of that complicated system.

21 Senator Byrd. What you are entirely overlooking, and  
22 what Mr. Schultze overlooks, you can curb spending. Nobody  
23 has looked at that. You can make up for this by curbing  
24 spending.

25 Mr. Woodworth. I think the Administration plans to curb



1           Senator Roth. If the Senator would yield, I have a  
2 three-page sheet, four pages -- that is correct. The Senator  
3 from Wyoming is absolutely correct. The Library of Congress  
4 points out that the Treasury-estimated revenue loss versus  
5 the actual revenue gain, I think the important point to keep  
6 in mind, the Chief Economist said to us at the end of the first  
7 year that the tax cut paid for itself.

8           You can argue that there are other factors in any  
9 situation. Of course, it is a bundle of wood or sticks, if  
10 you want to argue that. The fact remains, after that tax  
11 cut, certainly that was Mr. Kennedy's position, that this tax  
12 cut got the economy moving, and that is all we are proposing  
13 here.

14           The point the Senator from Virginia made is very good.  
15 We are all for tax reform, as I mentioned. Some of us feel  
16 there ought to be a hold down on how much spending goes up.

17           By making a tax cut today, a permanent tax cut, it does  
18 not mean we are jeopardizing balancing the budget. In fact,  
19 it could improve the chances of doing so.

20           Senator Danforth. Mr. Chairman, we can get involved  
21 in the question of changing the standard deduction vis-a-vis  
22 a permanent tax cut. If the objective of changing the  
23 standard deduction is simplification and alleviating the  
24 so-called marriage penalty, I would be happy, as a further  
25 move after we vote on this, to offer a proposal that working

1 with this would cost very little money, much less than the  
2 \$5.6 or \$5.7 billion that has been projected, which would  
3 bring in line, which would lessen the marriage penalty more  
4 than any of these present proposals would lessen the marriage  
5 penalty, which would accomplish the objective of simplifica-  
6 tion.

7 But really, the issue is, does the permanent tax  
8 reduction take the form of a reduction in tax rates in the  
9 amount of some \$9 or \$10 or \$12 million a year, or instead,  
10 does it take the form of a standard deduction in the amount of  
11 about \$5.6 billion the first year and after that, \$4 billion.

12 I would argue in favor of a reduction in rates for  
13 several reasons. One, obviously more money is involved.  
14 Two, it would affect about 70 million more returns instead  
15 of about 45 million returns, which would be affected by  
16 the change in the standard deduction.

17 Three, it is much more simple for the average person  
18 to comprehend.

19 If you are trying to create confidence on the part of the  
20 little guy, the small taxpayer, in what is going to happen  
21 in the future, the best way to do it is to say your tax rate  
22 is going to be cut by not sending around a blackboard where  
23 some people are going to have their taxes cut and some are  
24 going to have their taxes raised.

25 The Chairman. May I ask a question?

1 Are you proposing a substitute for your own amendment?

2 Senator Danforth. Not now.

3 The Chairman. I think we had better vote on one amend-  
4 ment before we go on to the next one.

5 Senator Danforth. All I wanted to do was point out that  
6 I would hope that we could put the question of simplification  
7 of the standard deduction and solving the marriage penalty  
8 question to the background, because with this kind of  
9 permanent tax reduction, we can accomplish the other things  
10 as well.

11 The Chairman. Let us call the roll, then.

12 Senator Byrd. May I ask a question?

13 The Chairman. Senator Byrd?

14 Senator Byrd. The question is whether this will be  
15 substituted for the Carter Administration program?

16 Senator Danforth. For the rebate part of the program.

17 Mr. Stern. Mr. Talmadge?

18 The Chairman. No.

19 Mr. Stern. Mr. Ribicoff?

20 (No response)

21 Mr. Stern. Mr. Byrd?

22 Senator Byrd. Aye.

23 Mr. Stern. Mr. Nelson?

24 Senator Haskell. No.

25 Mr. Stern. Mr. Gravel?

1 (No response)  
2 Mr. Stern. Mr. Bentsen?  
3 Senator Bentsen. No.  
4 Mr. Stern. Mr. Hathaway?  
5 Senator Hathaway. No.  
6 Mr. Stern. Mr. Haskell?  
7 Senator Haskell. No.  
8 Mr. Stern. Mr. Matsunaga?  
9 Senator Matsunaga. No.  
10 Mr. Stern. Mr. Moynihan?  
11 Senator Moynihan. No.  
12 Mr. Stern. Mr. Curtis?  
13 Senator Curtis. Aye.  
14 Mr. Stern. Mr. Hansen?  
15 Senator Hansen. Aye.  
16 Mr. Stern. Mr. Dole?  
17 Senator Dole. Aye.  
18 Mr. Stern. Mr. Packwood?  
19 Senator Packwood. Aye.  
20 Mr. Stern. Mr. Roth?  
21 Senator Roth. Aye.  
22 Mr. Stern. Mr. Laxalt?  
23 Senator Laxalt. Aye.  
24 Mr. Stern. Mr. Danforth?  
25 Senator Danforth. Aye.

