REMARKS OF SENATOR DOLE

ASSOCIATION OF PRIVATE PENSION AND WELFARE PLANS

MAY 25, 1983

I. INTRODUCTION--CHOICES TO BE MADE REGARDING RETIREMENT SAVINGS

I AM PLEASED TO HAVE THIS OPPORTUNITY TO SHARE MY THOUGHTS WITH YOU ON THE RECENT AND FUTURE LEGISLATIVE INITIATIVES REGARDING RETIREMENT AND WELFARE PLANS.

THE MAIN ISSUE, I THINK, AND THE GENERAL THEME OF MY DISCUSSION HERE WITH YOU TODAY, IS BASICALLY THIS: TO WHAT EXTENT SHOULD THE FEDERAL GOVERNMENT--AS OPPOSED TO INDIVIDUAL INITIATIVE--MANDATE OR ENCOURAGE RETIREMENT OR WELFARE BENEFIT COVERAGE?

AN EMPLOYER'S OR AN INDIVIDUAL'S DECISION TO EFFECT RETIREMENT SAVINGS DOES NOT TAKE PLACE IN A VACUUM. CHOICES MUST BE MADE. AN INDIVIDUAL WHO DECIDES TO PUT $2,000 IN AN IRA FOREGOES CURRENT CONSUMPTION. IN ADDITION, DIFFERENT ECONOMIC EFFECTS RESULT FROM THE ENCOURAGEMENT OF RETIREMENT SAVINGS. FOR EXAMPLE, BECAUSE ERISA LIMITS THE TYPE OF INVESTMENTS THAT A PRUDENT RETIREMENT ACCOUNT TRUSTEE MAY MAKE, CAPITAL SET ASIDE FOR RETIREMENT PLANS IS GENERALLY PROHIBITED FROM USE IN RISKY VENTURES TO INSURE THAT THE MONEY WILL BE AVAILABLE FOR RETIREMENT PURPOSES.

IN MAKING DECISIONS CONCERNING THE EFFECT OF OUR REVENUE MEASURES ON RETIREMENT SAVINGS, IT IS ALSO NECESSARY FOR CONGRESS

TO CONSIDER THESE MEASURES IN THE CONTEXT OF OTHER SAVINGS AND SPENDING MEASURES THAT WE WISH TO ENCOURAGE. TAX INCENTIVES USED TO ENCOURAGE RETIREMENT SAVINGS ARE NOT FREE. TAX EXPENDITURES USED TO ENCOURAGE RETIREMENT SAVINGS MAY BE JUSTIFIED IN LIGHT OF CERTAIN GOALS WE ARE TRYING TO ACHIEVE, BUT AT A TIME WHEN ALL SECTORS OF GOVERNMENT ARE REQUESTING A GREATER SHARE OF OUR LIMITED RESOURCES, WE MUST USE OUR LIMITED TAX DOLLARS TO FIND THE MOST EFFICIENT WAY TO ENCOURAGE RETIREMENT SAVINGS FOR ALL WORKERS.

WE MUST CONTINUALLY EVALUATE WHICH SEGMENTS OF OUR WORKFORCE BENEFIT FROM THE FEDERAL GOVERNMENT FISCAL 1984 TAX EXPENDITURES IN THE RANGE OF $60 BILLION FOR RETIREMENT INCENTIVES, NOT COUNTING SOCIAL SECURITY. THE TAX EXPENDITURE FOR EMPLOYER-PROVIDED PLANS ALONE IS EXPECTED TO REACH $109 BILLION IN FISCAL 1988.

II. DEVELOPMENT OF THE CURRENT RETIREMENT SYSTEM

OVER THE PAST FORTY YEARS, THERE HAS BEEN A DRAMATIC SHIFT IN SOCIETY'S ATTITUDES REGARDING THE INDIVIDUAL'S RESPONSIBILITY IN PLANNING FOR HIS RETIREMENT. PRIOR TO THE ENACTMENT OF SOCIAL SECURITY LEGISLATION IN THE 1930'S, IT WAS ASSUMED THAT AN INDIVIDUAL'S FAMILY OR THE INDIVIDUAL HIMSELF WOULD PROVIDE FOR THE TIME WHEN HE COULD NO LONGER EARN A LIVING.

