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

March 7, 1985

TO: Senator Dole

FROM: George Pieler

SUBJECT: Talk to Washington Non-Profit Tax Conference

Attached is an Outline of Remarks for this talk. The group is mainly interested in the budget and possible tax changes from the point of view of the leadership.

There might be a question about how the Treasury tax reform proposal would change the tax treatment of charitable giving. Under the Treasury plan, individuals and corporations could deduct charitable contributions only to the extent the contributions exceed 2 percent of the taxpayer's adjusted gross income. Now, of course, there is no such floor on the charitable deduction.

The 2 percent figure was chosen because it is the median charitable deduction claimed by taxpayers who itemize. Treasury claims this would have a minimal effect on charitable giving because tax considerations become important only at higher giving levels and with higher income taxpayers.

Chairman Packwood has not said yea or nay on this particular piece of the Treasury plan, but he has indicated an open mind on the charitable deduction--he will not necessarily push for continuing the above-the-line deduction, for example.

Non-profits may also be concerned about the general effect of lowering tax rates across-the-board, which reduces the value of any deduction, including the charitable deduction.

Attachment

REMARKS OF SENATOR DOLE

21st ANNUAL WASHINGTON NON-PROFIT TAX CONFERENCE

Thursday, March 7, 1985 -- 12:30 p.m.

J. W. Marriott Hotel

CAPITAL BALLROOM

1. The 99th Congress

- We face major challenges on the deficit, the MX missile, tax reform, Central America. We can meet these challenges by working with President Reagan on the basis of mutual respect.

- Congress knows that President Reagan's overwhelming election victory sent a strong message about what the people expect us to do. We already are at work on his agenda, but success will depend alot on mutual recognition that Pennsylvania Avenue is a two-way street.

- Our top priority is to cut spending to reduce the budget deficit. That is why Senator Domenici and I introduced S. 1, which commits us to getting the deficit down to $100 billion or less by 1988. The vital issue of tax reform should proceed on a separate track to allow us to sort out the options and see if we can build a consensus without losing momentum on the urgent problem of the deficit. Other issues that require attention in 1985--a new farm bill, Superfund, national defense, and arms control--will not be neglected.

2. Our Economic Progress

- Economic recovery remains on track and is moderating to a pace that can be sustained in the years ahead. Real GNP grew 6.1% in 1983, and continued at 6.8% in 1984, peaking at a 10.1% rate in the first quarter last year. That is the highest real growth rate since 1951. This remains one of our strongest recoveries.

- With national unemployment down to 7.4%, this recovery has created over 7 million jobs. More people are working than ever before. Factories are operating at the highest capacity levels in 4 years, close to 82%. Housing starts in January rose 15% to an annual rate of 1.83 million.

- The best news about this recovery is that inflation is staying low. Producer prices in 1983 showed the smallest increase since 1964. The CPI rose just 3.8% in 1983 and 4% in 1984. We can sustain strong growth with low inflation: especially if productivity keeps rising, as it did in 1984--by 3.6%.

- o Growth, lower inflation, and major tax relief have increased real personal income by over $116 billion since 1982. Real after-tax incomes grew 6.8% in 1984--the biggest increase in over a decade.

- o Trends in the economy still look good. The prime rate--which rose from 6.5% to 21.5% under Carter-Mondale--stands at 10-1/2%. The misery index, which peaked at 24.5% in March of 1980 is around 11%.

3. The Budget And the Deficit

Nature of the Deficit Problem

- o After several years of budget deficits that approached the $200 billion mark, some people seem to be getting complacent about the problem. Since the economy has continued to do well, with low inflation and strong growth, why worry about the deficit?

- o The answer is that everything we have achieved for the economy in the last several years is put at risk unless we deal with the deficit. And part of the problem is that the public can't get very excited about the deficit dilemma. It seems we need to have a crisis on our hands, or some kind of visible faltering in the economy, to convince people of the urgency of reducing the budget deficit.

The Real Point

- o Sustained deficits in the $200 billion range pose an imminent threat to the recovery, because they will lead to either higher inflation or slow growth and rising unemployment. Without assurance that inflation will remain under control, and credit available at acceptable rates of interest, business will not expand through new investment, and jobs will not be available for our sons and daughters when they are ready to enter the workforce.

What Needs to be Done

- o The sacred cow is a thing of the past: everything in the budget must be scrutinized for possible savings. We have not done all we can to reduce Federal spending when the budget still represents nearly 25% of the gross national product.