1 Mr. Stern. Mr. Chairman?

2 The Chairman. No.

3 There are eight yeas and eight nays.

4 Senator Ribicoff, how do you want to be recorded? Eight  
5 yeas and eight nays on the motion to substitute the Danforth  
6 proposal.

7 Senator Ribicoff. Prior to the vote, could I make a  
8 speech to the Administration?

9 Let me tell you, Larry, I support the Administration in  
10 this \$50 rebate with a great deal of skepticism. In all  
11 the years that I have been on the Finance Committee, I have  
12 never known any set of economic advisers to any President  
13 who have been correct.

14 (General laughter)

15 Senator Ribicoff. I am skeptical about the present  
16 economic advisers. Maybe we ought to give these economic  
17 ~~advisers~~ the benefit of the doubt, with this bill, anyway.

18 There has been a lot of commitment about what you are  
19 going to do by September and October 1st. I am impressed  
20 with the arguments that both Senator Roth and Senator Dan-  
21 forth have made. They make a lot of sense.

22 This is a new Administration and it should have an  
23 opportunity to prove itself economically. They feel that  
24 it is important. I am going to vote no' against Danforth  
25 not because I think that the Administration is absolutely

1 correct, on their point of view. I am going to vote no, but  
2 I do want to make the statement for the record.

3 Senator Haskell. Mr. Chairman?

4 The Chairman. Senator Haskell.

5 Senator Haskell. I wonder if I could make a statement  
6 for the record comparable to Senator Ribicoff's.

7 I am not at all sure that this \$50 rebate is going to  
8 get the job done. I have not had the experience that Senator  
9 Ribicoff has with a series of economic advisers to Presidents;  
10 I can make no comment there.

11 My vote really with the Administration is on the grounds  
12 that since their economists say that this is the way to  
13 go, I think they are entitled to at least, at the beginning,  
14 to get support from the Democratic side of aisle. That is  
15 why I voted.

16 The Chairman. Senator Moynihan?

17 Senator Moynihan. May I associate myself with Senator  
18 Ribicoff and Senator Haskell, particular Senator Ribicoff's  
19 statements about Senator Roth and Senator Danforth, who  
20 raise very serious questions. We know on this side that they  
21 are serious.

22 We know the economic advisers have put this rebate  
23 before us. In their private conversations, they are as  
24 anxious about it as you are.

25 I think we might say to Secretary Woodworth that



1 certainly on our side we are going to support you, because  
2 you deserve our support, but we would hope that we might  
3 have, in return, a certain amount of candor. If it does  
4 not work, we would like you to come out that it did not  
5 work and tell us if, indeed, the reasons are those that  
6 we have all heard around this table.

7 Senator Bentsen. Mr. Chairman, if I may say, I am  
8 going to go ahead and vote for the \$50 rebate, but I have  
9 done so with the understanding of what the Administration has  
10 said, that they will be coming up this fall with meaningful  
11 tax reform reductions, because I think we have to have  
12 further reduction for middle income, low income, and try to  
13 cut out some inequities in the tax system.

14 Rather than see it done in this Committee without the  
15 appropriate hearing, I would like to see them have the time  
16 to come up with a comprehensive package. That is why I am  
17 doing it, just to let them have the time to come up and  
18 do some of the things that Senator Danforth is talking  
19 about, and hopefully some of the others.

20 The Chairman. Senator Danforth?

21 Senator Danforth. I would like to propose a further  
22 substitute, the same proposal that I previously made, the  
23 same proposal contained in Senate bill 730, however, retro-  
24 active to January 1st, with a minimum tax refund of \$50 per  
25 taxpayer.

1 Senator Byrd. What is the revenue impact?

2 Mr. Shapiro. Could you restate your proposal again?

3 Senator Danforth. It is Senate bill 730, which is the  
4 same one I was talking about before, the permanent tax cut  
5 for the first \$18,000 adjusted gross income effective January  
6 1, 1977, refundable check, therefore, going back to the  
7 taxpayer and the lowest check, the lowest amount of the check  
8 per tax return -- not per taxpayer, per tax return -- would  
9 be \$50.

10 So you would not be sending back \$2.98.

11 Mr. Shapiro. You mean January 1 of this year?

12 Senator Danforth. This year.

13 Mr. Shapiro. The way the system really works, in  
14 general, is that reflected in the tax returns that are  
15 filed in 1977 by April 15, 1978. When you say refundable,  
16 I am not exactly sure how that would work administratively.

17 Do you want to give a refund now of what the withholding  
18 would have been between January and whatever withholding  
19 would take place?

