OUTLINE OF REMARKS

Boston University Congressional Forum

April 7, 1983--Hyatt Regency Hotel--8:30 a.m.

I. The Economy

A. Prognosis. We have to realistically assess the state of the economy and the prospects for the next few years. The fact is that the groundwork has been laid for a stable and lasting recovery, without renewed inflation. It is absolutely crucial that we proceed with care at this point, and not throw away the gains already made.

No one should doubt that we are making progress. In January the index of leading economic indicators jumped 3.6 percent--the biggest one-month rise since 1950, and the ninth increase in the last 10 months. In addition, the "concurrent indicators" of current economic performance rose .6 percent in January, showing we are in recovery.

1. Inflation was cut to 3.9 percent in 1982, from 12.4 percent in 1980. This is the lowest inflation rate since 1972. And the trend is continuing: consumer prices dropped 0.2 percent in February.

2. Interest rates are down and still falling. The prime rate is down to 10 1/2 percent, way down from the 21 percent that prevailed when President Reagan took office. Home mortgage rates are down 3 points since last year. Long-term rates for business loans are off 3 to 4 points from a year ago.

3. Government spending growth rate is down to 11.2 percent this year from 17.4 percent in 1980. The 1983 budget resolution projects the growth rate of government to fall to 7.5 percent by 1985.

4. Lower taxes with major improvements in tax equity will help buoy the recovery, both on the consumer side and on the investment side. The combined effect of the 1981 and 1982 tax bills has been to lower individual taxes over 3 years by $344 billion, as well as improve compliance and tax fairness. Lower individual rates boost personal income and restore incentive, while favorable capital cost recovery rules should spur investment.

5. In January, industrial production was up 0.9 percent; housing starts were up 36 percent; the stock market is up 300+ points over last August. These are tangible evidence of recovery.

B. Unemployment. The March drop in unemployment to 10.3 percent is continued good news, and the decline should continue, although there may be a few "blips" upward. Unemployment, of course, remains the major negative in the economic picture. High unemployment has to come down and stay down without inflationary stimulus--that is what we have failed to do in the past.

o Clearly there is a bipartisan consensus for more jobs. But resuming the inflationary policies of the past will not create lasting jobs, just an illusion of prosperity that leaves us worse off the next time we try to get "off the wagon."

o That means the most important thing we must do is judge carefully the degree of stimulus the economy can and should take, consistent with a firm anti-inflation policy. The Federal Reserve will play a key role, and has already shown a willingness to adjust its short-term goals based on an assessment of the weakness of the economy. We will not allow the recession to continue, but we will not reinflate the economy, either.

C. The Deficit and Interest Rates.

1. All our economic difficulties are, of course, related--high interest rates and slow growth boost the deficit, and higher deficits create greater uncertainty in the business community as to our future course; will there be more inflation, or less credit available for business expansion?

2. Because of this, it makes sense first of all to chart a path that is most likely to bring stable growth without inflation. Higher growth boosts revenues and cuts unemployment costs, thereby reducing the deficit as well: already, upward revisions of growth estimates are being made in light of the economic indicators.

3. In the short term, as the President urges, it makes sense to continue to review every part of the Federal budget in an effort to bring the deficit down. This means both defense and entitlements must be under scrutiny to maximize the efficiency of every dollar spent. A balanced deficit reduction program is still our goal: the Budget Committee will produce a budget resolution in the next few weeks.

4. Continued efforts to restrain the deficit by controlling Federal spending will give the Federal Reserve a bit more room to accommodate the potential for real growth that exists in the economy without inflationary pump-priming. But restraint in both fiscal and monetary policy is crucial if we want to maintain long-term confidence in the economic program. That means long-range goals must be carefully reconciled with efforts to respond to particular weaknesses in the economy. Radical attempts to reverse course would be self-defeating and must be resisted.

II. The Budget: The House and the President

A. We all know that developing a credible, deficit-reducing budget for 1984 and beyond is going to take a lot of hard work and give and take on all sides, Democrat and Republican, liberal and conservative. The President has made his proposal, and the House has adopted a radically different alternative. We are likely to end up with something in between, but we ought to consider for a moment who is closer to the mark in terms of the vital needs of our economy and in terms of natinal priorities.

