OUTLINE OF REMARKS

INTERNATIONAL PLATFORM ASSOCIATION

10:00 a.m. - August 6 - Hyatt Regency - Wash. D.C.

I. The Budget--Continuing Need for Action

A. The Senate is moving forward to implement our budget agreement: the Finance Committee reconciliation bill already has been approved, and the reconciliation bill from other committees is being debated. Now that we are getting down to substantive action on the deficit, the need to regain control over fiscal policy is more urgent than ever.

B. The President strongly endorses the tax reform and spending reduction bill passed by the Senate, because he knows it preserves the fundamentals of his program and increases the prospects for lower deficits and lower interest rates, which are crucial for recovery.

C. Congress now has to complete action on the tax bill and follow through to implement <u>every</u> part of the budget agreement. Spending has to be brought under control, or the budget will unravel and our efforts will have come to nothing. There are some disturbing indications that a "piecemeal" approach to the spending cuts advocated by the House leadership could block those cuts: that must not be allowed to happen.

D. The bill now in conference, originated by the Finance Committee, already includes the largest single spending reduction we will consider: about $17 billion. It also raises $98.9 billion in revenues from improved compliance, eliminating obsolete tax incentives, ensuring that everyone pays their fair share, and modest excise taxes and user fees.

II. The Economic Recovery Program

A. Sticking to Fundamentals

1. The deficits are not a result <u>of</u> the Reagan program, but of deep-rooted economic problems, some of which were underestimated by the administration. But we have to follow through on the administration's fundamentally sound principles of spending reduction, lower taxes to restore incentive, a firm but fair monetary policy, and a strong defense.

2. We are aiming at sustaining recovery <u>after</u> the recession. That is what the debate is all about.

No one advocates tax increases or further 'drag' on the economy while recession persists.

3. Significant progress is being made on the economy. Inflation in 1981 dropped to 8.9%, the lowest since 1977. Inflation is running at a 5 or 6 percent rate, and in March the CPI declined by three-tenths of a percent--the first such decline since 1965, and the largest drop since 1953. This is dramatic progress on what everyone considered to be our number one economic problem.

4. Interest rates remain too high, but they have come down. 15 percent is far better than 21 percent, and there is reason to expect a continuing, if gradual, downward trend this year.

B. The Recession

1. The recession is the reason our problems are more acute than anticipated. It has driven down revenues in the short run (lower inflation and slower growth) but has a lagged effect on slowing spending, while in the near term unemployment and related costs increase.

2. In 1980 the Carter administration tried to prime the pump after experimenting with monetary restraint--the subsequent clampdown proved that the "recovery" from that recession was a false one. Only now are the full effects of that same recession being felt. The important thing this time is to ensure a sustained, real recovery.

III. Tax Reform Package.

A. Many people are perplexed at the fact that we are raising new revenues this year, when we passed a tax reduction program last year that was supposed to restore certainty to the tax laws. The budget deficit problem is one major reason for the shift, of course: but our tax reform bill makes changes that are needed irrespective of the deficit problem. They are needed in the interest of fairness, simplicity, and economic efficiency.

B. We can get more revenue out of the present tax code. By improving compliance--which has dropped off in recent years because of inflation, high marginal rates, and the proliferation of special tax privileges--our bill raises about $26 billion over three years. Bu cutting back on the inefficient safe harbor leasing provision, we raise over $8 billion. And we cut back many other loopholes and preferences that no longer serve an important purpose, and which should be cut back or eliminated: tax breaks for self-employed pension savings, industrial development bonds, and insurance industry loopholes.

C. We reached a consensus to concentrate on improving our tax laws before we slap on new taxes. This is the approach President Reagan has endorsed, because it is fair and it preserves the tax cut for working people. Everyone must pay a fair share of tax: it is hard to justify new taxes, or cutting back the individual tax cut, unless we deal with the special exceptions that turn our tax base into swiss cheese.

D. Out of our tax package, all but $15 billion to $20 billion comes from tax reform and compliance measures. The rest comes from modest excise taxes and user fees, and taxes associated with particular government benefits.

IV. The 1983 Tax Cut

A. Senate Democrats persisted in trying to pare back the 1983 tax cut to raise revenue because that is "the path of least resistance." The President disagrees, and I disagree. That cut is needed to help American workers--it is needed to offset bracket creep and payroll tax hikes. And it is a firm promise we made to the American people.

