

MIRL W.

TRANSCRIPT OF PROCEEDINGS

UNITED STATES SENATE

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COMMITTEE ON FINANCE

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MARK-UP

Washington, D. C.
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WEDNESDAY, NOVEMBER 16, 1983

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United States Senate,
Committee on Finance,
Washington, D. C.

The Committee met, pursuant to notice, at 9:42 a.m., in Room SD-215, Dirksen Senate Office Building, Honorable Robert Dole, Chairman of the Committee, presiding.

Present: Senators Dole, Grassley, Symms, Durenberger, Heinz, Chafee, Danforth, Roth, Packwood, Long, Bentsen, Moynihan, Baucus, Boren, Bradley, Mitchell, Pryor, Matsunaga, Roth, and Warner.

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The Chairman. Do we have sound out in the hallway, because there are about 200 people out there?

And, do we have any doctors standing by as we go through this package, to administer first aid to lobbyists, or anything of that kind?

(Laughter.)

The Chairman. Let me suggest that we are going to start with the revenue package, and I want to first of all thank the members of our own staff and the Finance Committee staff, the Joint Committee staff, and Treasury. They have

1 been working--if some wonder why we have not met--they have
2 been working, I think, about eight solid days, tryin to put
3 together some of the details. We have also, obviously, been
4 aware of some of the public controversy concerning Social
5 Security COLAs, and other areas that became obviously too
6 hot to handle, and we have made some modifications on tax
7 indexing and also on COLA adjustments, that we will discuss
8 later on.

9 We have tried to be sensitive to the concerns that have
10 been expressed by Members on this Committee, other Members,
11 as well as at least voices we hear from other parts of the
12 City, and we hope that we now have a reasonable approach to
13 a \$150 billion deficit reduction plan. And I might suggest
14 that the urgency is greater than ever, because the Budget
15 Committee, I think in response to what they feel is their
16 duty, is prepared to offer a tax package on the budget
17 resolution and reconciliation, totalling about \$57.3 billion,
18 and I will ask that copies of that be made available--Rod,
19 do you have copies?

20 Mr. DeArment. Yes, Senator.

21 The Chairman. They do a number of things that I think
22 would fly in the face of the efforts of this Committee. First
23 of all, they would take over this Committee. That would be
24 the first thing that I would object to.

25 Secondly, there are a number of their provisions that I

1 think need some consideration--I understand they have not
2 been drafted, but I would hope that when Members look at the
3 tax list, which is the bottom half of that list, that our
4 package would look very good by comparison.

5 So, I would hope that Senator Domenici and Senator Chiles
6 would not pursue the amendment on taxes until this Committee
7 has had a chance to go over them today and then, hopefully,
8 meet again tomorrow morning and try to have a vote on a
9 package.

10 Senator Bentsen. Mr. Chairman, if I might ask a question
11 at this point.

12 The Chairman. Certainly, Senator Bentsen.

13 Senator Bentsen. I am concerned about the reconciliation
14 measure, and I am concerned about the question of what we are
15 going to do on the tax package insofar as the insurance
16 proposal on insurance companies, and I have, as you know,
17 repeatedly asked that it be placed on the agenda. I did that
18 some time ago, and I did it formally again on Monday, and I
19 am doing it again now. And I think we would make a serious
20 mistake going to conference with the House, if that point
21 ever comes and they get their bill considered, without the
22 input of this Committee as to what should be done on
23 insurance taxation.

24 The Chairman. Well, I certainly--.

25 Senator Moynihan. Mr. Chairman, could I simply associate

1 myself with Senator Bentsen's remarks.

2 Senator Chafee. And include this Senator.

3 The Chairman. I am certainly aware of numerous Senators'
4 concerns. In fact, I met with representatives of the industry
5 this morning. We were prepared to deliver to Senator Bentsen
6 and Senator Chafee sort of the Administration's position, but
7 based on my discussion, I have asked the Administration to
8 withhold that so that we might spend the rest of the day with
9 Treasury and someone from our own staff, the Joint Committee,
10 and the industry, to see if whatever disagreements there
11 might be can be hammered out. And if we can work out the
12 insurance package, we might be able to break that out of the
13 package, because I am advised this morning by the Chairman of
14 the Ways and Means Committee that he does not plan on going
15 going to conference this year. So, whatever happens on
16 reconciliation will probably happen Friday in the House, and
17 it is his present intention to go to conference next year.