THIS ATTITUDE CHANGED OVER THE YEARS. SOCIAL SECURITY LEGISLATION RECOGNIZED THE GOVERNMENT'S ROLE IN PROVIDING MINIMUM RETIREMENT SECURITY FOR INDIVIDUALS COVERED BY THE SYSTEM. LATER, CORPORATE EMPLOYERS BEGAN TO FEEL THAT THEY OWED SOMETHING MORE SUBSTANTIVE TO THEIR EMPLOYERS UPON RETIRMENT THAN THE PROVERBIAL GOLD WATCH, AND PRIVATE RETIREMENT PLANS BEGAN TO BECOME AN IMPORTANT FACTOR IN OUR COUNTRY'S RETIREMENT PLANNING. A MORE RECENT TREND HAS BEEN THE USE OF THE NATION'S TAX SYSTEM TO ENCOURAGE, THROUGH THE INCENTIVES OF TAX DEDUCTIONS OR CREDITS, THIS "PRIVATE" FUNDING OF RETIREMENT PLANS BY EMPLOYERS OR BY INDIVIDUALS.

TODAY WE HAVE WHAT I MIGHT CALL A THREE-PRONGED SYSTEM OF RETIREMENT SAVINGS--FIRST, THE SOCIAL SECURITY SYSTEM; SECOND, DIRECTED SAVINGS FOR RETIREMENT ENCOURAGED BY THE NATION'S TAX LAWS (THAT IS, PRIVATE PENSIONS AND IRA'S); AND THIRD, INDIVIDUAL SAVINGS.

III. SOCIAL SECURITY--FIRST PRONG OF THE RETIREMENT SYSTEM

SOCIAL SECURITY INVOLVES A DELIBERATE DECISION BY GOVERNMENT TO BECOME DIRECTLY INVOLVED IN A CITIZEN'S RETIREMENT SAVINGS. THE AMOUNT OF PAYROLL CONTRIBUTION, AND THE AMOUNT OF A CITIZEN'S EVENTUAL SOCIAL SECURITY BENEFIT, IS DETERMINED BY THE GOVERNMENT.

SOCIAL SECURITY INITIALLY WAS CREATED TO PROVIDE A MINIMUM BENEFIT FOR PERSONS NO LONGER ABLE TO WORK. NOW THAT THE SYSTEM HAS BEEN EXPANDED TO DEAL WITH A VARIETY OF SOCIAL CONCERNS IN ADDITION TO RETIREMENT, THE COST OF THE SYSTEM HAS INCREASED AT AN ENORMOUS RATE, THREATENING TO BANKRUPT THE SYSTEM.

IN RESPONSE TO THIS PROBLEM, THE NATIONAL COMMISSION ON SOCIAL SECURITY, ON WHICH I WAS PRIVILEGED TO SERVE, SUGGESTED A NUMBER OF MEASURES DESIGNED BOTH TO REFLECT THE CHANGES IN THE WAY AN INDIVIDAL IN TODAY'S SOCIETY IS COMPENSATED FOR HIS WORK AND TO DEAL WITH THE INCREASED COST OF THE SOCIAL SECURITY SYSTEM. THESE RECOMMENDATIONS BECAME THE FOUNDATION FOR THE LEGISLATION ENACTED THIS YEAR WHICH SHOULD ASSURE THE CONTINUATION OF THE SOCIAL SECURITY PROGRAM WELL INTO THE NEXT CENTURY.

AMONG THE PROVISIONS AFFECTING RETIREMENT BENEFITS TO WHICH CONGRESS AGREED WAS A LIMITED EXPANSION OF THE SOCIAL SECURITY WAGE BASE WHICH CONGRESS EXPANDED FURTHER TO INCLUDE OTHER TYPES OF INCOME WHICH HISTORICALLY HAVE NOT BEEN SUBJECT TO THE SOCIAL SECURITY TAX.

CONGRESS RECOGNIZED THAT FOR PURPOSES OF SOCIAL SECURITY, EMPLOYEES WHO WERE ALLOWED TO CHOOSE TO DEFER COMPENSATION SHOULD BE TREATED IN A MANNER SIMILAR TO CURRENT WAGE EARNERS. THE SOCIAL SECURITY AMENDMENTS OF 1983 MAKE IT CLEAR THAT WAGES

DEFERRED UNDER NONQUALIFIED DEFERRED COMPENSATION PLANS, TAX-SHELTERED ANNUITIES, AND "CASH OR DEFERRED PLANS" ARE "WAGES" TAXABLE UNDER SOCIAL SECURITY.

THUS, WE HAVE BROADENED COVERAGE UNDER THE FIRST PRONG OF OUR THREE-PRONGED RETIREMENT SYSTEM, BUT AT THE SAME TIME I WISH TO EMPHASIZE THAT I DO NOT SEE SOCIAL SECURITY IN ITSELF PROVIDING COMPLETE RETIREMENT SECURITY FOR MOST AMERICAN WORKERS.