B. Who is helped. There has also been a lot of criticism of the individual tax cut on the grounds it helps the rich at the expense of the average worker. But the American people want to keep their tax cut. In any event, the 'rich man' allegation is false. 36.6% of the 1983 cut goes to people with incomes between $20 thousand and $30 thousand. 53.7% of the tax cut goes to Americans earning $20 thousand to $50 thousand. 70% goes to those under $50,000.

C. In addition, it is worth noting who would be hurt worst by tampering with the third year. The group whose tax liability would rise the MOST is that $20-$30 thousand income class-in other words, the average working American. If this is a rich man's tax cut, explain it to the working man.

V. 1981 Tax Act and the Deficit

A. The 1981 Tax Act, though the largest tax cut in history, just stabilizes the tax burden. Revenues still will rise from about $600 billion in 1981 to about $800 billion in 1985. Receipts by 1987 should be 18.7% of GNP--the same as the average between 1963 and 1973. Without action, receipts would have been a crushing 24% of GNP in 1987.

B. The question is how high a deficit can be tolerated without "crowding out" or threatening a resurgence of inflation. Increased savings due to tax changes and the drop in inflation should ease pressure in financial markets. We must do more to ease that pressure without undermining the economic program.

C Many provisions of the tax act aid capital formation and innovation: R & D tax credits, capital gains reduction to 20%, IRA and other savings incentives. These coupled with rate cuts and accelerated depreciation, form the framework for regeneration of business activity.

D. Tax Indexing. Indexing is the major tax reform of 1981, and it is here to stay. It is also the most progressive change, and the most meaningful for working Americans. Indexing just means that Ccngress is accountable for tax increases--we cannot rely on tax inflation to keep the budget afloat to the tune of $1.7 billion or more per point of inflation. In Senate consideration of the budget resolution we defeated a move to repeal indexing by 56-34. Repealing tax indexing would risk signaling we intend to reinflate the economy.

E. Major Benefits in ERTA. With all the talk about deficits and tax increases, some have lost sight of the major--in some cases revolutionary--tax relief and incentives we provided in the 1981 tax cut.

1. Marriage penalty relief. A 10% deduction for the lower-earning spouse's income eases the tax burden on working couples.

2. Estate tax relief. The credit against estate and gift tax will rise to $600,000 by 1986: this will free many small and medium-size family estates from any tax, and greatly reduce the burden on all estates. An unlimited marital deduction forever eliminates the 'widow's tax'--there is no tax now on transfers between spouses. In addition, special use valuation for farm property was greatly expanded, easing the burden on family farms; and the maximum estate tax rate drops from 70% to 50% over four years.

3. IRA incentives. Every taxpayer can now deduct up to $2000 per year in contributions for individual retirement. This helps the small saver, can help boost the savings rates, and eases pressure on other private and government retirement programs.

4. Other provisions that provide significant help to the individual taxpayer include an expanded child care credit, an increase to $125,000 of the amount of gain on sale of a principal residence that can be rolled over, tax relief for Americans working abroad, and a charitable deduction for all taxpayers, regardless of whether they itemize.
For the first time in years we have a strong pro-taxpayer policy in Washington--that will not change, even though we are obliged to raise significant revenue in the short term to deal with the deficit. Our goal is to maintain tax relief over the long term and improve the fairness of the tax code.

VI. Future Agenda for Tax and Fiscal Policy

A. Revenues and Major Items in Our Tax Reform Package

1. Thrust of future tax legislation will be to eliminate abuses and obsolete incentives and improve tax administration and collection. The 1981 Tax Act shows this trend, as in closing the commodity straddle loophole.

2. Last September the administration proposed tightening in these areas, and by new enforcement devices. Many of these provisions are included in our tax package:

- Completed contract method of multiyear defense contracts.

- Industrial development bonds (restrict, require matching efforts from State or locality, and sunset).

- Eliminate insurance industry loophole (modified coinsurance).

- Capitalization of construction period interest and taxes.

3. Underground Economy

a. The Compliance Gap.

The IRS estimates that $100 billion is lost annually though noncompliance with the federal income tax laws and that amount will rise to $133 billion by 1985. Our tax bill raises nearly 30% of its revenues by steps to help close this gap.

b. The Proposal

Our bill would improve the current system of information reporting. 9 to 16% of interest and dividends paid go unreported, as do 44% of capital gains. We can improve the reporting system by including Federal debt and bearer obligations and impose real penalties on those who refuse to comply.

c. Withholding on Interest and Dividends.