18 But Senator Bentsen is correct, and we are not trying to
19 stall that issue; we are trying to work it out, and we hope that
20 we can do that before the day is over.

21 Senator Bentsen. Mr. Chairman, I would appreciate that,
22 and I would appreciate, too, that we be given some advance
23 warning and information, rather than coming into a committee
24 and being presented with a thick package which we have had no
25 chance to review or make any consideration of, and then to be

1 forced into a very hasty decision on it. I do not think that
2 is the proper way to approach something of that magnitude.

3 The Chairman. No, it certainly is not. And we have been
4 trying to be alert. In fact, we have been talking to different
5 staff people. I do not believe anybody is surprised on the
6 insurance part, but that is only one component. What we are
7 doing this morning in response to sort of the sub-working
8 group, six members of this Committee who made recommendations,
9 we have looked at those, we have tested those we have gone
10 back and tried to refine those, but essentially, many of those
11 suggestions are still a part of the overall package. We do
12 not believe anything in this package will come as a surprise to
13 any Member. There are a number of areas that Treasury wishes
14 to address in the loophole-closing area, but as we go down the
15 list, if there are questions, obviously, we have everybody here
16 prepared to respond.

17 Senator Bentsen. And if I might also say, Mr. Chairman, as
18 one of those six, I do not recall that these were recommenda-
19 tions of the six. These were proposals that were made by
20 staff to that committee of six, without any formal approval of
21 them.

22 The Chairman. Right, that is correct.

23 Senator Packwood.

24 Senator Packwood. Mr. Chairman, as we get down to the
25 later stages of this Session, obviously the Committees are

1 going to overlap and planning is going to overlap. But I
2 thought we were going to meet yesterday. I scheduled a meeting
3 of the Commerce Committee to mark up some bills, including the
4 "noncontroversial" item of syndication of television reruns
5 this morning, and I am going to leave.

6 But I want to compliment you on the leadership you have
7 taken in attempting to close the deficit--I do not know if you
8 are going to be successful. As I listened to some of these
9 statements by the Administration, it is clear that you are
10 carrying water uphill in a very difficult situation. But I
11 think you have done the best you can, and if you succeed,
12 congratulations, and if you do not, at least, well done.

13 The Chairman. Well, thank you. I must say I do not have
14 any--I did have a chance to indicate to the President that I
15 certainly agree with him on the deficit reduction--he wants
16 to do it, too--and I hope that we can--I am not certain we
17 can do it this week--I am not certain we are leaving this
18 week--but it seems to me that we have an obligation to
19 Committee Members to at least come back with what we believe
20 has some merit.

21 Now, I wonder, Rod, are you going to go through the
22 package? Let me say at the outset, on the revenue side,
23 which we will address first, any tax changes would be
24 contingent upon spending reduction, and we have gone over
25 the so-called trigger mechanism with the Congressional Budget

1 Office, Mr. Penner. We have tried to touch all the bases.
2 And again, I think Secretary Chapoton would indicate that
3 everything in this package at least has been addressed by
4 Treasury--I do not say you support every provision, but you
5 are aware of everything.

6 Mr. Chapton. Yes, we are aware of everything, and we will
7 have comments on some specific provisions.

8 The Chairman. And there are also about how many Members'
9 provisions in this package--30? It is \$2 billion worth.

10 Mr. Brockway. About 35, Mr. Chairman.

11 The Chairman. And we have also included in the package some
12 other areas that have been called to our attention by Members,
13 and again, I assume Treasury will have comments on those.

14 So, let us start on the revenue package.

15 Mr. DeArment. Mr. Chairman, in addition to the measures
16 that the Finance Committee reported out in the reconciliation
17 bill, we have some additional proposals. The total package
18 would add up over four years, '84 to '87, to \$74.3 billion.

19 The Chairman. I think that is point we want to make right
20 up front, that it is a four-year, not a three-year, package;
21 is that correct?

22 Mr. DeArment. That is correct, Mr. Chairman.

23 The Chairman. And there is very little impact in 1984.

24 Mr. DeArment. In analyzing the ability to make changes in
25 '84, we realized both on the spending side and on the tax side,

1 it was very difficult to effect changes in fiscal year '84.
2 The fiscal year is partially over, and we are facing various
3 deadlines in spending and on tax forms and the like, so it is
4 difficult to effect those changes.