IV. TAX INCENTIVES FOR RETIREMENT

A. EMPLOYER-PROVIDED PENSIONS

THE SECOND PART OF THE THREE-PRONGED RETIREMENT SYSTEM INVOLVES THE INDIRECT ROLE THAT THE GOVERNMENT PLAYS IN ENCOURAGING SAVINGS FOR PRIVATE PENSIONS. OF COURSE, THE TAX SYSTEM REWARDS "TAX QUALIFIED PLANS" BY ALLOWING EMPLOYERS TO DEDUCT A SET AMOUNT FOR THEIR OWN AND THEIR EMPLOYEES' RETIREMENT, AS WELL AS TO ACCUMULATE THE INTEREST EARNED ON RETIREMENT INCOME TAX FREE. THESE PRIVILEGES DO NOT COME FREE--AS ANY INDIVIDUAL DEALING WITH THE MORASS OF REQUIREMENTS UNDER ERISA WILL TELL YOU.

THE TAX EQUITY AND FISCAL RESPONSIBILITY ACT WAS AN ATTEMPT BY CONGRESS TO INSURE THAT AMOUNTS GIVEN SPECIAL TAX TREATMENT AS

RETIREMENT FUNDS ARE ACTUALLY USED TO PROVIDE RETIREMENT INCOME RATHER THAN TAX SHELTERS FOR THE HIGHLY COMPENSATED.

THE SENATE BILL DEALT WITH THIS PROBLEM BY LIMITING THE MAXIMUM ANNUAL CONTRIBUTIONS TO AND BENEFITS FROM TAX-QUALIFIED RETIREMENT PLANS. IN ADDITION, CONGRESS ADDED MEASURES, SUPPORTED BY THE HOUSE CONFEREES, DESIGNED TO INSURE THAT AN EMPLOYER WHO TAKE ADVANTAGE OF A TAX QUALIFIED RETIREMENT PLAN DESIGNS A PLAN THAT BENEFITS ALL EMPLOYEES--NOT JUST THE HIGHLY COMPENSATED.

THESE SPECIAL RULES FOR "TOP HEAVY" PLANS ARE COMPLICATED, TO SAY THE LEAST. THE SENATE CONFEREES RECOGNIZED THIS AND REQUIRED THAT THE EFFECTIVE DATE BE DELAYED FOR A YEAR. SENATOR CHAFEE HAS HELD HEARINGS ON THESE RULES ALREADY, AND THE STAFF IS ANALYZING POSSIBLE TECHNICAL IMPROVEMENTS.

B. <u>IRA's</u>

ANOTHER IMPORTANT PART OF THE SECOND PRONG OF RETIREMENT SAVINGS--INDIVIDUAL RETIREMENT ACCOUNTS OR IRA'S--ARE A RELATIVELY NEW FEATURE OF OUR TAX LAWS. IRA'S WERE INTRODUCED IN 1974 AS A MEANS OF ALLOWING INDIVIDUALS WHO WERE NOT PARTICIPANTS IN A TAX-QUALIFIED RETIREMENT PLAN TO SET ASIDE MONEY FOR THEIR RETIREMENT AND RECEIVE A DEDUCTION FROM INCOME FOR THE MONEY SET ASIDE. THE ECONOMIC RECOVERY TAX ACT OF 1981 ("ERTA") EXPANDED

THE ROLE OF INDIVIDUAL RETIREMENT ACCOUNTS BY ALLOWING ALL PERSONS WITH EARNED INCOME (REGARDLESS OF WHETHER THEY WERE COVERED BY A RETIREMENT PLAN) TO CONTRIBUTE TO AN IRA, AND BY INCREASING THE MAXIMUM ANNUAL CONTRIBUTION TO AN IRA.

THE 1981 CHANGES TO THE IRA SYSTEM CHANGED THE FOCUS OF AN IRA. AN IRA BECAME MORE THAN AN INADEQUATE SUBSTITUTE FOR THOSE EMPLOYEES WHO WERE NOT COVERED BY A RETIREMENT PLAN--IT BECAME A MEANS OF SUPPLEMENTING THE RETIREMENT INCOME PROVIDED TO AN EMPLOYEE BY HIS EMPLOYER AND BY SOCIAL SECURITY. AN EMPLOYEE GENERALLY HAS LITTLE CHOICE AS TO THE AMOUNT OF PRE-TAX DOLLARS SPENT ON HIS RETIREMENT PLAN, BUT THE IRA NOW PROVIDES HIM WITH AN ADDITIONAL CHOICE IN THIS AREA.

GIVEN THE EXPANDED ROLE OF IRA'S, IT SHOULD COME AS NO SURPRISE TO YOU THAT THERE HAS BEEN A DRAMATIC GROWTH IN FUNDS INVESTED IN IRA'S OVER THE PAST TWO YEARS.

