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COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES
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The following is the text of remarks delivered April 9, 1981 by Representative Dan Rostenkowski (D-Ill.), Chairman of the Ways and Means Committee, to the Chicago Association of Commerce and Industry in Chicago:

Seven weeks ago I said the Ways and Means Committee will pass a bill to cut taxes for both individuals and business. Today I will give some shape to that promise.

I'm not here to define a Democratic alternative to the President's tax proposal. I'm not here to lay out a Rostenkowski alternative. I'm here to define the scope of a bill that preserves the spirit of the President's tax plan -- creates a much healthier climate for investment and productivity -- and most important, strikes that essential political and economic balance to pass Congress.

Inflation is both the enemy and the measure of any economic package. The President is clear in his promise to slow inflation. It's also clear that the nation will measure the success of the final package by the rise or fall of the inflation rate. The announcement last week that the wholesale price index was up to an annual rate of 16 percent only emphasizes the power of this dragon.

For all the talk about inflation -- going all the way back to the "Whip Inflation Now" buttons of the mid-70s -- we have not been able to control it. Worst we seem to be learning to live with it. After almost a decade of economic uncertainty we are becoming a nation of hedgers -- always looking for safe, if not productive, mattresses for our income.

This anxiety builds on itself as workers fight for higher wages, as business prices chase wages, and interest rates -- the most sensitive gauge of our national confidence -- ride the top of the spiral.

Inflation has robbed us at the pay window. It has robbed us in the supermarket. It has pushed housing and cars and other durables beyond our reach.

Inflation has driven up the cost of government -- whether paying social security benefits or building battleships. Inflation has also distorted the impact of the tax code.

As working Americans try to stay even with inflation, their increasing earnings become the ironic victims of a progressive income tax. As marginal tax rates have risen we have turned savers into spenders -- pushed investors into shelters -- and driven many taxpayers underground.

When Americans feel that spending is wiser than saving or investing, the productive engine of business and industry is robbed of its fuel. Inflation, high tax rates and low return on investment make a share in Detroit or Pittsburgh far less attractive to most people than running up their Mastercard bill.

When equity investment falls off and debt financing becomes habit, business turns as cautious and pessimistic as the bankers they borrow from. Inflation has outstripped their ability to recover capital investments. Energy costs have rendered yesterday's technology obsolete. The bottom line is a reluctance -- born of uncertainty -- to commit massive amounts of capital required to finance future productivity and expansion.

Does the economy need a jolt of new investment? Of course it does. President Reagan's instincts are absolutely correct.

Does the country need a large tax cut? Of course it does. But not a tax cut invented in a test tube -- but rather a tax cut shaped by the push and pull of real economic and political forces.

That's what the democratic process is all about.

I applaud the President for his drive and his goals. (I also appreciate his commitment to campaign pledges.) Without question, he carries forward the broad demands of the nation. I think Congress will answer those demands with an economic package that he can confidently sign. After all, we too were elected to make economic policy -- and every two years this nation judges that policy at the polls.

Work on this year's tax bill began the day the 1978 bill was signed into law. We held extensive tax hearings the following year. Last year we spent much of the summer listening to tax proposals from the private sector. In September the Senate Finance Committee passed a $40 billion tax cut bill that reflected the most visible tax issues of the day. Ronald Reagan -- then on the campaign trail -- even said he could vote for it.

The Reagan Administration answered the November "mandate" with a new brand of economics -- a dramatic increase in defense spending -- and the pledge to balance the budget. I think the President has done a terrific job of concentrating pressure to check excess in the federal government. His parallel goals of dramatic economic growth and a sharp decline in inflation and unemployment have deep support in Congress.

What concerns me -- and most of the economists that testified on the question of the President's tax plan -- is not his ends, but his means. There is broad doubt in the committee and on the House floor that massive, across-the-board individual cuts and depreciation reform will produce the economic results promised.

The supply-siders are the only ones who claim not only to know the true dynamics in the economy -- but the inner thinking of the 100 million or so working Americans who shape that economy. The rest of us aren't nearly as sure what $50 billion or so in tax cuts will do to the economic behavior of Mr. and Mrs. Smith.

What we do know is that lower marginal tax rates will give working families more money to spend.

What we don't know is where -- and how much -- people will save and invest. We don't know whether a middle-income family will invest their tax cut in U.S. Steel -- or a trip to Disneyland.