The administration proposed withholding, and this has been adopted at a 10% rate. Exemptions are provided for the elderly and low income taxpayers, and protection are available to institutions while they make the transition to the new system. Withholding brings in about $12 billion over three years without raising anyone's taxes.

d. Coverage

In addition, new penalties would hit the sophisticated tax avoider and the fraudulent corporate tax manager. The interest rules would be revised to reduce current incentives to defer paying taxes.

4. Minimum Tax

a. Current Law

Current law includes three very complex minimum taxes, two on individuals and one on corporations. These taxes raise only $1.5 billion and still permit significant numbers of taxpayers to pay no tax.

b. Tax Bill Provisions

The provisions in our tax equity bill would completely revise and simplify the minimum tax. In lieu of the overlapping alternative and add-on taxes on preference items, the minimum tax on individuals is a flat rate of 10% and 20% on a more comprehensive, economic income base. Similarly, certain corporate preferences are cut back 15%.

c. The Tax Base: Individuals

Included in the tax base for individuals are adjusted gross income and items like excess accelerated deductions, intangible drilling costs, research and experimental expenditures, interest on all-savers, and other items.

d. Corporations

Certain tax preferences for corporations will be cut back 15%. These include DISC, some percentage depletion, intangible drilling costs, interest deductions for banks to the extent that tax-exempt

e. The minimum taxes are fully consistent with the 1981 tax cut. That tax cut provided incentives by reducing marginal tax rates. The marginal tax rate of a minimum tax will only be 10% or 20%, with a 15% scaleback for corporations: all taxpayers with substantial real income ought to pay some income tax.

5. Leasing

a. Over $8 billion is generated by cutting back on the safe-harbor leasing provisions of the 1981 Tax Act. Those provisions would otherwise cost about $30 billion over six years, and the figure could go higher when Treasury completely analyzes its report on leasing transactions.

b. Changes include a 1985 Sunset, offsets in other tax preferences, and direct limits on tax sheltering.

6. Altogether our tax package paves the way for a broader tax base,a fairer tax system. This is the direction we will have to take in future revenue bills.

VIII. Flat Rate Tax

A. Growing frustration with our complex tax system and desire to ensure fairness are increasing interest in a flat-rate, or low-rate, simplified tax. More people believe that the complexity of the tax law puts a premium on getting sophisticated legal and accounting advice to take advantage of loopholes--and that seems to benefit the wealthy at the expense of the average taxpayer.

B. Several flat tax proposals have been made, and there is no question that in the years ahead we will be working to simplify taxes, eliminate obsolete tax provisions, and bring rates down in exchange. At the same time, there is no comprehensive scheme we could implement right away--we need input from the Treasury, which is reviewing the issue. Most proposals leave some progression in rates, allow for certain highly popular deductions, and exempt low incomes. When it comes to a comprehensive tax base, everyone has their favorite exemption they want to protect.

C. There will always be some complexity: we do have to define "income", and our work with the minimum tax may help us reach a more comprehensive definition. But we can agree on the principles of equity, balance, and simplicity in taxes, and work to improve the system. These are the issues the Finance Committee will review in hearings later this year.

IX. Balanced Budget Amendment

A. Our acute fiscal imbalance and signs of deterioration in the budget process are increasing support for constitutional restraints on fiscal policy. The Senate on Wednesday approved S.J. Res. 58, a proposal the President has endorsed.

B. S.J. Res. 58 requires Congress to adopt a balanced budget unless overridden by 3/5 vote. It also requires an actual majority to raise taxes over the previous year as a percentage of national income. This means we will be obliged to balance and coordinate decisions on spending and taxation--a sort of 'truth in government' provision.

C. No one wants to resort to the Constitution unnecessarily, but Congress has proved too often that it will not maintain long-term fiscal restraint. We need strong measures to redress that balance, and only the Constitution can provide them. We have tried statutory controls: they have not worked.

D. There is no 'perfect amendment' and there are other ideas that merit consideration; a two-year budget cycle, an item veto for the President, and different accounting systems to clarify how we are spending taxpayers' dollars. But S.J. Res. 58 is as good a proposal as we have developed, and it deserves a chance to work. Enforcement legislation, and cooperation between the President and Congress, will be crucial to the success of this fiscal reform.