THE WIDESPREAD USE OF IRA'S HAS RESULTED IN A POTENTIAL REVENUE LOSS MUCH GREATER THAN ANTICIPATED. PRELIMINARY STUDIES BY THE JOINT TAX COMMITTEE ESTIMATE THAT THE CHANGES RESULTING FROM THE EXTENSION OF IRA'S TO PARTICIPANTS IN QUALIFIED PLANS RESULTED IN A REVENUE LOSS OF $~~1~~3 TO $~~2~~4 BILLION IN 1982. SOME COMMENTATORS ARGUE THAT THIS ESTIMATE IS TOO LOW. THIS ESTIMATE, HOWEVER, MAY NOT REFLECT FUTURE TRENDS BECAUSE TAXPAYER'S INITIAL ENTHUSIASM FOR IRA'S MAY NOT CONTINUE INTO FUTURE YEARS. I WILL

DISCUSS LATER SOME POSSIBLE STEPS THAT COULD BE TAKEN IF THIS REVENUE LOSS IS DETERMINED TO BE TOO LARGE.

V. INDIVIDUAL SAVINGS--THE THIRD PRONG

THE LIMITS PLACED ON THE AMOUNT OF RETIREMENT INCOME THAT RECEIVES SPECIAL TAX TREATMENT REFLECTS CONGRESS' FEELING--AND MY OWN--THAT NOT ALL RETIREMENT SAVINGS NEED TO BE DIRECTLY OR INDIRECTLY SUBSIDIZED BY THE GOVERNMENT.

IF AN INDIVIDUAL WISHES TO SET A LARGE AMOUNT OF MONEY ASIDE TO IMPROVE HIS STANDARD OF LIVING UPON RETIREMENT, HE MAY USE THE THIRD SEGMENT OF OUR THREE-PRONGED SYSTEM OF RETIREMENT PLANNING--INDIVIDUAL SAVINGS WITHOUT PREFERENTIAL TAX TREATMENT.

VI. FUTURE CHOICES REGARDING RETIREMENT SAVINGS

IDEALLY, THIS THREE-PRONGED SYSTEM OF RETIREMENT SAVINGS SHOULD PROVIDE THE PERFECT BLEND OF MANDATORY REQUIREMENTS AND TAX INCENTIVES TO ALLOW INDIVIDUALS BOTH A COMFORTABLE RETIREMENT AND THE FLEXIBILITY AS TO HOW AND WHEN THEY WILL EFFECT RETIREMENT SAVINGS. THIS SYSTEM SHOULD PROVIDE LOWER PAID WORKERS WITH AN ADEQUATE RETIREMENT INCOME BECAUSE OF SOCIAL SECURITY AND THE REQUIREMENT THAT EMPLOYERS PROVIDE PENSIONS FOR EMPLOYEES IF THEY WISH TO OBTAIN TAX-QUALIFIED PENSIONS FOR THEMSELVES.

BUT ONE THING I CAN PREDICT WITH LITTLE HESITATION IS THAT THE SYSTEM IS NOT QUITE PERFECT. HOWEVER, WE ARE ATTEMPTING TO DISCOVER HOW IT CAN BE IMPROVED.

A. S. 19

AT PRESENT, FOR EXAMPLE, THE REQUIREMENTS FOR A TAX-QUALIFIED PLAN DISCRIMINATE AGAINST CERTAIN CLASSES OF SOCIETY. THE REQUIREMENTS FAIL TO RECOGNIZE ADEQUATELY THAT A FAMILY AS WELL AS AN INDIVIDUAL WAGE EARNER MAY DEPEND ON RETIREMENT SAVINGS. S. 19, WHICH I INTRODUCED, PROVIDES THAT IF A PLAN ALLOWS RETIREMENT BENEFITS TO BE RECEIVED IN THE FORM OF A JOINT AND SURVIVOR ANNUITY, THE WRITTEN CONSENT OF A NONEMPLOYEE SPOUSE WOULD BE REQUIRED TO ELECT NOT TO HAVE JOINT AND SURVIVOR ANNUITY COVERAGE. S. 19 WILL ALSO CLARIFY FEDERAL LAW TO ASSURE THAT ACCRUED PENSION BENEFITS MAY BE SUBJECT TO A STATE LAW PROPERTY SETTLEMENT IN THE EVENT OF DIVORCE OR SEPARATION, AND WOULD PROTECT THE PENSION BENEFITS OF A SURVIVING SPOUSE WHERE PAYMENT OF JOINT AND SURVIVOR BENEFITS HAVE BEGUN PRIOR TO DIVORCE.