B. House resolution. The House-passed budget resolution, engineered by the Democratic leadership, simply is not a credible plan for meeting our priorities and achieving sustained economic growth. The House recommends a $30 billion tax increase in FY 1984 alone. That is not only an unreasonable increase in the tax burden as we come out of a recession, it can only mean that House Democrats want to repeal the third year of the tax cut for the working people. Reneging on promises is no way to run the government, and that proposal must be rejected. Even the members of the House Ways and Means committee have expressed strong doubts that any more than $8 billion in revenue can or should be raised in 1984.

C. Defense spending. The President has recommended a 10 percent real increase in defense spending, and the House recommends a mere 4 percent increase. We all know that defense, like every area of the budget, will have to assume a fair share of the burden of deficit reduction. But surely we ought to take more seriously the President's concern about our national strength vis-a-vis the Soviet Union. We can and probably will have to modify the President's defense request, and the President will have to deal with both the Senate and the House leadership if we are to get agreement. We do have to get more out of each defense dollar spent. But the House-proposed increase is not wise, reasonable, or in the national interest.

D. Domestic spending. There is widespread agreement that we cannot let the burden of deficit reduction continue to fall on benefits for lower-income Americans. But that does not mean domestic spending is untouchable--it can and must be reduced, something the Democratic budget fails to acknowledge. The House resolution provides $25 billion more for nonmilitary spending than does the President's budget. $6 billion of that difference is in the health area: and certainly we have reached the point where we should acknowledge that Federal health program costs are not under control, and that changes to control costs are very much in order. The American people do want to share the cost of reducing the deficit in a fair way. But they do not want national security risked, or the tax burden on individuals raised to an unconscionable degree, just because some members of Congress do not want to reexamine programs that may have outlived their usefullness or have become grossly inefficient. Instead, let us work together, and with the President, to reach a bipartisan agreement like that worked out on social security.

III. <u>The Budget: Tax Issues</u>

A. There are lots of ways to raise revenue, but our job is to choose ways that are fair and consistent with good tax policy. We should resist the temptation to undo the progress that has been made in providing greater incentives for savings, work, and investment: those incentives will become more important as recovery proceeds. There are many base-broadening measures still to be considered that would improve the equity and efficiency of the tax code.

B. <u>Indexing</u>. The House budget assumes repeal of the tax indexing provision of the 1981 tax act, which takes effect in 1985. We all know that we have to compromise to get things done, but this is one area that we ought to leave alone if we are interested in sound tax policy and honesty in government. We can raise revenues--but why resort once again to back-door revenue increases generated by inflation? Tampering with indexing further risks sending a signal that we are prepared to reinflate the economy and generate revenues through bracket creep to deal with the deficit. That would mean undoing all the progress we <u>have</u> made over the past two years, and it would be a tremendous mistake.

C. <u>Outyear tax increases</u>. The President's budget recommends a contingency tax to raise $46 billion in FY 1986, consisting of a 5% surcharge and an oil tax, to be triggered if the deficit remains too high despite adoption of major spending cuts. It is not clear why we would need to use a "trigger" device to raise taxes based on deficit levels. It seems unlikely that a "trigger" mechanism would create the kind of reassurance on the deficit that the country is looking for.

If growth and revenues turn out <u>better</u> than now projected, we can always reduce taxes to the extent that becomes fiscally desirable. One possibility is to enact some additional base-broadening measures--improvements in equity and eliminating tax provisions that are economically inefficient--then provide for further rate reductions if the deficit is brought under control more rapidly than is now expected. This would maintain the momentum for a lower-rate, broader-based tax system that has been built over the last two years. It is also consistent with the administration's consideration of a streamlined and simplified tax structure with lower rates.

SOCIAL SECURITY

- Early in the morning of Friday, March 25, the "Social Security Act Amendments of 1983" were passed by Congress. This legislation implements the recommendations of the President's National Commission on Social Security Reform.

- Like the consensus reached by the National Commission last January, the social security bill was passed with broad bi-partisan support. Major groups representing the elderly, working people, and business came out in support of the legislation.