We have no guarantees that the tens of billions of dollars in additional budget cuts the Administration expects over the next few years will -- or should -- make it through Congress. We don't have any guarantee that the military budget won't put heavy pressure on inflation -- or overrun its budgetary limits. We don't know whether today's ailing industries will regain enough strength to reduce unemployment -- or whether the price of imported oil will remain stable.

In short, the future is less than certain.

Yet we are asked to go along with the new supply-side theories and commit hundreds of billions of dollars in tax cuts for the next three years with the promise that if we throw on the automatic pilot that David Stockman will land the plane on a balanced budget in 1984. That demands more trust than I can give. I want at least one hand on the wheel -- and so would you.

The tax plan I am outlining today is born of the same economic concerns that move the President. It is a bold plan -- strongly guided by the President's economic goals to promote more work, more savings, more investment and more productivity. It truely matches the spirit of the President's plan.

We differ on the size of the overall tax cut -- and the three-year escalation. Congress will no doubt give a greater share of the tax cut to middle-income families -- on the faith that they will essentially determine how strong the economic recovery will be. I think we feel a stronger obligation to protect the working poor.

The proposal has three major sections: individual tax cuts, savings and investment incentives and tax cuts to stimulate business growth. I will only dwell on the broadest areas, leaving some of the more narrow provisions for later discussion.

In keeping with the thrust of the President's bill, there is universal support on the committee for cuts in marginal tax rates beginning July 1. Our goal will be to offset payroll tax increases and bracket creep in most income ranges.

I fully endorse a reduction in the maximum rate on investment income from 70 percent to 50 percent -- effective July 1 -- bringing the maximum capital gains rate down from 28 percent to 20 percent. Almost to the man, economists appearing before the committee agreed that this reduction will do more to spur productive investment than any other measure under consideration. They are convinced that investment will be drawn out of tax shelters and funneled into much more productive areas of the economy.

There is near unanimous support on the Committee to ease the marriage tax penalty against working spouses -- beginning January 1, 1982. It is an inequity that has become more accute as inflation and social trends have dramatically increased the number of two-earner families. The adjustment is expected to encourage more productivity as well-trained men and women are encouraged to move back into the marketplace as second earners.

The collective effect of these cuts is focused most directly on people earning between $20,000 and $50,000. This segment of the workforce makes up 43 percent of all taxpayers -- and pays 50 percent of all individual taxes. These are the people who will make the most critical economic decisions in the coming months. They -- not the very poor or the very rich -- will be the measure of confidence in the final economic plan. If I -- as a Democrat -- can be accused of income redistribution, it's to this group. I trust that Congress will vote a greater proportional share to those in this income range than the President's plan.

Without question, the hardest hit by inflation and payroll taxes are the working poor -- those whose earned income rarely lifts them above the poverty line. When you combine increased taxes with the reduction of public assistance (both as a result of inflation) workers in this income range have less and less incentive to work.

As a matter of philosophy, I question the benefit of taxing families below the poverty line. It doesn't make much sense to collect just enough income tax to make welfare more attractive than work. To that end I support a modest increase in the level at which the income tax begins to fall on earnings.

There is broad committee support for several tax incentives specially targeted to personal savings and investment. Instead of taking on blind faith the supply-side argument that the taxpayers -- especially those in the highest brackets -- will generously invest and save, most members on the committee would like more specifically targeted incentives. That way we get a much stronger guarantee that a tax cut dollar is headed toward a productive end.

Highest on the list is a significant expansion of individual retirement accounts (IRAs). From a tax policy point of view, we achieve two critical objectives -- forced long-term savings and greater economic security for retiring workers.

The present limit on deductible contributions should be increased from from $1,500 to $2,000 of earned income for employees without a qualified pension plan.

We should extend the IRA concept to employees who are already covered by a pension plan -- allowing tax deductible contributions of up to $1000 of earned income. Roughly three-fourths of the tax cut generated by expanding IRAs will benefit taxpayers with incomes below $50,000.

I will also support an increase in the maximum limitation on contributions to a Keogh plan -- from $7,500 to $15,000.

And finally, as an additional savings and capital formation incentive, I will support the concept of establishing tax-deferred dividend reinvestment plans to encourage people to purchase new shares in public utilities that are trying to expand capital investment into more efficient plant and equipment.