S. 19 ALSO ADDRESSES OTHER POTENTIAL PROBLEMS IN THE CURRENT RETIREMENT SYSTEM. FOR EXAMPLE, THE LAW NOW PROVIDES THAT EMPLOYEES UNDER AGE 25 NEED NOT BE INCLUDED AS PARTICIPANTS IN A TAX-QUALIFIED RETIREMENT PLAN. THIS REQUIREMENT MAY DISCRIMINATE AGAINST INDIVIDUALS--PARTICULARLY WOMEN--WHO GENERALLY ENTER THE WORKFORCE AT AN EARLY AGE. I HAVE PROPOSED IN S. 19 THAT THIS

MINIMUM AGE BE LOWERED TO 21. S. 19 ALSO PERMITS AN EMPLOYEE UP TO A ONE YEAR LEAVE OF ABSENCE DUE TO THE BIRTH OF A CHILD WITHOUT LOSING CREDIT FOR PRIOR SERVICE WITH THE EMPLOYER. THIS MAY IMPROVE THE RETIREMENT BENEFITS OF INDIVIDUALS WHO LEAVE THEIR JOBS TEMPORARILY TO HAVE OR CARE FOR A CHILD.

I MIGHT ADD THAT WE HAVE SCHEDULED A FULL COMMITTEE HEARING ON S. 19 AND ON S. 888 (THE ECONOMIC EQUITY ACT) ON JUNE 20TH AND 21ST.

B. CBO STUDY

WE WILL CONTINUE TO STUDY CAREFULLY THE BALANCE BETWEEN THE GOVERNMENT MANDATES, TAX INCENTIVES, AND PRIVATE INITIATIVE THAT ENCOMPASS THE U.S. PENSION SYSTEM. I HAVE REQUESTED THE CONGRESSIONAL BUDGET OFFICE TO EXAMINE HOW THE CURRENT MIX OF TAX INCENTIVES FOR PENSIONS AND RETIREMENT SAVINGS PROVIDES AN ADEQUATE RETIREMENT INCOME FOR AMERICAN WORKERS AND FINANCES PRODUCTIVE INVESTMENTS.

ONE ISSUE INVOLVES QUESTIONS OF INCENTIVES IN ADDITION TO THOSE OF S. 19 TO ENCOURAGE PENSION PROTECTION FOR THE FAMILY IN ADDITION TO THE WAGE-EARNER. FOR EXAMPLE, CAN CASH OR DEFERRED 401(K) PLANS BE USED FOR THIS PURPOSE, OR SHOULD SPOUSAL IRAS BE INCREASED?

OTHER ISSUES ARE RAISED WITH RESPECT TO IRAS. DO IRAS ALONE PROVIDE ENOUGH FLEXIBILITY FOR AN INDIVIDUAL'S RETIREMENT PLANNING? IS A $2,000 PER YEAR CONTRIBUTION SUFFICIENT? WHAT ABOUT PERSONS WHO ARE NOT COVERED BY A PRIVATE RETIREMENT PLAN? ARE HIGHER IRA CONTRIBUTIONS (AND THE RESULTING TAX LOSS) JUSTIFIED IN LIGHT OF OTHER EXPENDITURES? SHOULD THERE BE INCOME LIMITS TO ALTER THE DISTRIBUTION OF IRA USE AMONG DIFFERENT INCOME CLASSES? SHOULD THE PENALTY STRUCTURE BE REVISED TO PROVIDE GREATER INCENTIVES TO KEEP SAVINGS INTACT UNTIL RETIREMENT?

C. INTEGRATION

ANOTHER ISSUE THAT SOME COMMENTATORS BELIEVE DESERVES ADDITIONAL CONSIDERATION IS THE EFFECT OF "INTEGRATION" OF PRIVATE RETIREMENT PLANS WITH SOCIAL SECURITY. INTEGRATION, IN EFFECT, ALLOWS AN EMPLOYEE TO TAKE INTO ACCOUNT PART OF THE SOCIAL SECURITY BENEFITS PAYABLE TO EMPLOYEES WHEN CALCULATING RETIREMENT BENEFITS.

ALTHOUGH THERE ARE LIMITS TO THE EXTENT THAT INTEGRATION MAY BE USED IN PRIVATE RETIREMENT PLANS, THE NET EFFECT OF INTEGRATION IS TO ALLOW EMPLOYERS TO USE THE SOCIAL SECURITY CONTRIBUTIONS THAT THEY MAKE FOR THEIR EMPLOYEES AS PART OF THEIR EMPLOYEES' STATED RETIREMENT PACKAGE. FOR EXAMPLE, THIS CONCEPT MEANS THAT IN SOME CASES A RETIREMENT PLAN MAY PROMISE AN

EMPLOYEE A CONTRIBUTION OF 10 PERCENT OF EARNINGS, BUT IN EFFECT PART OF THAT CONTRIBUTION IS MADE BY THE SOCIAL SECURITY TAX THAT THE EMPLOYER WOULD HAVE TO PAY IN ANY CASE.