5 The Chairman. I wonder if you could move that mike a
6 little closer. I am afraid you are not going to be heard
7 outside.

8 Senator Baucus. Mr. Chairman, are we working off of a
9 chart or a table?

10 Mr. DeArment. I think the best document to work on is
11 the document labelled, "Summary of Proposed Deficit Reduction
12 Package, Total Revenue Effect." The first item is the
13 contingent revenue increases. It is contemplated that all of
14 the non-loophole-closing items in this package would be contin-
15 gent on the spending cuts both in this Committee and in ot er
16 committees being achieved, and these taxes would not take place
17 until January 1st of 1985 and trigger on only if those spending
18 cuts were achieved.

19 The first item is a 2 percent energy tax which would be
20 imposed on the sale of energy consumed within the United
21 States. The energy source subject to the tax would be oil,
22 natural gas, natural gas liquids, coal, and electricity.

23 In designing the proposal, we provided that the amount of
24 the tax collected on coal would be deposited into an acid rain
25 trust fund, and I think that is something like \$600 million a

1 year.

2 Mr. Brockway. I think it is something less than \$600
3 million a year.

4 Senator Moynihan. Over the period, \$2.4 billion--is that
5 what you are saying--sorry, Mr. Chairman--.

6 The Chairman. No, certainly. Are you talking about the
7 trust fund?

8 Senator Moynihan. Yes, that would accumulate--is this
9 a permanent tax that we are proposing or just a four-year?

10 Mr. Brockway. Well, you are proposing just a three-year
11 energy tax that would be on all fuels, but the amount that
12 you collect attributable to coal only--.

13 Senator Moynihan. Would be 1.8?

14 Mr. Brockway. ---that would go into the fund, and in a
15 second, I will have the precise number.

16 Senator Moynihan. All right. When you get it, let us
17 know.

18 Senator Danforth. Mr. Chairman, first, do we have a
19 program on acid rain? I think we should, but do we?

20 Mr. DeArment. This would merely be a trust fund that
21 would be set up for that purpose to fund a program on acid
22 rain. That would not be within our Committee's jurisdiction.

23 Senator Danforth. Well, isn't this a little premature
24 without a program?

25 The Chairman. Well, one of the problems they are having--

1 and again, this is something the Committee can make a judgment
2 on--is that they do not have a program because they do not
3 have the money. This would provide at least--how much, over
4 the three years?

5 Mr. Brockway. It would be \$1.5 billion into the trust
6 fund for this purpose.

7 Senator Danforth. Would this truly affect the deficit--I
8 mean, if we are setting aside a fund in trust for a new spend-
9 ing program as yet undevised, is it reasonable to count this
10 money as part of a deficit reduction program?

11 The Chairman. I think these figures--well, it would be in
12 a trust fund, correct?

13 Mr. Brockway. It would be in a trust fund. You would
14 affect the deficit as you raised the funds, and you would
15 reduce the deficit. It is only to the extent that they are
16 appropriated out of the trust fund on the spending side that
17 that might have a countervailing reduction in the deficit
18 savings.

19 The Chairman. Senator Baucus?

20 Senator Baucus. Mr. Chairman, on that same point, would
21 the tax on the coal then be--how would it be levied on the
22 coal, at what stage?

23 Mr. DeArment. It would be levied at the sale to a major
24 fuel-burning installation.

25 The Chairman. I was going to clarify for those in the

1 Western states. How is the tax itself levied--it is based on
2 what?

3 Mr. DeArment. It would be based on the national average
4 sales price for each energy product. So at the point of sale
5 to a major industrial user, there would be a sort of fixed
6 amount, 2 percent of the national average sales price, that would
7 be collected on that.

8 Senator Baucus. So that would mean that Western coal
9 and Eastern coal would be taxed at the same rate?

10 Mr. DeArment. That is correct, that is correct.

11 Senator Baucus. And that would further mean that
12 the degree that that is passed on by utilities to consumers
13 would be at the same rate, whether the utility is a coal-fired
14 that burns either Western low sulfur or Eastern higher sulfur
15 coal?

16 Mr. DeArment. That is correct.

17 Senator Baucus. That would further mean, therefore, that
18 Western utilities, which have already spent--and I can say
19 this, anyway, for my State of Montana--about \$300 billion, in
20 meeting Class 1 standards of the Clean Air Act, and will
21 have reduced sulfur dioxide to about .02 pounds per million
22 cubic feet, will also have to pay that tax, even though the
23 proceeds from this trust fund will go not to those plants
24 who have met these requirements, but will go to Eastern
25 plants who have not met these requirements, and therefore, be

1 every discriminatory against Western coal.