X. Summary--Where We Are Now

A. A Watershed Year. The recession makes this a tough year for Congress and the President. There are no easy or palatable options available. That means we have had to establish our priorities swiftly but with care: not an easy task. But if we prove that we can work together to deal now with problems that have been building over many years, we will have a major breakthrough in favor of economic recovery.

B. Shared Effort. The economic problem can only be addressed by a joint effort all around--Congress and the President, Democrats and Republicans. Those who would seek partisan advantage from our economic dilemma are mistaken. If we hang, we all hang together, regardless of party. The people will not care who prevented action, if nothing is done. What we need are results.

Summary of H.R. 4961

Spending Provisions

• Medicare: In general, the program changes in this area are designed to achieve better allocation of costs among beneficiaries, providers of services, and the government. Thus, for example, deductibles are increased, premiums would fixed in one case at a percentage of costs, and copayments would be introduced for the first time in the area of home health care. These changes are designed to avoid actually cutting benefits while increasing incentives for cost control on the part of all concerned. Better controls are put on certain reimbursements and fees to health care providers, also in the interest of controlling costs. Administrative improvements such as better audit coverage and changes in timing of certain payments also contribute to the savings in the package.

• Medicaid: As with Medicare, the focus is on better cost-sharing and administrative improvements. Expanded use of copayments and reduction in error rates (better administration) play a key role in achieving savings in this area.

• Aid to Families With Dependent Children (AFDC): The emphasis here is on tighter enforcement and simplifications that cut costs, including rounding of benefits and eligibility cut-off amounts and reducing Federal matching for payment errors. Applicants would be required to search for work, sanctions would be imposed on those who refuse to work without good cause, and the Federal coverage of particular needs and individuals would be clarified. Coverage of minor parents would be tightened, and States would be allowed certain administrative adjustments. Child support enforcement would be strengthened.

• Supplemental Security Income: First month benefits under the program would be prorated from the later of date of application or date of eligibility, and benefit payments and eligibility cut-offs would be rounded down. Cost-of-living adjustments would be coordinated with social security, the Federal commitment to 'hold harmless' certain States would be phased out. Overpayments under SSI could be collected from other Social Security Administration programs.

• Unemployment Compensation: Federal matching share of extended benefits would be withheld to the extend those benefits result from a State's failure to round down benefits.

Revenue Provisions

• Individual Tax Base: A stronger minimum tax ensures that upper-income taxpayers must pay a fair share. The floor under the medical deduction is raised to 7 percent, and that under the casualty loss deduction is raised to 10 percent. Deductions for pension plans by high-income people are limited.

• Tax Compliance: Information reporting and penalty provisions are strengthened, and voluntary withholding on pensions is restructured. Ten-percent withholding is imposed on interest and dividends, where currently 9 to 16 per cent of income goes unreported. Most of our major trading partners have a similar requirement, which the IRS has long deemed essential for equitable enforcement: especially when you consider that wage withholding results in a 99 percent compliance rate. Appropriate exemptions are allowed for the elderly and those with low incomes.

• Business Tax Base, Eliminate Obsolete Incentives: The bill tightens up on obsolete or unjustified tax preferences in the business sector, including safe harbor leasing, tax treatment of life insurance, the completed contract method of accounting for long-term contracts, and foreign oil income. A range of tax preferences is scaled back by 15 percent, tax incentives for mergers and acquisitions are reduced, and construction period interest is required to be capitalized. ACRS is scaled back so benefits do not exceed that of an immediate deduction. Abuses of tax benefits for companies operating in U.S. possessions are eliminated, corporate tax payments are accelerated, and the deduction for business meals is limited to 50 percent of the cost unless the taxpayer is away from home on business. The goal is not to squeeze business, but to ensure a fair distribution of the tax burden and eliminate 'incentives' that have not been helpful to the economy or the business community as a whole.

• User Charges, Taxes Associated with Specific Spending, Excises: User charges, such as the taxes that finance the Airport and Airway Trust Fund, are increased, the telephone tax in raised, and Federal employees are subject to the Medicare tax on the ground that they benefit from the Medicare system. Unemployment taxes are raised to avoid a drain of general revenues to cover unemployment benefits. Finally, the cigarette excise tax is temporarily increased