BY ALLOWING THE CONCEPT OF INTEGRATION, CONGRESS RECOGNIZED THAT EMPLOYERS WHO OFFER RETIREMENT PLANS SHOULD BE GIVEN SOME CREDIT FOR THEIR CONTRIBUTIONS TO SOCIAL SECURITY. IN THIS CASE, THEN, THE SOCIAL SECURITY PRONG AND THE TAX INCENTIVE PRONG OF OUR RETIREMENT SYSTEM ARE COMBINED. TEFRA IMPOSED SOME NEW LIMITS ON THE USE OF INTEGRATION. HOWEVER, FURTHER STUDY OF THE EFFECT OF SOCIAL SECURITY INTEGRATION ON PRIVATE RETIREMENT PLANS MAY BE REASONABLE AS PART OF AN OVERALL REVIEW OF RETIREMENT INCENTIVES.

D. FLEXIBILITY

A MORE GENERAL QUESTION PROMPTED IN PART BY THE RECENT CHANGES REQUIRED FOR TAX QUALIFIED RETIREMENT PLANS IS HOW TO ENCOURAGE EMPLOYERS TO ADOPT PLANS THAT ARE FLEXIBLE ENOUGH TO MEET THEIR EMPLOYEES' NEEDS AND AT THE SAME TIME INSURE THAT RETIREMENT BENEFITS ARE PROVIDED FOR LOWER-PAID EMPLOYEES?

CONCLUSION

THERE ARE NO EASY ANSWERS TO THE QUESTIONS I RAISED THIS MORNING, AND I DO NOT PROPOSE ANY HERE. I REALIZE THAT CONGRESS HAS BEEN CRITICIZED FOR NOT CAREFULLY CONSIDERING SOME OF THESE PROBLEMS AND SOME OF THE OBJECTIONS OF PENSION PROFESSIONALS DURING THE PASSAGE OF TEFRA. WE HAVE TRIED TO MEET THIS CRITICISM WITH SENATOR CHAFEE'S HEARINGS ON THE PROBLEMS RAISED BY TEFRA AND WITH THE DELAYED EFFECTIVE DATE OF THE TOP-HEAVY PROVISIONS OF TEFRA. I HOPE THAT YOU WILL WORK WITH US AS WE ATTEMPT TO FIND THE MOST EFFICIENT AND EQUITABLE MANNER TO PROVIDE THE RETIREMENT AND WELFARE BENEFITS THAT ARE SO IMPORTANT TO ALL AMERICANS.

OUTLINE OF REMARKS

ASSOCIATION OF PRIVATE PENSION AND WELFARE PLANS

May 25, 1983--8:00 a.m.--L'Enfant Plaza Hotel

I. The President and the Congress

A. President Reagan has made clear that he and the 98th Congress need to work together, but at the same time he is trying to set firm limits on possible areas of compromise. We have had constructive action on social security but the deficit, unemployment, and the shifting patterns of industry ad job creation in our economy all need to be dealt with. As we proceed we should not compromise away the gains won towards restraining the growth of spending, controlling the tax burden, and beating back inflation. The American people still overwhelmingly support those goals.

B. The President still sets the agenda. On taxes, spending, deficits, employment, and trade the President proposes, and Congress must dispose. Those of us who have ideas of our own will work with the White House to get things done--but leadership still must come from the President. That is why we are unlikely to see any major departure from the principles of government Ronald Reagan has espoused in his first two years in office.

C. The fact remains that there is no coherent alternative to Republican leadership. The people still recognize that our economic problems were a long time in the making, and that the cure will take time too. According to CBS/New York Times voter exit polls in the last election, voters by a 5 to 4 margin blamed our economic problems on past Democratic policies rather than on President Reagan.

II. 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 March the index of leading economic indicators jumped 1.5 percent--the seventh straight such increase, and the 10th increase out of the last 11 months. In addition, industrial output rose 1.1 percent in March and 2.1 percent in April: the highest monthly rise in 8 years. Economists agree we are in a broad based 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 rose less in the

first quarter of 1983 than in any quarter since 1965. Wholesale prices dropped 0.1 percent in April.

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. 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.

4. Housing starts are up; the stock market is up 450+ points over last August. These are tangible evidence of recovery. Consumer confidence is rising; retail sales rose 1.6 percent in March and 1.7 percent in April and auto sales were up 5.2 percent in the first 10 days in May.

B. Unemployment. The January drop in unemployment to 10.4 percent was followed by a further decline to 10.3 percent in March and to 10.2 percent in April. That is major good news, and the decline has not been reversed, 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.

o While the main emphasis must remain on the long-term goals of growth with low inflation, there are steps we can take in the short term to deal with the plight of the unemployed. Many things have already been done:

- A new Federal supplemental unemployment compensation program was passed with the 1982 tax bill, providing additional unemployment benefits to about 2 million workers in 38 States. The House and Senate have agreed to extend this program through September 30.