2 Mr. Brockway. Senator Baucus, the general theory of this
3 tax--the Administration had proposed a \$5 per barrel tax on
4 oil, which would have been about a 10 percent increase, and
5 that would have raised the price level on all products. The
6 general theory here is to spread it out on all fuels and impose
7 on all fuels just a much lower tax, a 2 percent tax, so that
8 would have been imposed in any event, regardless of the region,
9 and this is just allocated in some of the revenues.

10 Senator Baucus. I understand that, but the degree to
11 which the proceeds of this tax go into a trust fund, which
12 then go out of that trust fund to clean up acid rain
13 problems which will go to high-sulfur coal-burning plants
14 will be discriminatory against Western coal. And I can tell
15 this Committee right now, this is not going to fly. This is
16 one Senator, and other Western Senators are going to oppose
17 this to the end.

18 So I would just firmly suggest that we do not go down
19 this road.

20 The Chairman. We are not going to vote--.

21 Senator Baucus. But I am raising the red flag right now.

22 Senator Danforth. Can I ask Senator Baucus, would it fly
23 if they did not have the acid rain trust fund?

24 Senator Baucus. It would more likely fly.

25 The Chairman. We can vote on that, but I think what we are

1 trying to do is even out the tax, so it is not all on one
2 commodity, and we can vote on whether or not we ought to have
3 a trust fund. That is not the most important thing in this
4 package.

5 Mr. Brockway. If you wish, Mr. Chairman, another
6 approach is to only dedicate part of the funds, just turning
7 on how much high-sulfur coal is consumed, and that might be
8 responsive to--.

9 The Chairman. Yes, I think they have a problem there
10 that I have read about.

11 Senator Durenberger. Mr. Chairman, I am going to have
12 to leave for a hearing, but as one who has been in the middle
13 of this acid rain controversy for a long time, and have my
14 own version of how to solve the problem, I would say that I
15 could support the tax to cut the deficit, but I could not
16 support it if you are going to start a new program to take
17 money from Kansas or Louisiana, where you use natural gas,
18 largely, and you do not create acid rain and send it to Ohio
19 to cut down on sulfur dioxide emissions there. So it would be
20 my recommendation, too, that you just forget about the trust
21 fund.

22 The Chairman. Let's go on.

23 Mr. DeArment. The next item, Mr. Chairman, is a high-
24 income individual surcharge.

25 The Chairman. That is Senator Danforth's suggestion, I

1 think.

2 Mr. DeArment. That is correct. It is a surcharge at a
3 lower rate on income taxes over \$6,300; \$5,700 in the case of
4 single returns, and 5 percent on taxes over \$22,000. That is
5 essentially in terms of the taxpayers that it would effect, it
6 would be 2 percent on taxpayers, roughly, over \$45,000--.

7 The Chairman. Again, I think the point to make is the
8 Administration did recommend a surcharge.

9 Mr. DeArment. They recommended a 5 percent surcharge on
10 all taxes, and this is only a portion of that.

11 Senator Bentsen. Mr. Chairman, he had started to say, I
12 think, the taxable income that that applied to, to give us some
13 feeling of the range. Could you at least state that?

14 Mr. DeArment. The rates are \$45,000 and \$100,000.

15 Senator Bentsen. Forty-five thousand single return?

16 Mr. DeArment. No; \$45,000, you would have a 2 percent
17 surcharge, adjusted gross income above that, and 5 percent
18 above \$100,000.

19 Senator Chafee. Mr. Chairman, do you want to have
20 questions as we go along, or how do you want to do this?

21 The Chairman. I would like to just run through it, if
22 we could, so the Members would be alerted to each provision,
23 and then come back and have some questions.

24 Mr. DeArment. The next item would be rounding down of
25 tax indexing, which will take effect on January 1st of 1985.

1 The indexing of the brackets exemptions and the zero bracket
2 amount would be computed with reference to the Consumer Price
3 Index rounded down to the next lower full percentage point. So
4 that if the CPI is 3.4, it would be rounded down to 3.

