REMARKS OF SENATOR DOLE

LOUISIANA ASSOCIATION OF INDEPENDENT PRODUCERS & ROYALTY OWNERS

Friday, March 30, 1984--12:00 p.m.--New Orleans, Louisiana

Why worry about the deficit--What does it mean to the average American?

- If nothing is done to reduce deficit spending over the next five years, the total Federal debt will nearly double to over $10,000 for every man, woman and child in America.
- At this level, by 1989 it will take one-half of all Americans' personal income tax payments just to pay the Federal Government's interest bill.
- By 1989 the annual Federal interest cost will amount to $250 billion--about $1,100 for every American.
- That $1,100 per person interest cost is equal to 40% of each person's annual expenditure for food.
- Virtually all economists agree that the sustained enormous deficits that we are facing will be economically harmful.
- Many Americans will find home-buying more difficult with higher deficits. Consider a family purchasing a home at today's current interest rate, averaging about 12-1/2%, with a $55,000 mortgage. If the deficits push interest rates up, total interest costs over the 30 year term will be $15,500 more for each one percentage point increase.
- All Americans will directly feel the results of high deficits if they lose jobs as a result of a business slowdown resulting from a crowding out of private investment, or if they lose jobs to imported products made more competitive because of an abnormally strong dollar or if they end up paying higher prices because inflation is rekindled.

What is the Federal deficit likely to be?

- The estimates of future Federal deficits are quite sensitive to one's economic assumptions. Yet even under the most optimistic of economic assumptions, the deficit will remain at historically high $200 billion levels over the foreseeable future, unless drastic action is taken.
- Assuming an extremely strong recovery (4% real growth of GNP) is sustained over the next few years and all of the Administration's

proposed spending cuts and revenue proposals are enacted, the deficits are still projected to be:

FY 1985	FY 1986	FY 1987	FY 1988
$180 billion	$177 billion	$180 billion	$152 billion

- If economic growth is not so strong (3% real GNP growth) and interest rates are slightly higher (9% T-bill rate), and Administration's spending cuts are not enacted, the projected deficits would be:

FY 1985	FY 1986	FY 1987	FY 1988
$202.6 billion	$236.7 billion	$270 billion	$290.1 billion

- If we have an economic downturn during this period, we may be facing $300 plus billion deficits.

Why should we act this year on the deficit

- If we fail to deal with the deficit now, the problem will become worse. Current projections showing deficits holding in the range of $200 billion probably are optimistic, as they are based upon assumption of steady economic growth through 1989. However, postwar experience suggests that the average recovery lasts only 3 years, making a recession in 1985 or 1986 likely.

- If we postpone action until 1985 and we do suffer another recession, the deficits would then hit the $300-$400 billion range. At that point, it may be difficult to cut the deficit without further weakening the economy. Our choices would become very difficult indeed.

- Of course, failure to reduce the deficit in 1984 makes a recession likely to come sooner, as interest rates are forced up by private credit demands clashing with Treasury borrowing needs.

- By postponing action of the deficit, we increase the risk of recession. The average increase in the unemployment rate during a postwar recession is about three points, or three million jobs. By acting to reduce the deficit, we can significantly lower the risk that three million workers will lose their jobs in 1985 and 1986.

- The rise in interest rates will depress auto sales, housing starts, and capital goods orders. It is widely recognized that sustained economic recovery will be impossible unless these key sectors are healthy.

- Alternatively, the Fed could offset the deficits' impact on interest rates by "monetizing" the debt, leading to a resurgence of inflation in 1985. If we do nothing, we will force the Fed to choose between high interest rates and recession, or inflation.

- Failure to reduce the deficits in 1984 may also depress the stock market. A key factor in determining equity and bond prices is investors' confidence that Congress and the Administration can produce a sound fiscal policy. If we send the signal that the deficit problem is secondary to politics, equity and bond prices may fall.

- The exploding cost of servicing the Federal debt will make controlling spending more difficult each year, unless the deficits are reduced soon. Each year that we add $200 billion in new Federal debt adds about $15 billion to the next year's interest costs.

- The economy is now on a path where more and more of its resources go just to pay off the debt. According to economist Lawrence Summers, "It's a case where the miracle of compounding (interest) works against you."

- In 1976 net interest accounted for just 7% of total outlays But if we do nothing, by 1988 the total Federal debt will be more than half of total GNP, and the net interest cost of servicing this debt will reach 14% of all spending. Each year that we do nothing, the share of Federal spending that we can control gets smaller.