20 Senator Danforth. Right, retroactive to January 1, 1977,  
21 \$50 per return.

22 Mr. Shapiro. A \$50 rebate per return would be \$3 billion.

23 Senator Hansen. May I ask a question?

24 Does your proposal envisage returning, or making a  
25 refund to those persons who have actually paid taxes?

1 Senator Danforth. Yes,

2 Senator Curtis. Do you mean to say that of the \$11  
3 billion package, \$8 billion on the rebate goes to people  
4 who pay no taxes?

5 Mr. Shapiro. I understand Senator Danforth to say you  
6 are talking about a rebate only to the extent we would have  
7 had this withholding, but withholding will not take  
8 place until, for example, May; that you want them to get  
9 that money now.

10 Senator Danforth. Yes.

11 Mr. Shapiro. You would have a \$50 rebate? They could  
12 not get more than \$50, but they would be entitled to \$50  
13 based on what the reduction would have been?

14 Senator Danforth. \$50 or more.

15 Mr. Shapiro. The rebate in the Administration proposal  
16 is \$7.3 billion, actually tax refunds, not the refundable  
17 portion. That is the House bill.

18 Senator Danforth. It could be worked either way. You  
19 could get \$50 per return to all taxpayers, or you could  
20 get a minimum of \$50 and anything over that. My proposal  
21 right now is for \$50 per return.

22 The Chairman. Can you tell us about that, Mr. Woodworth?

23 Mr. Woodworth. Wholly apart from the revenue effect,  
24 it seems to me that it is not administratively workable. You  
25 are referring to returns for the year 1977, which are filed

1 in the year 1978. In other words, the return with which you  
2 are giving back the \$50 rebate does not exist yet. It will  
3 not exist until next year.

4 The only conceivable way is to assume that the employers  
5 can hand out the \$50 and they have no knowledge of with-  
6 holding. I sincerely do not see how it is possible to make  
7 it work.

8 Senator Danforth. How would it be more difficult  
9 than the \$50 rebate you have now?

10 Mr. Woodworth. That relates to the returns filed for  
11 1976, and the rebate goes back with respect to an individual  
12 who has filed a 1976 return.

13 You are asking in this case -- unless I misunderstand  
14 you -- you are asking that the amount go back with respect  
15 to somebody who has not yet filed a return, and we do not  
16 even know who they are.

17 The Chairman. Call the roll.

18 Mr. Stern. Mr. Talmadge?

19 The Chairman. No.

20 Mr. Stern. Mr. Ribicoff?

21 Senator Ribicoff. No.

22 Mr. Stern. Mr. Byrd?

23 Senator Byrd. No.

24 Mr. Stern. Mr. Nelson?

25 Senator Haskell. No.

1 Mr. Stern. Mr. Gravel?  
2 (No response)  
3 Mr. Stern. Mr. Bentsen?  
4 Senator Bentsen. No.  
5 Mr. Stern. Mr. Hathaway?  
6 Senator Hathaway. No.  
7 Mr. Stern. Mr. Haskell?  
8 Senator Haskell. No.  
9 Mr. Stern. Mr. Matsunaga?  
10 Senator Matsunaga. No.  
11 Mr. Stern. Mr. Moynihan?  
12 Senator Moynihan. No.  
13 Mr. Stern. Mr. Curtis?  
14 Senator Curtis. No.  
15 Mr. Stern. Mr. Hansen?  
16 Senator Hansen. No.  
17 Mr. Stern. Mr. Dole?  
18 Senator Dole. No.  
19 Mr. Stern. Mr. Packwood?  
20 Senator Packwood. Aye.  
21 Mr. Stern. Mr. Roth.  
22 Senator Roth. No.  
23 Mr. Stern. Mr. Laxalt?  
24 Senator Laxalt. No.  
25 Mr. Stern. Mr. Danforth?

1 Senator Danforth. Aye.

2 Mr. Stern. Mr. Chairman?

3 The Chairman. No.

4 Mr. Gravel wanted to be recorded as voting no on the  
5 previous Danforth amendment; I do not know how he will want  
6 to be recorded on this one.

7 The vote will be two yeas and fifteen nays.

8 Senator Packwood. Mr. Chairman?

9 The Chairman. Senator Packwood.

10 Senator Packwood. I have two or three amendments. The  
11 first one relates to the subject of heads of households that  
12 I raised the other day. Mr. Chairman, I do not intend to  
13 fight the entire battle of single taxpayers. I still think  
14 singles are discriminated against.

15 With four exceptions, all the members of this Committee  
16 voted the last time we had a vote to tax singles as we tax  
17 marrieds. This relates to only heads of households. That  
18 is defined as someone who has a dependent.

19 In most cases, 82 percent of the households are women  
20 in this country, most of them divorced or widowed, most of  
21 them with minor children, although on occasion, an aged  
22 parent, usually minor children.