- The President signed into law the new Job Training Partnership Act, which emphasizes training for permanent employment rather than make-work jobs. New initiatives outlined by the President focus on the long-term unemployed, youth, and on training or relocating displaced workers who lost jobs due to plant closures or force reductions.

- The targeted jobs tax credit, which was extended for 2 years by the 1982 tax bill, gives employers a real incentive to hire the disadvantaged--about 600,000 workers are certified under the program.

- The administration's enterprise zone legislation, just approved by the Finance Committee, can provide us with an experiment in private-sector job creation in depressed areas, through a combination of Federal tax incentives and State and local efforts to target an area for development with regulatory and tax relief, neighborhood participation, and capital and other improvements.

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.

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.

III. The Budget Impasse

A. 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 modification or repeal the third year of the tax cut for the working people. Why run the risk of aborting recovery? 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.

B. When all is said and done, the real debate in the Senate is over the revenue question. While some may prefer a defense increase of 5 percent or 6 percent or 7 percent, there seems to be room to compromise and reach agreement on that issue. Similarly--and unfortunately--it seems to be conceded that we will not make any significant net reduction in domestic spending under this budget resolution. That leaves the choice between accepting for now the deficits that result from these decisions, or agreeing to implement tax increase now that would bring those deficits down somewhat while spending remains at high levels.

C. 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. 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.

D. If we do succeed in getting a budget agreement through conference, we had better be sure it is one that we can implement. Otherwise we will not be doing the financial markets any favor, and we will lose even what credibility we still have on the deficit question.

Even if, for some reason, we should fail to get a workable budget agreement, that does not mean the fight against the deficit is over. The President will use his veto to try to keep spending in line, and his like-minded supporters in Congress are likely to sustain him in many cases. A case can be made, in fact, that hand-to-hand combat over individual programs may be preferable to swallowing whole the House-passed budget, which increases domestic spending with tax increases and has no real, credible impact on the deficit.

IV. Taxes: Third Year and Indexing

A. The President has said time and time again that he will fight to retain the third year of his tax cut and indexing, and many of us will continue to support him, even if a veto is required. Thirty-four Senate Republicans and 146 House Republicans have signed letters to that effect. The reasons are quite simple: these measures are good for the economy, they are fair, and they give long-needed real tax relief to the hard-pressed middle income American.

B. Third year. Why is the third year important? First, most economists agree that the timing of this last stage of President Reagan's individual tax program is excellent in terms of giving the economy a boost on the consumption side as we emerge from recession. This is a sharp contrast with the past, when tax changes to counter recession were too little and too late.

Equally important, the third year is needed in the interest of fairness. Only the third year gives a full measure of tax relief to working people. For taxpayers with incomes $10,000 or less, repeal of the third year means a tax increase averaging 13.9 percent. For those between $20,000 and $30,000 in income it means a 12 percent jump in taxes. 72 percent of the benefit goes to Americans making $50,000 or less.

In dollar terms, repealing the third year would cost a taxpayer at $15,000 income $112 in FY 1984; at $20,000 income, it would cost $203 in 1984; at $30,000 income, taxes would be $410 higher in 1984.

C. Indexing. Indexing is crucial not just because it provides tax relief, but because it insures truth in government: tax changes will have to be voted on openly and directly, rather than having Congress rely on inflation to raise revenues through the deception of bracket creep. Whatever attitude you take on the question of generating new revenues, it makes sense to keep indexing in place.

In addition, indexing is an important symbol of our commitment to fight inflation. Repealing it only generates significant revenues if you assume inflation will persist at fairly high levels. If we de-index, we send a signal that we are not committed to beating inflation--and that means bad news for financial markets, for interest rates, and for consumers and investors alike.

Finally, the tax relief provided by indexing is real and sustained. Indexing means $98 billion in tax relief between 1985 and 1988, assuming modest inflation. $78 billion of that goes to taxpayers earning under $50,000. This group now pays about 66 percent of taxes, but will get 80 percent of the benefit--proving that indexing is a truly progressive tax reform.

A median income family of four would pay $1,000 in additional taxes between 1985 and 1988 if indexing were repealed (assuming they earn $24,000 in 1982). Remember that consumers are homebuyers as well, and their after-tax income is as important as interest rates in determining whether they will buy.

V. Tax Issues of Continuing Concern

A number of issues that have been around for some time may receive attention from the 98th Congress.

1. 6-month holding period. Efforts to reduce the capital gains holding period to 6 months will continue. There is very strong support for this change, because it can give a boost to capital markets at a time when greater savings and investment is vitally important to sustained economic recovery. This change was approved by the House in 1981 and by the Senate on three separate occasions in 1982, so it is time to get it enacted into law.