- Recent studies indicate that current and prospective budget deficits may have helped to overvalue the American dollar. If the deficits are not reduced, the problem of overvaluation could become worse, weakening the competitive position of American exports and costing the U.S. jobs in such industries as steel, electronics, and agriculture.

Deficit downpayment in 1984

- The President took the lead to begin a deficit-reduction effort in 1984 by calling for bipartisan negotiations on a package to reduce the deficit by $100 billion over 3 years. Now he has worked with congressional Republicans to outline a $150 billion package including defense savings ($40 billion), nondefense cut

($43 billion), revenue increases ($48 billion), and debt service savings ($18 billion). As the President suggests, we can work with a variety of modest spending reductions, and tax reforms that raise revenue, to enact a significant deficit "downpayment" in 1984.

- Even though election-year politics makes it difficult to launch the kind of major assault on the deficit that we really need, that is no reason to do nothing. Making a noticeable dent in the deficit will make our job easier in the years ahead. Even more importantly, it will demonstrate that we can face up to the deficit problem even in an election year.

- The Finance Committee has agreed on spending and revenue options just within its jurisdiction that achieve about $74 billion of the "downpayment" goal. To do that we are drawing on a number of proposals that have been on the table for some time, including some already in the legislative "pipeline":

  -Items included in the FY 1984 reconciliation bill, S. 2062, which awaits Senate action

  -Treasury-endorsed proposals on tax shelters and other abuses

  -Administration -proposed spending cuts that were not followed through on last year

  -Administrative savings and other proposals made by the Grace Commission

  -Additional proposals considered in the Finance Committee last fall

- Target. With an overall goal of $150 billion in savings, we can achieve $21.4 billion from revenue changes pending in S. 2062, $3.8 billion in spending reduction from Finance Committee programs in S. 2062, $3.1 billion from Grace Commission recommendations, $9.6 billion in debt service savings, and the remainder from additional spending and tax changes aimed at desirable policy reforms.

- Feasibility. The key is to keep following the President's suggestion and concentrate on relatively non-contentious items, avoiding things like the third-year tax cut and indexing, mean-tested entitlements, social security, and the like. Our effort must be bipartisan and balanced to do the job: Democrats and Republicans alike will benefit by cooperating to take swift action on the deficit. Time is of the essence if we are to make a beginning this year.

- Initial Finance Action. On February 23, the Finance Committee began action to reduce the deficit. So far the Committee has agreed to changes in health care programs that save $8.3 billion between now and 1987, over and above the provisions in S. 2062. In addition, the Committee agreed to tax reform and modest revenue raisers that generate $48.1 billion between now and 1987, provided at least that amount of spending reduction can be achieved. The House Ways and Means Committee has also reported a $50 billion tax bill, so we may be on our way.

Recovery--What progress have we made

Strength of recovery

- A strong recovery is on track and appears to be moderating to a pace that can be sustained in the years ahead. As an indication, look at the expansion of real gross national product. It grew by 9.7% in the second quarter of 1983, 7.9% in the third quarter, and an estimated 4.5% in the fourth quarter. By this measure, the recovery is the strongest since 1961.

- Housing starts are running at a rate of about 2.2 million units a year, and jumped 11.2 % in February.

- Industrial output in 1983 rose 6.5%, and factory utilization is up to 80.7%--the highest level in two years, and close to the normal capacity of 82%.

- The Commerce Department's survey of business plans for 1984 show that business plans to increase capital investment by 16%--this is higher than that seen at comparable points in previous postwar recoveries.

Inflation

- The best news about this recovery is that it is noninflationary. In 1983 the producer price index rose just 0.6%--the lowest increase since 1964. The CPI for 1983 was 3.8%, the lowest since 1972. Continued moderation in producer prices indicates low inflation will continue.

Creating Jobs

- People are going back to work, and the pace of job creation has been unusually high for a postwar recovery. On January 6 the Labor Department announced the civilian unemployment rate dropped from 8.4% last November to 7.8% in February. Overall, this means unemployment has dropped 2.9 percentage points over the past year.

- The continued strength of the recovery shows that recent growth in employment has not just been a statistical fluke, but shows a real turnaround in the labor market. Unemployment fell 230,000 in December, and there have been 4.9 million jobs created in the last year.

- What is more, the growth in jobs is broad-based. While manufacturing industries showed the most dramatic gains, all industries other than government and agriculture showed dramatic drops in unemployment.

