Kay Luther

BOB DOLE
KANSAS

United States Senate
OFFICE OF THE MAJORITY LEADER
WASHINGTON, DC 20510

February 3, 1986

TO: SENATOR DOLE

FROM: GEORGE PIELER

SUBJECT: TALK TO MORTGAGE BANKERS ASSOCIATION
Tuesday, February 4, 1986 - Capital Hill Club

Attached are current materials on budget and tax for your talk to the MBA Legislative Conference Breakfast.

MBA has strong views on a number of tax and budget issues that will come up this year, the most important of which are as follows:

1. User Fees on Subsidized Mortgage Credit

The President's budget is likely to include proposals, similar to those made last year, imposing fees on Federal mortgage credit programs (for example, loan origination fees). The MBA is concerned about fees on loans by FHA, VA, Ginnie Mae, Fannie Mae, or the Federal Home Loan Mortgage Corporation.

MBA's argument is that fees should not be allowed beyond what is needed to cover the cost of administering the program. The Administration has argued, and no doubt will continue to argue, that Federal mortgage credit programs constitute a subsidy and that it is appropriate to charge a fee for the benefit conferred by that subsidy.

As examples, last year the President proposed increasing the mortgage insurance premium on FHA loans from 3.8% to 5%, and on VA loans from 1% to 3.8%.

2. <u>VA loan guaranty Authority</u>

The authority of VA to guarantee loans under the home loan guaranty program is set at $11.47 billion for FY 86. MBA claims that this is inadequate, and that $17-18 billion will be "needed" this year. The $11.47 billion figure takes into account the effect of the March 1 Gramm-Rudman sequester (4.3% cut).

3. <u>Tax reform</u>

MBA has fairly weak and ill-defined positions on most real estate tax reform issues, but they do oppose the application of at-risk rules to real estate. Generally they oppose limits on interest deductions (including interest from limited partnerships invested in real estate) and want "consistent" depreciation schedules.

4. MBA Supports the Chafee Bill

S. 1959, which would reform the tax treatment of mortgage-backed securities. Finance held a hearing last Friday. The basic point is to clarify when taxable income should be passed through to investors, and when taxed to the entity that actually issues mortgage obligations.

Attachment

February 3, 1986

THE ECONOMY IN 1986

- No one can really predict the course of the economy in 1986, although of course we have to take a stab at it to guide our budget decisions. But it is increasingly clear that the economy began picking up late last year. Leading indicators rose 0.9% in December, the eighth month in a row. Unemployment is down to 6.9%, the lowest since 1979.

- There are forces at work that improve the prospects for strong growth this year. One of these is the drop in oil prices, which acts like a tax cut for energy users and helps moderate inflationary pressures that might build as a result of the dollar's decline. Coupled with the monetary stimulus the Federal Reserve provided in the last six months of 1986, and the prospect for improvement in our balance of trade later in the year (as the effects of the dollar decline are felt), this means we have a good chance for healthy growth in 1986.

- Clearly the number one threat to maintaining a healthy economy remains the U.S. budget deficit. If it's not reduced sharply this year, we won't meet the commitment we made to our trading partners to secure their agreement to ease the dollar down. What's more, we would put an unconscionable burden on the Federal Reserve to keep the recovery going by pumping more money out in order to keep interest rates down. That's a sure recipe for inflation.

- We've created 9 million jobs with a near record economic recovery. We've got inflation down to the lowest levels in two decades. Let's not throw it all a way by punting on the deficit issue. The fact is that <u>all</u> the economic pundits we've been hearing in recent years have been wrong: the economy is more resilient than many believed, but not so strong as to be able to sustain huge deficits this late in the recovery. It's time for everyone to "give" a little in the interest of a deficit-reduction plan that will steer us safely through the potentially treacherous waters ahead.

Gramm-Rudman, the Dollar, and Inflation

- Gramm-Rudman should help us meet the commitment we made last September to our trading partners: to reduce the deficit as part of our effort to moderate the value of other dollar.