5 The Chairman. All right. Let me suggest that we tried
6 to get some symmetry, and since it appeared obvious to me that
7 there are not enough votes and not enough support either by
8 the Speaker or the President to even look at COLAs, it seemed
9 to me the least we could do was round down to the nearest
10 percentage on both the COLAs and indexing. And it is \$10
11 billion total. You get about 5.1 in Social Security and 5.6
12 here. At least we ought to be able to do that much; that is
13 hardly touching it at all.

14 Mr. DeArment. The next proposal would be to increase
15 the zero bracket amount in 1985 by \$100 for single taxpayers,
16 \$200 for joint returns. We would also restructure the zero
17 bracket amount for heads of households, so that the new
18 zero bracket amount for heads of households would be halfway
19 between the single and married rates, and we would adjust the
20 rate schedule so that that change would be revenue-neutral.

21 Senator Danforth. Now, Mr. Chairman, I would just like
22 to say on the zero bracket that this was Senator Baucus' idea,
23 and the theory of it was that if we were going to have
24 CPI minus 3 on tax indexing, the effect would disproportionately
25 ly hit the relatively low income taxpayer, and therefore, the

1 purpose of the zero bracket increase was to offset that, that
2 is, to provide greater equity in the distribution of any tax
3 increase. Now, what we have done is to have almost nothing
4 done on other than the surcharge on the high income taxpayers,
5 which is fine, but almost nothing done on tax indexing, and if
6 we have given up the zero bracket increase, we have gotten very
7 little in return.

8 The Chairman. Well, what we did--there was about an
9 \$8 billion revision, or 7.6, as I recall, and we cut it in
10 half, I think partly because of the indexing, but I think
11 partly because it just has not been adjusted for some time.

12 Mr. Brockway. And also, I think, because the energy tax
13 as a tax on consumption would tend to fall disproportionately
14 on lower income than upper income, so that you have the
15 high-income surcharge and the ZBA sort of balance out the
16 overall package and keep progressivity roughly comparable to
17 present law.

18 The Chairman. We did reduce that based on the change in
19 indexing and the change in the COLAs.

20 Mr. Brockway. As you had discussed it last week, it was
21 going to go up \$200 for singles and \$400 for joints, and now
22 it is only going to go up to \$100 for singles and \$200 for
23 joints--all of the individual income tax increases would be
24 scaled down in this package.

25 The Chairman. Mr. Chapoton, I do not want to put you

1 on the spot, but you are aware of this provision. Is that
2 something the Administration could support if there was some
3 agreement on everything else?

4 Mr. Chapoton. Well, we have examined a couple of aspects
5 of this. One is the zero bracket amount for heads of house-
6 holds, and we have agreed that there is a concern there. The
7 problem with doing something about it in every case is the
8 expense of doing so. I see this package would not only
9 increase from \$100 and \$200 for married and single, but also
10 have a new zero bracket amount in-between married and single
11 for the heads of household, and that seems to be a problem
12 to be addressed.

13 The Chairman. Well, we can modify all these things, but
14 I do remember attending a meeting at the White House with
15 Secretary Heckler--and I think you may have been there--and
16 they were discussing it, so again, it is something I know the
17 Administration has an interest in.

18 Mr. Chapoton. Yes, sir, that is correct.

19 Mr. DeArment. The next item would be a 2 percent tax on
20 corporate economic income. That would be an additional tax
21 imposed on economic income of corporations over \$100,000.
22 The economic income would be defined as the gross income less
23 certain deductions for things such as trade or business
24 expenses, interest cost, taxes, capital losses, bad debts--.

25 The Chairman. And this is two years?

1 Mr. Brockway. It would be three years.

2 Senator Long. I want to make a suggestion about this
3 type thing. It would apply to both this and the percentage
4 surtax. I would like to suggest that we stay with--like on the
5 surcharge, that we stay with the overall 50 percent rate. In
6 other words, that is your top rate, 50 percent, for example,
7 on individuals, and then you add the 2 percent, that the
8 ceiling should be 50 percent. In other words, you go up to a
9 50 percent rate. And you can get 2 percent more if you go to
10 52 percent by just picking up stuff that is either in the zero
11 bracket amount or taxable amounts that were in the rate scale,
12 going on up, but that we have a limit of 50 percent on the
13 personal income tax, and that we try to hold to a particular
14 rate with the rest of it. So that what you would be doing,
15 you would be losing the benefit of the lower tax rate on the
16 brackets as you go up, but when they get to the point where
17 they are hitting you with a 50 percent rate, then at least
18 we would not have to disturb that. I do not think that would
19 make much difference in revenue.