- This does not mean that everyone is happy with each and every aspect of the bill. The important fact, however, is that consensus was reached on the critical issue of shoring up the social security retirement system. As most of us know by now, the retirement fund would have been unable to pay full benefits beginning in July, and the remainder of the system -- including disability insurance and medicare would have been insolvent before the end of the year.

- The legislation will require concessions from everyone who has a stake in social security -- current beneficiaries, the working people who support the system, as well as government workers who do not now contribute to the system. Great care was taken to protect those least able to bear an additional burden.

MAJOR FEATURES

Coverage:

- As of January 1, 1984, all members of Congress, the President, Vice President, Social Security Commissioner, Federal judges, and other high level political appointees will be covered by social security. All other Federal employees hired on or after January 1 will also be covered. To this point, Federal employees have been the only major group not covered by the system.

- Employees of nonprofit organizations will also be covered. State and local governments will no longer be permitted to opt out of social security.

Benefits:

- For current beneficiaries, the annual cost of living adjustment (COLA) will now be payable in January each year rather than July. The COLA will be paid in full, but 6 months later.

- To protect the elderly poor, Supplemental Security Income (SSI) payments will be increased by $20 monthly beginning in July. This change will help all elderly, blind, and disabled poor who are on SSI, and will more than compensate for the COLA delay.

- For high income beneficiaries, half of social security benefits will become subject to Federal income taxes. Only those people who have an adjusted gross income plus tax-free interest income plus half of their benefits which exceeds $25,000 ($32,000 for couples) will be affected in any way.

Taxes:

- For working people, part of the social security tax increases already scheduled in the law (by legislation passed in 1977) will be accelerated. There will be no increase in the permanent tax rate scheduled for 1990, however. In recognition of the fact that social security taxes are already a heavy burden, a tax credit will be provided against the full amount of the increase in 1984.

- The self-employed will also have their taxes increased. This was necessary to equalize their contribution to the trust funds with that of a worker and his employer. Again, the added burden of these tax increases will be moderated by tax credits in future years, replaced by income tax deductability of self-employed taxes in 1990.

Long-range Reform/Elimination of Work Disincentives:

- For people turning 62 in the year 2000 or later, the social security retirement age will be very gradually increased from 65 to 67. (The age at which full benefits are payable would reach 67 in the year 2027.) Early retirement benefits would continue to be payable at age 62.

- Beginning in 1990, people who voluntarily delay retirement beyond age 65 will have their benefits increased by more than 3% a year, as is now the case. The delayed retirement credit will be gradually raised from 3% to 8% a year.

- Rather than reducing benefits by $1 for every $2 earned by a beneficiary 65 and older, benefits will only be reduced by $1 for each $3 earned in excess of the exempt amount (which is $6,600 this year).

- Together, these three reforms will adjust the system to take account of the improvements in longevity of Americans and will provide real incentives for older people to continue working.

Eliminating Inappropriate Benefits/Improving Equity

- In addition to all the "big issues" addressed by this legislation, this bill makes a number of small, but important, improvements in the way benefits are distributed. There are five provisions, for example, which will improve the adequacy of benefits for divorced and widowed women, thereby making headway toward a more equitable social security system for women.

- At the same time, scarce dollars will no longer be spent on inappropriate benefits. The bill includes provisions to cut off benefits to convicted felons who are in jail as well as to aliens abroad who are drawing benefits as dependents or survivors without having lived in the U.S. for at least five years as a relative to the wage earner on whose account they are drawing benefits.

Stabilizing the System:

o In the past, with benefit increases tied to inflation and income to the trust funds tied to wage growth, the economic well-being of social security has been completely determined by the relative increases in prices and wages. Under a new provision, if trust funds are critically low, and if inflation exceeds wage growth, --as has occurred in recent years--the annual COLA will be based on the lower of the increase in wages or prices. When reserves rebuild again, "catch-up" payments would be made to make up for any years in which the COLA was based on wage growth.

All in all, I think the "Social Security Act Amendments of 1983" represent a good, sound piece of legislation that goes a long way toward shoring up the system both in the short- and the long-range. The short-range deficit (1983-1989) will be reduced by $160-$170 billion; the long-range deficit projected by the social security actuaries will be eliminated.

This is a necessary first step toward restoring the confidence of the elderly and young people alike in the long-term viability of social security.

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