23 The average income of an average household is \$6400,  
24 compared to the married, filing jointly, of \$16,075, yet  
25 today we give the head of household the smallest standard

1 deduction and we tax them at a higher rate than we do  
2 married taxpayers, even though in almost all of these cases  
3 there is only one wage earner with dependents.

4 So my amendment would simply say that a head of household  
5 will have a \$3,000 standard deduction or, if we change that,  
6 if we change that in the bill, whatever standard deduction  
7 we give to a married couple -- at the moment, it is \$3,000;  
8 the Chair was talking about \$3100.

9 In terms of tax equity or fairness, if there is any  
10 single group in this country that is unfairly treated, it is  
11 the head of household, earning relatively slight wages with  
12 usually ~~minor, dependent~~ children.

13 Mr. Chairman, I move that amendment.

14 The Chairman. Let me just explore one or two things  
15 about it that give me some problems.

16 Let us assume that a couple has two children and the  
17 marriage is dissolved. Where would they stand under the law  
18 that we are voting on here if the father took one child and  
19 the mother took the other so that they would both be heads  
20 of households?

21 Can you put that on the board and show you how that  
22 would work out?

23 Senator Packwood. They would both be able to claim  
24 head of household, but I think 82 percent of the cases, that  
25 only one adult, has all of the dependents. They could each

1 claim head of household in that case.

2 The Chairman. Put on the board there, Mr. Stern --

3 Mr. Shapiro. While he is doing that, let me make some  
4 observations. The heads of households treated as single  
5 people, they would have the lower end, two flat standard  
6 deductions. Mr. Packwood wants to go to the higher end to  
7 be treated as joint returns would be treated.

8 Based on the House bill, the revenue effect would be  
9 \$133 million for fiscal 1977, \$492 million for fiscal '78.  
10 The full year effect would \$363, less for fiscal '77; more  
11 for '78; on a full year basis it is approximately \$363 billion.

12 The Chairman. Suppose you put on the board how that  
13 would work out, where they each took one of the children.

14 Mr. Shapiro. Let's have one column be joint return.  
15 We will probably have three columns, joint return, then  
16 two columns, one for each spouse as head of household. One  
17 would be head of household, where they would only have one  
18 children I guess.

19 We are trying to do three cases, one if they are married  
20 and looking at them separately if they were divorced, and  
21 we are going to make several assumptions, where one has  
22 both children or where each one has a child. Where they  
23 are a joint return, they would be limited to the \$3,000.

24 If the family had two children and they were married,  
25 they would be limited to the standard deduction of \$3,000.



1 If they separated, each would be entitled to a \$2400  
2 standard deduction under the House bill.

3 The Chairman. At that point, those two people would be  
4 entitled to \$1800 more deduction if they separated and each  
5 ~~took a child~~, then they would if they both stayed together.

6 Mr. Shapiro. Under Senator Packwood's proposal and  
7 Senator Long's example they would have each a \$3000  
8 deduction.

9 The Chairman. That would be a \$540 bonus for a marriage  
10 breakup.

11 Senator Packwood. Let's put it in prospective, Mr.  
12 Chairman. If they split up and each take a child -- we  
13 realistically know what we are talking about in the real world.  
14 We are talking about women who in most cases, in many cases,  
15 are unable to get support trying to take care of their  
16 children, getting a very low wage and getting discriminated  
17 against in every direction in the tax code.

18 If that is not an inequitable situation, I do not  
19 know what is.

20 The Chairman. I want to do the right thing by the  
21 mother. I want to do something that makes overall sense,  
22 too.

23 By contrast, if that same family reunited, that would  
24 work out to be a \$540 penalty on the reconciliation. That  
25 would then proceed to set the stage for the same kinds of

1 games that we saw in Sixty Minutes where the people break up  
2 and have a divorce about Christmastime and then re-form the  
3 marriage the next year. The whole trip is taken care of,  
4 the vacation to the Caribbean island is covered in the  
5 expense of flying down to the Caribbean, having a vacation,  
6 having a good time, coming back and reforming the marriage  
7 after the 1st of the year.

8 You set the stage for all kinds of shenanigans. That  
9 admittedly would be the exceptional case, but you would have  
10 them.

11 I want to help these ladies. I have been trying to  
12 push -- and hope we have, in this bill, in the tax reform  
13 bill -- to give more help to these mothers, child care and  
14 things like that.

15 Senator Packwood. Mr. Chairman, what you are trying to  
16 do is take some very narrow specifics and argue to a  
17 generality. Most of these women are not going to get  
18 remarried to the husbands they have left, whether or not they  
19 have this tax deduction.

20 To be serious about it -- we can make light of this --

21 The Chairman. I do not mean to make light of it, but  
22 that is a fact. If they break up, each takes a child, it  
23 works that way.

24 Now, suppose they break up the marriage and one takes  
25 both children, how does that work out? Show us how that

1 works out on the board on head of household?