- By the same token, the risk of inflation should be reduced if we bring down the deficit under Gramm-Rudman, because the pressure to pump up the money supply to keep interest rates down will ease considerably.

Gramm-Rudman: Challenge to the Established Fiscal Order

- The first actions in response to the new Gramm-Rudman deficit control reform will be taken early in 1986. For those of you who missed it, late last year the Congress imposed a new fiscal straightjacket on itself. The new law sets firm deficit targets for each of the new five years, and mandates automatic across the board spending cuts if the deficit exceeds the target. The first round of automatic cuts under the proposal will take effect March 1 unless Congress comes up with a better way to meet the target.

- In addition, President Reagan's budget for fiscal year 1987 is due to Congress by February 5. So we will have reconsideration of the 1986 budget proceeding simultaneously with our first shot at the 1987 budget.

That is a tall order, but is one we ought to be able to fill. Difficult as it seems, we should remember that the Gramm-Rudman law contains new procedures designed to make it easier to meet the deficit targets. We explicitly bring loan programs and other 'off-budget' items into the budget process; set a point of order against legislation from committees that have not met their budget savings allocation; and rule out of order legislation inconsistent with the deficit targets.

Possible Problems. We know there may be a rocky road ahead in implementing Gramm-Rudman. Congressmen Synar and others have filed suit claiming it is unconstitutional, and the Reagan Administration has some problems as well with the role of the Congress' General Accounting Office in mediating the deficit forecasts. The courts will have to guide us on all that. Even more important, what Congress can legislate, Congress can back out of. That's why we need a constitutional mandate for budgetary restraint, as well as a statutory one.

- o So Gramm-Rudman hasn't made our options any easier: but if it works as planned, it will force us--and the President--to make some decisions and choose among the various deficit-reduction options. That means everyone's cherished spending programs will be put to the test of fiscal responsibility.

Spending the Key. Finally, let me emphasize that Gramm-Rudman is a device for reducing Federal spending. It is not a tax increase plan, or a subterfuge for one. If we fail on the spending front, we can look at other options. But the sooner we entertain any revenue options, you can bet the pressure for spending cuts will drop fast.

The Deficit and the Average American

- o Unless we follow a deficit reduction path like that mandated under Gramm-Rudman, American families will face either higher interest rates or higher inflation: not to mention the risk of a disastrous new recession throwing millions of breadwinners out of work. That is what the Gramm-Rudman-Hollings initiative is all about.

- o Most economists believe that enactment of deficit reduction measures that eliminate the deficit by the end of the decade will produce a drop of at least 1 percent in interest rates over the short run and 2 to 3 percentage points over the long term: relative to what they otherwise would be.

  -- With a 2% drop in interest rates, the monthly payment on a median priced home ($80,000) would go down by about $100 a month.

  -- Conversely, if we don't reduce the deficit to keep rates as low as they are now, homeowners could face that large an increase--or more-- in monthly payments.

  -- A 2% drop in interest rates would mean an additional $4,000 in income for the average wheat farmer with a 1,000 acre operation.

  -- In 1985, the Federal Government will overspend close to $1,000 for every man, woman, and child in America.

  -- This $1,000 per head of additional federal debt will be one more burden for our children to repay in higher taxes or higher inflation in the future.

Interest on the Debt

The massive increase in debt has itself created one of the largest and fastest growing components of Federal spending--interest on the debt. Constant deficits have put fiscal policy on an endless treadmill of paying for the irresponsibility of previous decades:

- In 1965, interest on the national debt cost $9 billion and consumed 1.4% of GNP. By 1980, annual interest costs rose to $52 billion--2% of GNP. But the worst was yet to come.

- In 1985, interest on the national debt cost taxpayers $130 billion--almost three times the level of five years ago. this represents 3.8% of GNP, 13.5% of the entire 1985 budget, and a 1,450% increase in costs over 1965.

- $130 billion is equal to the sum total of all Federal spending from 1789--the founding of the republic--to 1936. It also equals total Federal outlays in 1966, the entire defense budget in 1980, and twice the level of medicare funding today.