HIGHLIGHTS OF FINANCE COMMITTEE DEFICIT REDUCTION DECISION (to date)

(Savings estimates are for period 1984-87, and include outlay savings in S. 2062)

Spending Restraint

- Medicare Part B Premium. Stablize the premium as a percent of program costs between 1985 and 1990. ($1.2 billion)
- Delay initial Medicare eligibility until month after an individual's 65th birthday. ($630 million)
- Working age. Non-working spouses age 65 to 69 could elect primary medical coverage under spouse's employer health plan rather than Medicare regardless of working spouse's age. ($1.1 billion)
- Physican freeze. Continue until July 1986 a freeze on physican's fees for those unwilling to accept assignment for all services to Medicare patients. ($2.8 billion)
- Fee schedule for lab services. Payments for clinical lab services would be held at 62 percent of prevailing charge levels through October 1987 ($1.0 billion)
- Limit on hospital costs. For FY 1985 and FY 1986 increases in hospital cost payments under Medicare would be limited to one-half percent less than the hospital wage and price index increase. ($1.1 billion)
- Grace Commission. Improved cash management techniques (e.g. faster deposits of receipts to the government), improving income verification procedures for benefit programs, and using IRS refund offsets to collect debts owed the government would be implemented. ($3.1 billion)
- Debt service. $9.6 billion.

Revenue Increases

- Tax reform. New rules would be applied to limit tax shelters in such areas as partnership allocation of expenses and income interest deductions on discount obligations, transactions between related parties, current deductions for future liabilities, and corporate deductions for extraordinary dividends received. ($10.2 billion)
- Tax benefits. Where a taxpayer receives a refund or other recovery for State taxes or other situations that previously gave rise to a deduction, the tax benefit portion of the deduction would be brought back into income first. ($800 million)

- Real Estate. Depreciation rules (20 years for all structures, new or used), and recapture rules for real property would be adjusted. ($4.4 billion)

- Freeze. Expensing for small business investment would be frozen at $5,000, the cost of used property eligible for the ITC would be frozen at $125,000, and the foreign earned income exclusion would be frozen at $80,000. ($1.9 billion)

- Distilled Spirits. Federal excise tax would be increased $2.00 per proof gallon ($1.0 billion)

- Income Averaging. The base period for determining the income averaging threshold would be reduced to 3 years and the formula slightly modified. ($1.6 billion)

- Earnings and Profits. The definition of earnings and profits would be modified so that it more closely reflects a corporation's economic income rather than its taxable income. This change will reduce a corporation's ability to pay tax-free dividends. ($1.7 billion)

- Add-Ons. In addition to miscellaneous items, the Committee agreed to phase in spousal IRAs; an R&D package; foundation tax changes; extend the targeted jobs credit for 3 years; enterprise zones; increase the earned income credit; Foreign Sales Corporations; energy credit extension with credit reordering; and others.

March 23, 1984

PRELIMINARY ESTIMATES OF THE SENATE FINANCE COMMITTEE PACKAGE

SPENDING	1984-87 Total (Savings in $ billions)
Reconciliation (S. 2062)	
Finance Committee provisions	3.8
Additional Spending Reductions	
*Part B Premium	0.4
*Delay in Initial Eligibility for Medicare	0.6
Working Aged	1.1
*Physician Freeze	0.8
Hospital Market Basket	1.1
Lab Fee	0.9
Medicaid Reduction	1.4
Alcohol Rebate	0.9
Revaluation of Assets	0.3
Lesser of costs of charges	0.3
Competitive Bidding/Claims	0.1
Round Part B Payments	0.2
SNF Rates	(0.1)
Grace Commission	3.1
Debt Service	9.6
Total	24.5

	1984-87 Total (In $ billions)
Reconciliation Tax Provisions (S. 2062)	21.4
Additional Revenue Items:	
Tax shelter, accounting abuse, and corporate reform	10.2
Tax Federal Home Loan Mortg. Corp.	0.3
Tax benefit rule	0.8
Alcohol and tobacco collections	0.5
Freeze ACRS expensing, ITC for used prop. and foreign income exclusion	1.9
Postpone finance lease rules	2.7
Extend telephone-excise tax	3.2
Modification of Sec. 1231	0.2
Factoring of trade receivables	1.4
Source of shipping income	0.2
Recharacterization of U.S. income as foreign source income	0.3
Trust distributions	0.7
Income averaging modification	1.6
Delay in ESOP	0.4
Corporate preference exclusion increase	0.5
Increase distilled spirits tax	1.0
Deferred rent on real and taxable property	1.7
Repeal dividend reinvestment	0.4
Installment sale recapture rule	0.2
20-year life for structures	4.2
Other miscellaneous revenue increase proposals	2.6
Major Revenue Loss Provisions:	
Spousal IRAs	-.9
Enterprise zones	-1.3
R&D credit extension and expansion	-2.0
R&D foreign source allocation	-0.2
Targeted jobs tax credit	-1.6
Life insurance tax change	-1.3
Earned income tax credit	-0.4
Mortgage revenue bond extension-IDB package	-0.6
Grand Total	$48.1