2. Tuition Tax Credits. Although the Finance Committee fashioned a compromise tuition tax credit proposal last year after extensive consideration, the bill received no further action last year. But the Committee's efforts could form the basis for legislation in the 98th Congress. Legislation, S. 528, was introduced February 17.

3. Enterprise Zones. The Finance Committee has again reported out a modified version of the administration's enterprise zone proposal. A major question remains whether the House will take an interest in the idea, which they did not in the 97th Congress.

4. DISC. While no specific DISC proposal was made in the 97th Congress, the issue was extensively discussed--particularly the question of legality under the GATT. The Administration has committed itself to bringing the DISC into conformity with the GATT and will submit legislation to do so shortly.

VI. Social Security

A. The National Commission developed a bipartisan package that deserves support. It is not perfect, and everyone had to swallow hard on some items: that is the cost of reaching agreement.

B. The work of the Commission made clear that we had to confront the crisis in social security. The Commission agreed that $150-$200 billion is needed between 1983 and 1989 to ensure the solvency of the system through 1990. This means providing about a 15 percent reserve ratio by 1990 under the pessimistic--some would say realistic--assumptions.

C. The bipartisan package, includes a 6-month delay in cost-of-living adjustments, partial acceleration of scheduled payroll tax increases, coverage of new Federal workers and non-profit organizations, and partial taxation of benefits for higher-income beneficiaries.

D. We cannot forget that the payroll tax burden is already heavy and scheduled to increase, and the confidence of young people is critically low. The long-term deficit can be reduced considerably by very gradually slowing the growth of the system as people come on to the rolls in the future. The bill raises the retirement age to 67, again very gradually, for people retiring some 20 or 30 years from now. Ample time is available for people to adjust their savings and retirement decisions.

VII. Trade

A. Trade deficit is too large. The size of our trade deficit (which is now projected at $75 billion in merchandise trade and $30 billion in current account) alone means Congress will continue to look hard for ways to reform our trade policy. The system of multilateral arrangements has been called into serious question as many believe it fails to meet our needs. Many voters and members of Congress will want to see us approach more of our trade problems on a bilateral basis. The average American simply does not understand why Japanese cars and TV's sell well here but American cigarettes, beef, baseball bats, and cosmetics cannot be sold in Japan. Remedies for this type of situation are certain to be a major focus of attention in this Congress.

B. Export issues. Unfortunately, the GATT ministerial failed to make progress on the question of foreign subsidies for agricultural exports. This will continue if pressure from Congress to resolve this situation through negotiation or for other export promotion actions like the recent wheat flour sale to Egypt. S. 822, recently passed by the Agricultural Committee, would establish several export promotion activities.

I support efforts to equalize the rules under which trade is conducted. This does not mean trade war, but does mean seeking to expand East-West trade, developing a viable substitute for

DISC, utilizing Ex-Im Bank resources more adeptly, and enacting the trade reciprocity bill that the Senate approved April 21. Fair access to markets must be a two-way street, and Congress will be under considerable pressure to see that that is so.

C. Import issues. As you know, the House passed "local content" legislation at the end of the last Congress. That is a drastic proposal and likely to be counterproductive in the long run if our goal is to increase access to markets and to gain maximum benefit from the mutual advantages of international trade. There may be other areas, however, where we might make adjustments: in considering extension of the Generalized System of Preferences, there may be an interest on the part of some members of the Finance Committee to seek some reciprocal benefits from the major GSP beneficiaries. There appears to be substantial support for the trade provisions of the President's Carribean Basin Initiative, however, as those countries offer U.S. exporters a potentially strong market. It may be difficult to renew the President's general authority to negotiate tariff reductions on a limited basis. It is a good sign that the Japanese have agreed to continue voluntarily to restrain their automobile imports to this market for a third year until the domestic industry has had an adequate time to get back on its feet.

D. Clearly the heat is on when it comes to seeing that American producers get fair treatment under our system of international trade. If we choose our battles carefully to secure an appropriate response from our trading partners, we have an opportunity to making trade freer and fairer, to the advantage of everyone. But we must avoid the two extremes of allowing the world to think only the U.S. will play by the rules of free trade, regardless of disadvantage to our citizens; or, on the other hand, taking extreme unilateral actions that may look good politically but that, in the long run, will provoke severe reaction and deprive us of market opportunities. We need just the right amount of leverage to open more doors, not have them slammed in our face.

VI. Conclusion

The months and years ahead must not be dominated by rigid ideologies on either side--but neither can the President or the Republican leadership be expected to cast aside the principles of Government the American people so soundly endorsed in 1980. Those principles--a more restrained Government, a freer economy, greater accountability to the American people--are as valid today as they ever were, and there is no indication that the people have changed their commitment to these same principles. Guided by these principles, we will try to work together to build on the sound foundation for recovery that has already been laid.