20 Do you understand what I am talking about, Mr. Chapoton?

21 Mr. Chapoton. Yes, sir, yes, sir, the desirability of
22 retaining the decision in 1981 to make certain that the marginal
23 tax rate never exceeds 50 percent.

24 Senator Long. Now, as precedent for that, back at the
25 time when we had those enormous tax rates, when we went up to

1 about 94 percent or something like that--I think we said that
2 in no event would it take more than 90 percent of what you
3 took in, your taxable income. It would seem to me as though we
4 could hold a 50 percent rate, and I do not think that would
5 cost you hardly anything in terms of revenue. You might give
6 us an estimate, but I bet you it would cost you precious
7 little.

8 Mr. Chapoton. As I understand it, this provision just
9 affects corporations. The provision which would cause the
10 problem you are addressing is the surcharge.

11 Senator Long. Earlier, on the list, you had one that
12 affects individuals, a high-income surcharge.

13 Mr. Chapoton. That is correct.

14 The Chairman. Have you done any work on that, Dave?

15 Mr. Brockway. Well, Mr. Chairman, the surtax as structured,
16 a significant portion of the revenue would come from people at
17 the 50 percent rate, and if you cut it off there, then you
18 would be having a tax increase on people in sort of the
19 upper-middle income, and not that much of a tax increase on--.

20 Senator Long. No, Dave, I do not think you get the point
21 I have in mind. I am just saying suppose you apply the 52
22 percent rate. Well, you see, you start out paying at zero,
23 on the zero bracket amount, and then you go on up the scale at
24 14 percent and so on up. So that you can stand a lot of
25 additional taxing before you finally get to the point that

1 you have got an overall effective 50 percent rate, you see.
2 You can take an awful lot of taxing before you have wiped out
3 your zero bracket amount and all these other amounts. I am
4 just urging that we say that in no event would the Federal
5 government for income tax purposes take more than 50 percent
6 of the entire thing.

7 Mr. Brockway. You are correct, and limiting the average
8 tax to 50 percent would affect relatively few cases. It would
9 be a very small amount of revenue.

10 Senator Long. At least, if we do that, we can say at
11 least we do not take more than half of it.

12 Mr. DeArment. That is not dissimilar to what we did on
13 the corporate side in the previous package, in terms of
14 recapturing the lower rates.

15 Senator Long. The same type thing.

16 The Chairman. Okay, let's get that information for
17 Senator Long.

18 As I understand, the proposals on revenue effect, on
19 tax shelters and accounting abuses and reform of the taxation
20 of corporations and their shareholders, this is something that
21 the Administration does recommend; is that correct?

22 Mr. Chapoton. Mr. Chairman, this is a long list of items
23 that we have testified with respect to over the year, or more
24 than a year, of problems that we have pointed out in the
25 law.

1 The Chairman. The point I wanted to make, so there will
2 not be any misunderstanding--and I am not directing this to
3 Mr. Chapoton--but every portion of this package, with the
4 exception of rounding down on indexing, in some form has either
5 been proposed by the Administration or supported by the
6 Administration, with maybe some modification of the zero
7 bracket area. But when you look at the President's proposal
8 in the '84 budget, I want it understood that we are not off on
9 some fishing expedition, and many of these in some form are
10 recommended by the Administration.

11 Mr. Chapoton. That is correct. As of course you know
12 and I understand this package, the President proposed on a
13 contingent basis--and I see that that is here--it was contin-
14 gent on his spending cuts.

15 The Chairman. In fact, we even have some language drawn
16 on the contingency that we will circulate later on, so that
17 Members will have a chance to review it over the day and the
18 night. We have gone over it with CBO, Mr. Penner, to see if
19 it will work.

20 I wonder, does Treasury want to go down the list of--I
21 do not want to say loophole closures--but at least some of the
22 abuses that we are trying to correct in the next category?

23 Senator Mitchell. Mr. Chairman, before you leave Item 1,
24 did I understand you to say that you will be circulating
25 something to define what is meant by--.

1 The Chairman. About the year that is prepared? Yes, we
2 do have it, and it will be submitted.

3 Senator Mitchell. So that we can defer further questions
4 on that.

5 The Chairman. In fact, it is being handed out right now.
6 I would like to go through the other provisions before we
7 go back to that.