But if we can adhere to the deficit-reduction goals we've set for ourselves, I am very, very optimistic about the course of the economy. I think we take too much for granted what we have achieved so far: strong growth without inflation. We can keep that going if we reduce the deficit substantially. The way is open to economic performance unprecedented in the postwar period if we have the will to find it.

Tax Reform Talking Points

- The President's tax plan and the House bill are similar in concept--they both shift more of the tax burden to corporations and reduce the tax burden on individuals. But the bills are very different in how they make the change.

- Both substantially reduce tax rates for individuals (the President to a maximum of 35%; Ways and Means to 38%) and for corporations (President 33%; Ways and Means 36%). But the Ways and Means rates take effect at much lower income levels: the 35% rate clicks in at $43,000 for married couples, as opposed to $70,000 under the Reagan plan.

- Neither plan gets an A+ for the major objectives of tax reform--simplification and fairness, but the President's plan repealed many more of the overly complicated provisions of the tax code than the Ways and Means Committee effort. The House bill just modifies, but leaves in place, many complex tax rules.

- The House bill falls far short of the President's on fairness grounds. Fringe benefits and itemized deductions are major causes of differing tax liabilities, and unlike the President's proposal, the House retained the State and local tax deduction, did less to limit interest-paid deductions, and did nothing on fringe benefits. This means that taxpayers with equal incomes can still have substantially different tax liabilities.

- The House retained many of the politically popular big-ticket items like tax-free fringe benefits and the State and local tax deduction. Unless we want to tackle those, the Senate will have limited flexibility in trying to enhance investment and savings incentives.

- I have personally long favored income tax reform and, as Chairman of the Senate Finance Committee, led the fight over a number of years to plug unjustified tax loopholes.

- Nevertheless, I know that many of my Senate colleagues have no enthusiasm for the President's version of tax reform and even less for the House bill, which they view as even more likely to have harmful economic effects. In the Senate, with its more open procedures, it is easier for a determined minority to block or slow down a bill they oppose.

- It is possible that the Senate might be able to fashion its version of a tax reform bill by June, but only with intensive effort by the President to push the bill and reshape it along the lines he favors.

Speak

February 3
Mon. eve.

in Boston that eve.

1125 Fifteenth Street, N.W.
Washington, D.C. 20005

Mortgage Bankers Association of America

Burton C. Wood
Senior Staff Vice President
and Legislative Counsel

202-861-6507

Joyce
(also copy to Mike P.)

Nowlin Mortgage Co.
Ft. Worth,

Tues. Feb 4
7:30 Bkfst
Cap. Hill Club
8:40 SPEAK
could speak at 8:35 8:40

at Hyatt

November 21, 1985

OK

advise if they are flexible

Walt Nowlin - in Ft. Worth.

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The Honorable Robert Dole
United States Senate
Washington, D. C. 20510

Attention Ms. Betty Meyer

Dear Senator Dole:

The Mortgage Bankers Association of America has scheduled its annual Washington Legislative Conference for February 3, 4, and 5, 1986. On behalf of MBA's Legislative Committee, I would like to extend an invitation to you to attend and speak at a dinner to be held on February 3, 1986 at the Hyatt Regency on Capitol Hill.

The Mortgage Bankers Association of America is a nationwide organization devoted exclusively to the field of mortgage and real estate finance. MBA's membership comprises mortgage orginators, mortgage investors, and a variety of industry-related firms. Mortgage banking firms, which make up the largest portion of the total membership, engage directly in originating, financing, selling, and servicing real estate investment portfolios. The audience would total approximately 150 of the leading mortgage bankers from across the country.

I realize your schedule is a busy one, but I am hopeful that you can be with us for the evening to share your insights and observations on the major issues that Congress will be considering during the coming year.

For the convenience of your staff in working out any details, my office phone number is 861-6507.

Burt or Sharon Canavan

Sincerely,

Burton C. Wood

BCW:amk

1/15 Sharon advised only time they have is Mon. eve. dinner

12/10 - Interim ltr They will try Sen. again -

Hon. ? $2,000.00