Last year my colleagues on the committee -- Barber Conable and Jim Jones -- rallied broad support for accelerated capital cost recovery and a simplified depreciation system. Their concept -- known as "10-5-3" -- was modified in the President's bill.

The need for depreciation reform is unquestioned. The President's formula, however, contains a series of defects that have been identified by most of the economists and businessmen who have testified before the committee.

We have not arrived at a formula ourselves. We continue to debate and test alternatives. But I will quickly lay out the standards that essentially guide us:

-- simplifying the present system by reducing the 130 different classes of assets under the ADR system -- and dramatically shortening capital cost recovery periods for personal and real property.

-- eliminating the uncertainty of debating "facts and circumstances" with the IRS by making use of the recovery periods mandatory -- as well as audit proof.

-- preventing the combination of the investment tax credit and a liberalized depreciation formula from yielding back more than a dollar in tax relief for a dollar invested. No investor should get more from Uncle Sam than he would by deducting the full cost of the asset in the year the investment was made.

-- maintaining tax neutrality between industries, between short-lived and long-lived assets, between commercial and residential structures, and between owner-occupied and leased structures. We intend to give all capital investment a better cost-recovery formula -- without creating any distortions.

-- making any revised capital cost recovery system fully effective January 1, 1981. Phasing in any formula simply delays the productive impact of full investments.

I am concerned that the bill developed by the Ways and Means Committee address the critical capital needs of distressed industries such as autos and steel. Many companies in these industries have substantial unused investment tax credits. It is my sincere hope that effective tax relief can be developed for these industries -- short of refundability -- to improve their cash flow. One possible approach -- which needs further review -- might be to lengthen the present 3-year carryback period for the investment tax credits -- or allow them to be carried back against 100 percent of tax liability.

As a congressman from Chicago I am committed to stimulating the vitality of our cities. I am concerned that tax policy not encourage the migration of business from cities to the suburbs -- and from one region of the country to another. To that end, I will actively press for a higher and better targeted rehabilitation tax credit. Specifically, I will support a graduated credit that will encourage renovation of industrial and commercial structures based on the age of the building. In addition, the graduated credit should provide significant incentives for the restoration of historic structures.

I trust the tax bill developed by the Ways and Means Committee will include provisions targeted to small business, research and development, and export promotion through reduced taxes on American citizens who work abroad.

This package is limited not only by the President's economic goals -- but also by budget constraints. I will oppose any additional measures that exceed those limits -- or substantially escalate revenue losses in the out years.

The sum of the parts add up to about $40 billion in the coming fiscal year. That puts it about $14 billion short of the President's mark --- carrying with it a smaller deficit and less inflationary risk -- and moving us more quickly toward a balanced budget.

We also move the most productive elements now being readied for the President's second bill up into this bill -- but again, maintaining the thrust of the President's overall economic package.

The President has proposed a three-year plan. I understand his concern that we give the country the certainty of extended tax cuts to encourage longer-range investment. In a perfect world, I would vote for a 10-year tax cut. But we're not living in a perfect world.

Rather, I think Congress can give the President the first year of a recovery plan -- with the promise that we will be only too ready to increase the cuts next year if growth is up and inflation is down. Congress has never been shy about stepping up to the tax cut table. And don't forget that the I am proposing today -- marginal rate cuts and savings and investment incentives -- are permanent -- not just one-year "fixes".

This package didn't come to me in the middle of the night. Tax bills don't fall from heaven, they evolve from years of experience and debate. Accute distortions and inequities in the tax code -- like the marriage penalty -- rise to the surface. Less critical -- and often less deserving -- appeals don't. By the time an issue is ready for passage into law, it has completed the roughest legislative slalom imaginable.

This is not my package. This is not a Democratic package. This is a consensus package . Components come from all the members of the Way and Means Committee. Together they comprise an overall design --- an overall balance -- an overall impact -- that we believe is right, given today's economic circumstances.

The package reflects a mood of caution and skepticism prompted by such optimistic "scenarios" from the White House. It is smaller in size than the President's bill. It asks for stricter accounting of the tax cut dollar. I think it is more efficient in speeding economic recovery.

This plan does not have unanimous support on the committee -- but it does have enough support among Democrats and Republicans to pass. And that -- at least by my training -- is the final measure of any proposal.