2 How much tax advantage and one takes the children and  
3 the other does not have a child?

4 Mr. Shapiro. That would be \$5400. The one with the  
5 children would be entitled to \$3,000; the one without the  
6 child would be entitled to \$2400. They would get the \$5400.

7 The Chairman. How much more deduction do they get that  
8 way than they do if they keep the marriage together?

9 Mr. Shapiro. If they keep the marriage together it is  
10 \$3000. \$5400 less \$3000 is \$2400, at a 25 percent rate is  
11 \$600.

12 Senator Curtis. May I ask the staff a question?

13 Could we not eliminate all of this, eliminate the  
14 penalty and so on, by transferring all of this tax benefit  
15 to the personal exemption?

16 Just do away with the standard deduction and apply,  
17 increase the personal exemption enough to do that? If  
18 there are two people supported, they get twice what it is,  
19 if they are five, they get that. It does not make any  
20 difference where they live.

21 Mr. Shapiro. Senator, it would eliminate the problem  
22 of the marriage penalty. One of the purposes of the  
23 standard deduction is to make it easier for people to fill  
24 out their tax returns, and they do not have to itemize  
25 deductions. If you do not have a standard deduction, that

1 means everybody would have to itemize their deductions.

2 Senator Curtis. There were as many people using the  
3 short form before we introduced the standard deduction.  
4 Before we introduced the standard deduction in a sizable  
5 amount to reduce taxes for the low income.

6 Mr. Shapiro. Most of the people use the standard  
7 deduction because at the time those great numbers were on  
8 the short form, 80 percent of the people were on the standard  
9 deduction. As wages go up, more people were itemizing.

10 The standard deduction has been increased over time to  
11 take that into account.

12 Senator Curtis. We have not done anything for them.  
13 The 1976 tax return was the toughest of them all and it has  
14 the highest standard deduction.

15 It seems to me that a person is a person. The way to  
16 grant the tax relief is to figure out how much ought to be  
17 given and raise the personal exemption that much. We are  
18 overstating the simplification value of the standard  
19 deduction.

20 The present tax return people have to file this spring  
21 is the most difficult that has ever been had in the history  
22 of the Internal Revenue Code and we have the highest  
23 standard deduction ever.

24 Mr. Shapiro. My observation is that you do need a  
25 full re-examination of much of the Internal Revenue Code to

1 solve many of the problems you have from a structural stand-  
2 point, when we get into a full review of the tax reform  
3 provision; but in this particular bill, it would be very  
4 difficult, in this context, to take care of some of the  
5 concerns you have.

6 The Administration has a full standard deduction,  
7 intended to alleviate most of the problem of filling out the  
8 tax return that has been caused by having a standard  
9 deduction, a minimum and a maximum. So 95 percent of the  
10 people can use the tax tables.

11 Senator Curtis. What we have done here - I am in favor  
12, of generous treatment of people of modest income. I think  
13 it has to be, with the high cost of living. But I do not  
14 think it has to be done by soaking the rich, or soaking the  
15 middle class.

16 When we move from personal exemptions to credits, and  
17 when we put emphasis on the minimum standard deduction rather  
18 than increasing the exemption or lowering the rates, we do  
19 it again.

20 I think it is ending up with all sorts of complications  
21 in our tax returns. I think it is not good for the overall  
22 economy.

23 If there is any particular bracket, middle-class, or  
24 rich or anyplace else that are not paying their just share,  
25 we should raise the rates. If we give credit for this and

1 credit for that, we are not going to have any taxes.

2 Mr. Shapiro . These are the concerns that when you get  
3 into structural revision, you will want to take account of.  
4 There are some advocating a credit for example, in lieu of  
5 the personal exemption, that would allow great reductions in  
6 the higher bracket to make up for the loss of the personal  
7 exemption at the higher level. They want to simplify the  
8 return by having a credit built into the rates and not have  
9 a personal exemption.

10 At the same time, some advocate the rates at the higher  
11 levels so they do not absorb this loss. There are a number  
12 of these types of structural provisions you are concerned  
13 about that the Committee should review thoroughly in the  
14 context of the revision of the tax system.

15 The Chairman. Let me say this about this amendment that  
16 is pending. I very much share Senator Packwood's desire to  
17 help these mothers who are trying to support children,  
18 and he has my complete sympathy in what he wants to do for  
19 these people.

20 I just think we need a better way to do it than this  
21 particular method.

22 For example, I supported this earned income credit.  
23 That would help these people here. In fact, I have been  
24 fighting for it for many years. That gives them a 10 percent  
25 add-on, you might say, if they are not making enough to even

1 pay a tax, and I would like to see us even on this bill  
2 do something to help these mothers, for example, to help  
3 cover the cost of child care. If we could expand on that  
4 to help them get somebody to look after those children or  
5 pay the expense of looking after those children while that  
6 mother is out trying to earn some money to support that  
7 family.