ENERGY TALKING POINTS

LOUISIANA ASSOCIATION OF INDEPENDENT PRODUCERS AND ROYALTY OWNERS

March 30, 1984

I. Windfall Profits Tax History

- Although it may be hard to believe, it has only been four years since the so-called Windfall Profit Tax was enacted by an Administration and Congress that were decidedly "anti-oil".

- I am proud of the role I played in opposing that legislation and improving it when it was obvious that the legislation could not be defeated.

- In the course of Senate Committee and floor consideration of the Windfall Tax, I offered amendments:

  (1) to exempt totally all newly discovered oil,

  (2) to exempt totally independent and royalty stripper oil,

  (3) to reduce the tax rates and Tier 1 and Tier 2 oil;

  (4) and to exempt from the tax interest held by non-profit educational institutions and medical facilities.

- In conference I worked hard to reduce the tax burden on independent producers. This work, along with the work of others, resulted in a tax structure that provided generally lower tax rates for independent producers.

- Despite these improvements, I voted against final passage of the Windfall Profit Tax.

II. Subsequent Windfall Tax Relief

- I am pleased to report that the general attitude toward the oil industry within both Congress and the Administration has radically improved since April 2, 1980 when President Carter signed the Windfall Profit Tax into law.

- In the 1981 tax cut bill we were able to significantly alleviate the burden of the Windfall Tax.

- In 1981, we:

  - o totally exempted independent stripper oil,

  - o exempted royalty owners on their first two barrels of production per day (three barrels per day beginning in 1985). This amounts to a total exemption for more than 90 percent of all royalty owners in the country.

  - o phased down the tax rate on newly discovered oil from 30 percent to 15 percent by 1986.

- This relief was originally estimated to save the industry more than $12 billion between 1981 and 1986, although lower than expected oil prices have substantially reduced that figure.

III. House Ways and Means Bill Freeze

- The House Ways and Means Committee current tax increase bill (H.R. 4170) would freeze the Windfall Tax rates on newly discovered oil at its 1983 level (25%) through 1987. The rate would be allowed to phase down to 15% by 1990.

- It is estimated this change will pick up only $15 million in 1984 and $15 million in 1985.

- There is no similar provision in the Senate Finance Committee's bill.

- In my view it is vital that we continue to reduce the tax burden on domestic oil exploration and thus I intend to fight in conference to have the new oil rate freeze eliminated.

IV. Other Issues of Interest

A. New Energy Taxes Dead This Year.

- Almost every time the subject of budget deficits arises, there are those in Congress who advocate some form of massive new energy tax as the panacea.

- Consequently over the past several years we have heard about oil import fees, BTU taxes, a 50 cent per- gallon gasoline tax and an ad valorem tax on all energy.

- Last November the Senate Finance Committee considered a 2 1/2% ad valorem tax on all forms of energy -- oil, natural gas, coal and electricity.

- This energy tax proposal was a refinement of the Administration's contingency tax proposal which includes a $5-per-barrel excise tax on crude oil.

- Since the President definitely rejected any contingency tax, including any crude oil tax, the idea of a big energy tax is dead for this year. None of the major budget proposals -- Democrat or Republican -- contains an energy tax.

- That does not mean that the idea will vanish from Washington. Undoubtedly next year energy taxes will again be raised as a revenue option.

B. <u>Percentage Depletion on Secondary and Tertiary Oil Production.</u>

- Because of a technical drafting error in 1975, all percentage depletion on production from secondary and tertiary methods expired at the beginning of this year.

- Last year I introduced legislation to correct this problem and reestablish 15% depletion on such production, as was Congress' original intent.

- It makes no sense to have 15% depletion on primary production, and no depletion on more costly secondary and tertiary oil production.

- A log jam in all tax legislation at the end of the last session prevented our enactment of corrective legislation.

- Nevertheless, my bill to correct this problem has been approved as part of the Finance Committee's deficit reduction package.

- Unless this error is corrected, the industry will be saddled with a $700 million additional and unintended tax burden over the next three years.

- Unfortunately, revenue considerations and some opposition prevented us from dealing with the problem of the availability of depletion on transferred properties. I did not want to jeopardize the relief for all secondary and tertiary properties by insisting on $130 million in transfer relief.