Spending "Freeze Plus"

- The President's FY 1986 budget proposes to freeze total spending plus reform some programs and terminate others that have outlived their usefulness. That would cut $50 billion from the deficit next year: the minimum we need to sustain a healthy recovery, according to Paul Volcker and other experts.

- Congress will change some of the President's budget priorities, for example, by cutting a bit more from defense. And Senate Republicans want to go a little further in the outyears to get the deficit down to 2% of gross national product by 1988.

- In the Senate, we are moving toward a major spending cut package. The Budget Committee has begun work on the President's plan, and our committee chairmen have already pledged about 60% of the needed domestic cuts--contingent on getting a balanced package that includes defense. We are working on an expedited scheduling and hope to have a budget approved by March.

Popular Support

- The people want spending cut. The Los Angeles Times poll shows that by a 5 to 1 margin, Americans prefer cutting government spending over tax increases to deal with the deficit.

- The Gallup poll shows that 54% of Americans believe the deficit is a very serious problem: but it's tough to translate that into action because the public has varying views on which spending should be cut.

- Experts also agree that spending reduction is the way to go. In January, distinguished experts such as Alan Greenspan, Charles Schultze, and Martin Feldstein told the Finance Committee that cutting spending by $50 billion or more in 1986 will reduce interest rates, keep inflation down, and ensure continued recovery.

Risks Ahead

- Time is of the essence, because we are at the point where economic expansion will either continue, competing against heavy Treasury borrowing, or the recovery will slow and possibly slip into recession. That is why Senate Republicans moved ahead of schedule to work out a budget plan. The risk is that the deficit problem will compound itself: each year that we add $200 billion in new Federal debt adds about $15 billion to the next year's interest costs. The exploding cost of servicing the Federal debt will make controlling spending that much more difficult each year.

All Aboard

- o Everyone must share in the effort to close the deficit gap. People will accept a limited, short-term sacrifice for fiscal restraint if they understand that it is the best investment they can possibly make for their own, and their families', economic future.

4. Major Tax Reform

- o The Treasury Department has proposed an innovative, constructive new plan for reforming our tax system, and the President made tax reform a high point of the State of the Union address. Some of the proposal is highly controversial, and the President no doubt will modify some things. The Treasury initiative provides an excellent starting point for the 1985 tax reform debate.

- o Under the Treasury plan, there would be just three tax rates: 15, 25 and 35 percent. The personal exemption would double, to $2,000. Rate brackets, the zero bracket, and the personal exemption would continue to be indexed. For corporations, there would be a single rate of 33 percent.

- o Major tax breaks that would be dropped include the deduction for State and local taxes, the marriage penalty offset, the investment tax credit, the capital gains exclusion, the tax exemption for private purpose bonds, and the exemptions for employer-provided fringe benefits.

- o Tax provisions that would be modified include mortgage interest deductions for second homes (disallowed); the charitable deduction (limited to amounts in excess of 2 percent of adjusted gross income); business expense deductions (limited); and taxation of dividends (a partial dividends-paid deduction).

- o Indexing would be extended to capital gains; interest income and expense; depreciation deductions; and the earned income tax credit.

- o It is important to build a consensus for any far-reaching changes, drawing on the Treasury plan, Bradley-Gephardt, Kemp-Kasten, and other plans. It may be necessary to move gradually, and reform will not be possible without strong Presidential leadership. And the people will have to let us know if they think the kinds of trade-offs being proposed are worthwhile.

5. International Trade

- Another major challenge is to keep international markets as free and open as possible in an era of record U.S. trade deficits. Reducing the budget deficit will be a tremendous help, because it will help moderate interest rates and the value of the dollar.

- So far we have done well in keeping avenues of trade open. It is especially significant that last year's trade bill extended for 8 1/2 years, the Generalized System of Preferences, which provides duty-free treatment for certain imports from the underdeveloped world.

- In a similar trade liberalizing vein, the bill authorized the negotiation of free-trade zones, specifically with Israel, and the reciprocal reduction of tariffs on semiconductors.

- It is hoped that the authority to negotiate bilateral free trade arrangements may induce other countries to join in trade liberalization.

- The trade bill recognized, for the first time, the importance of trade in services (including banking); The President is directed to negotiate reduction in barriers to trade in services (a sector in which the U.S. has the competitive advantage and which represents a major portion of our GNP.)

- At the same time, the U.S. must be prepared to use what leverage it can when markets are unfairly closed to American producers. That is why we are reviewing overall trade relations with Japan to help remove artificial barriers to American entry to the Japanese market.