8 Those are approaches I would be happy to support.

9 Senator Packwood. This is an old subject; I do not want  
10 to dwell on it at length.

11 You know, the IRS pronounced recently they are not  
12 going to recognize these quickie divorces and remarriages  
13 for purposes of tax evasion. If people really got divorced,  
14 then got married for a standard deduction and split the  
15 dependency of the children for a month or two, the IRS is  
16 not going to recognize that for tax purposes.

17 Here you have, of all the people who file returns, the  
18 female head of household is the lowest average income, she  
19 has a higher than average cost problem. She gets the  
20 lowest standard deduction and is taxed at a higher rate  
21 than married who has a higher income.

22 How gross can the disparity be? I would just like to  
23 ask for a vote.

24 The Chairman. Here is what troubles me about this.  
25 If you look at the same number of people -- I do not care if

1 you are talking about a family of three or a family of  
2 four, you are looking at the same number of people and you  
3 give them a better tax treatment because they are separated  
4 than because they stayed together in the marriage, and that  
5 is already subject to criticism, that singly they get better  
6 tax treatment than they do if they are together. And then,  
7 so taxwise you already have an advantage on the people not  
8 married. There is already an advantage on marital break-up.  
9 This makes it greater, and furthermore, it also creates  
10 trouble with what Mr. Woodworth is trying to work out for  
11 simplification.

12 I wish you would tell me what the Treasury attitude  
13 about this thing is, Mr. Woodworth.

14 Mr. Woodworth. First of all, we recognize that there  
15 is a problem on the tax treatment of heads of households and  
16 we hope to be able to work on that this fall. We believe  
17 that this is a bigger job than it is possible to do in the  
18 short period of time available.

19 Now, both from the standpoint of our study and the  
20 standpoint of your consideration, as I analyze your proposal,  
21 it does seem to me as if it contains some very real problems.

22 While I understand what you are driving at, it seems  
23 to me that it would not be the kind of thing that this  
24 Committee would want to see happen.

25 I do not see why you would want to have an increase in



1 the standard deduction of the additional -- there is  
2 already some increase, let me point that out, there is  
3 already an increase when they are divorced. That goes from  
4 \$3,000 to \$4,800 ~~under~~ the House bill.

5 Now, what you would do is you would increase this still  
6 further, and it seems to me as if you are providing a very  
7 definite incentive for divorces.

8 I know that that is not the intent. I think it clearly  
9 has that effect, and that is true, even if they both do not  
10 claim head of household. That is true if only one of them  
11 claims head of household and the other one claims single  
12 status.

13 Senator Packwood. I am almost struck by the argument  
14 that these women are getting divorced for tax reasons. It  
15 is incredible beyond belief that the Administration would  
16 say that.

17 I would like a vote.

18 Senator Hathaway. I would like to offer a substitute.  
19 We will split the difference and give them \$2700, the  
20 difference between the single and the married.

21 The Chairman. Senator Matsunaga?

22 Senator Matsunaga. As we legislate here, we need to  
23 remember that one of the basic purposes of taxation is to  
24 set a sound, national policy. Of course, the Chairman has  
25 already hinted, but as much as I have great sympathy for the

1 class of people, taxpayers, as Senator Packwood has,  
2 it would be setting a bad social policy.

3 Furthermore, the Senator's proposal goes counter to  
4 the word from the White House -- ye who is living in sin,  
5 get married.

6 The Chairman. Senator Moyhihan?

7 Senator Moynihan. Mr. Chairman, I recognize the  
8 difficulties that you have with this proposition and that  
9 will be decisive with me in the vote we are going to have,  
10 but I would like to say that Senator Packwood has raised  
11 a fundamentally serious question, in that area, where tax  
12 policy, fiscal policy, intersects with social policy and  
13 Dr. Woodworth should know my respect for him, but to say that  
14 there are realms of evidence beyond the mere calculation  
15 of what a classical economic man or woman will do in a set  
16 of circumstances, there is just no evidence.

17 I think that I know the literature. There is not any  
18 evidence as to what is the impact of the income tax measures  
19 on social structure.

20 At the same time, we see an ever-increasing number of  
21 female heads of households which do have the disadvantages  
22 which Senator Packwood has spoken of where a very large  
23 proportion of American children are raised -- I think you  
24 would be startled at how large a proportion of American  
25 youth, probably as much half, at some time lived in a single

1 parent, typically female, head of household in which the  
2 sole source of support is what that woman has.

3 The Senator has raised a good question. My disposition  
4 is that it is a complex question and ought to be for a  
5 permanent change of the kind the Administration can propose  
6 or we can devise.

7 I do hope the Administration would come before this  
8 Committee with information better than it must be assumed  
9 that people prefer not to get divorced, not to get divorced  
10 or break their vows.

11 We know that there is little to suggest that such  
12 fundamental human life decisions are made in terms in a  
13 calculation of a \$350 bonus. We have an urgent social  
14 problem and we ought to address it. Senator Packwood has  
15 raised the right question.

16 The Chairman. Let me address myself quite apart from  
17 the possibility of just deliberate tax avoidance, just in  
18 terms of how it works out. Let us assume that everybody is  
19 in total good faith, which is the average case. A, they  
20 get better tax treatment; they save money by divorce. That  
21 is the way it is now: you make money by divorcing and  
22 having two homes rather than one. Against taxes, you make  
23 a profit.

24 The discrimination is you have a big marriage penalty  
25 anyhow. This places a further burden on staying married.

1           Assuming that there is a separation, this places a big  
2 tax burden on a reconciliation.

3           Why would you want to do that? It seems to me that  
4 there is bound to be some way you could help these mothers  
5 and children without putting a bigger penalty on marriage  
6 and a bigger tax burden on reconciliation.

7           Senator Roth. Would the Chairman yield at that point?

8           The Chairman. Yes.

9           Senator Roth. There seems to be, however, a problem,  
10 not only with mothers and their children, but it is often  
11 true that the single person has the burden of taking care of  
12 a parent. I do not think going the route you are talking  
13 about of child care and something like that would entirely  
14 answer the problem.

15           The Chairman. Let us amend that to take care of the  
16 old people, too. Give them a tax advantage for taking care  
17 of the aged. I am for that also.

18           Senator Packwood. A tax advantage for taking care of  
19 your parent?

20           Could we have a vote? I would like to have a vote on  
21 my motion.

22           The Chairman. Call the roll.

23           Mr. Stern. Mr. Talmadge.

24           The Chairman. No.

25           Mr. Stern. Mr. Ribicoff?

1 Senator Ribicoff. Aye.  
2 Mr. Stern. Mr. Byrd?  
3 (No response)  
4 Mr. Stern. Mr. Nelson?  
5 (No response)  
6 Mr. Stern. Mr. Gravel?  
7 Senator Gravel. Pass.  
8 Mr. Stern. Mr. Bentsen?  
9 (No response)  
10 Mr. Stern. Mr. Hathaway?  
11 Senator Hathaway. Aye.  
12 Mr. Stern. Mr. Haskell?  
13 Senator Haskell. No.  
14 Mr. Stern. Mr. Matsunaga?  
15 Senator Matsunaga. No.  
16 Mr. Stern. Mr. Moynihan?  
17 Senator Moynihan. No.  
18 Mr. Stern. Mr. Curtis?  
19 Senator Curtis. Aye.  
20 Mr. Stern. Mr. Hansen?  
21 Senator Hansen. Aye.  
22 Mr. Stern. Mr. Dole?  
23 Senator Dole. Aye.  
24 Mr. Stern. Mr. Packwood?  
25 Senator Packwood. Aye.

1 Mr. Stern. Mr. Roth?

2 Senator Roth. Aye.

3 Mr. Stern. Mr. Laxalt?

4 Senator Roth. Aye.

5 Mr. Stern. Mr. Danforth?

6 Senator Danforth. Aye.

7 Mr. Stern. Mr. Chairman?

8 The Chairman. No.

9 I have Mr. Bentsen's proxy: no.

10 Nine yeas, seven nays.

11 How much would that cost?

12 Mr. Shapiro. On a full-year basis, \$363 million; fiscal  
13 year effect, \$133 million for fiscal '77.

14 The Chairman. On your simplification, that gives you  
15 three kinds of people to look at instead of two.

16 Mr. Shapiro. There would be two columns.

17 Mr. Woodworth. Just two columns. What you were talking  
18 about might have done that, this does not.

19 Senator Packwood. Mr. Chairman?

20 The Chairman. Senator Packwood?

21 Senator Packwood. I have a second amendment.

22 \$5 million a year, relates to day care, As of January  
23 1st of this year -- Senator Hathaway is a co-sponsor, that  
24 provision ran out, which allows employers to build day care  
25 facilities for employees, and to amortize them on a five year basis.

1 This would extend it for five years. The cost is  
2 \$5 million or less.

3 Mr. Shapiro. I estimate that it is even less; closer  
4 to \$1 million.

5 Let me just tell you some background. There were a  
6 series of provisions which would provide a special five-year  
7 amortization. This was one of those.

8 When it came time to extend those, the House Ways and  
9 Means Committee heard testimony on a series of these and  
10 it did not appear of checking the data of some of these  
11 agencies downtown there was a significant interest in  
12 extending this one at that time.

13 Therefore, this particular provision lapsed; therefore,  
14 it was not extended after 1977.

15 Senator Packwood's amendment would extend it five more  
16 years, beginning January 1, 1977 through 1982. The reason  
17 it has a low revenue effect, very few people have used it.  
18 That was the reason why it was allowed to lapse.

19 The Chairman. All in favor, say aye.

20 (A chorus of ayes.)

21 The Chairman. Opposed, no?

22 (No response)

23 The Chairman. The ayes have it.

24 Senator Packwood. I have a third one; again, it  
25 relates to day care.

1           You will recall last year when we passed the using your  
2 homes for business purposes, we said you could only write  
3 off those rooms that were used for exclusive use. It has  
4 presented problems for those people who have day care in  
5 their homes, because if you have kids sleeping in the  
6 bedroom, they feed them in the kitchen, they use the  
7 bathrooms, yet they do not use any room exclusively for  
8 daycare, so the amendment that I have would cost about \$40  
9 million a year, and the amendment that I would have, which  
10 says that for home day care purposes the exclusive use test  
11 does not apply, but there are two exceptions so it is not  
12 abused.

13           One, you cannot deduct any more for day care than the  
14 amount that you receive in day care income. If you have  
15 an apartment for \$1,000 a month and you have day care and  
16 are using part of it and you are picking up \$200 or \$300  
17 a month in day care, you cannot disproportionately write off  
18 the cost of your apartment. That is one provision.

19           The other is, you can only use it in terms of deprecia-  
20 tion of your rooms, that portion of it that time is devoted  
21 to day care. If you take care of kids one day a week, you  
22 can only take that proportion in depreciation.

23           The Chairman. Mr. Woodworth, what is the Treasury's  
24 view?

25           Mr. Woodworth. Treasury would oppose the basic point



1 that I think this suggestion overlooks, that is the fact  
2 that if the individual has a home in the first place, if  
3 they do not use it exclusively for this purpose, but do use  
4 it for personal purposes as well, then they would have  
5 incurred the cost of maintaining the home in any event,  
6 so that there is no additional business expense involved  
7 in making the use of the home available part of the time  
8 for this purpose, or for any other business purpose.

9 The only difference between this and other cases is  
10 that this happens to be a more appealing use of the home  
11 than some other uses of the home. The same conceptual  
12 problem exists in both cases.

13 Senator Packwood. It is a pro rated deduction. If  
14 they use the home for day care twenty hours a week they can  
15 take 20/176 in their deductions.

16 Mr. Woodworth. It is virtually impossible to compute,  
17 for anyone to know precisely how much it is used for  
18 different purposes.

19 Senator Packwood. I remember something, Mr. Chairman,  
20 that you said when Mr. Charls Walker was Under Secretary of  
21 the Treasury. You said, Treasury is normally opposed to  
22 any amendment that loses money, and the Treasury is normally  
23 wrong.

24 The Chairman. All in favor of the amendment, say aye.

25 (A chorus of ayes)

1 The Chairman. Opposed, nno?

2 (A chorus of nays)

3 The Chairman. The ayes have it.

4 Let me ask you about the matter I raised yesterday.

5 Mr. Shapiro, can you give us some estimates on what the cost  
6 would be on respect to this day care matter?

7 Mr. Shapiro. All right, Senator.

8 You are referring to providing a credit for domestic  
9 workers and aged?

10 The Chairman. I had in mind a credit for day care for  
11 mothers to hire someone -- something you will like, Senator  
12 Packwood -- something to make it more attractive for  
13 mothers to hire, for working mothers to hire someone to  
14 help with the children while the mother is out trying to  
15 increase the family income or trying to earn something for  
16 the family.

17 How does the cost of those things work out?

18 Mr. Shapiro. Senator, under present law we have a  
19 child care credit which is a 20 percent figure for children.  
20 If you are talking about increasing the 20 percent to  
21 25 percent, the same percentage you have for employing the  
22 credit, somewhere in the neighborhood of about \$200 million.  
23 just by increasing that 20 percent existing law for child,  
24 care; but increasing that so the same 25 percent credit  
25 applies as applies to the employment credit.

1 Of course, that would not change the rules. For  
2 example, it would not apply to domestic workers, it would  
3 not apply to the care of the aged. It would apply only to  
4 domestic workers if they were hired to help out with the  
5 care of the children in the home as well as doing some of  
6 the household work.

7 If you wanted to expand the existing law to apply it  
8 more generally where working people can hire domestic workers  
9 or where elderly people can have people come in their home,  
10 there is a series of rules that can be considered by the  
11 Committee and the revenue costs would vary.

12 The Chairman. What is the range of costs?

13 Mr. Woodworth. We have a proposal which is essentially a  
14 25 percent credit on the first \$4,000 of wages. If you apply  
15 that to the series of rules that we have here, it goes up  
16 to \$700 billion.

17 The Chairman. I am not going to offer it at this time.  
18 I will talk to you about that later.

19 (Thereupon, at 12:10 p.m. the Committee recessed to  
20 reconvene Friday, March 18, 1977.)

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