8 I might also say that the matter you raised and Senator
9 Cohen raised has been included in this package, over the mild
10 objection of Treasury.

11 David, or whoever wants to continue.

12 Mr. Brockway. The various items that are either
13 considered in the general tax shelter hearings that Senator
14 Grassley had, where there were proposals submitted by Treasury,
15 and this picks up a good proportion of those proposals that
16 Treasury had suggested in those hearings and also a number of
17 proposals in the corporate reform area that were subject of
18 hearings about a month ago--not the major proposals, but a
19 number of particular proposals there that Treasury supported.

20 The first item on the list deals with partnership item
21 allocations. Under present law, within certain limitations,
22 you can allocate in a partnership gross income to one partner
23 and deductions to another, so you allocat the gross income to
24 a taxpayer who does not have tax liability and deductions to a
25 high income taxpayer--this proposal would say that generally,

1 you have to allocate taxable income or loss pro rata to
2 partners. There would be exception, however, in the case of
3 real estate depreciation and also in oil and gas for intangible
4 drilling costs, and depletion, where those could still be
5 specially allocated items.

6 The Chairman. Does Treasury want to comment?

7 Mr. Chapoton. I will just make a comment or two on a
8 couple of these. We did not suggest the exception for the
9 oil and gas and real estate. We recognize there might be some
10 support for that, and we think those exceptions ought to be
11 limited, because this is a problem area. Special item
12 allocations where you can have no loss in a partnership, but
13 one partner gets a loss out of the partnership, we have
14 problems with that.

15 Mr. Brockway. The second item on the list deals with
16 the retroactive allocation of partnership deductions, the
17 general rule that if a new partner enters a partnership during
18 the year, cannot allocate to that partner deductions that
19 accrued before he entered the partnership. Under present law,
20 however, if it is a cash basis partnership, you might have
21 deductions that accrued earlier in the year, and the partner
22 enters after the deductions have been incurred by the
23 partnership, but before they were paid; they pay the expense
24 after the new partner enters the partnership and allocate to
25 him the deduction, even though it was financially incurred

1 before that partner entered the partnership. This would
2 basically say we have a new partner entering; they would have
3 to allocate the expenses during the period they were incurred,
4 so an expense that was incurred before that new partner
5 entered, he would not be allowed the deduction for that
6 expense.

7 The Chairman. Would Treasury care to comment?

8 Mr. Chapoton. Yes, sir. That really is basically making
9 work what the Congress thought it did in 1976.

10 Mr. Brockway. The next item deals with contributions of
11 property to a partnership. You can contribute appreciated
12 property to a partnership where the taxpayer has a built-in
13 gain in the property--if he sold it, he would be taxable on
14 it--if he contributes that property to a partnership in a
15 tax-free exchange, then the partnership sells the property and
16 allocates the gain to other partners, so you can shift gain
17 to other partners. Also, you might have a situation where a
18 capital item to the individual partner contributes that to a
19 dealer partnership, and the partnership sells the item,
20 and if it is a loss item, converts a capital loss in the hands
21 of a partner into ordinary income by having the dealer
22 partnership sell it and then allocating the loss back to that
23 partner. This says that if you contribute appreciated or
24 depreciated property to a partnership, then the unrealized gain
25 or loss at the time you contributed is allocated to that

1 contributing partner and retains the character that it had in
2 the hands of the contributing partner, as long as that property
3 is sold within five years of the time that it was contributed
4 to prevent this either shifting of the gain or loss to other
5 partners, or the conversion of it from capital to ordinary,
6 or vice versa.

7 The Chairman. Again, if Treasury has any objection--.

8 Mr. Chapoton. Okay. I will just raise them, if we have
9 any concerns or comments, Senator.

10 The Chairman. But can it be assumed for the record that
11 where you do not raise objection that you support the proposal?

12 Mr. Chapoton. Yes, sir.

13 The Chairman. And I want to make it clear that we are no
14 at odds with the Administration.

15 Senator Danforth. The Administration does not feel that such
16 a proposal as the one just described is not a little bit on the
17 complex side?

18 Mr. Chapoton. Well, some of them are a little complex.
19 Actually, this one is probably not too complex, Senator, other
20 than the fact that any time you get into the partnership area,
21 you have complexity. Some of them are complex, yes.

22 Mr. Brockway. Under present law, you can elect to have
23 this treatment, and this was just to make that method that is
24 used in a number of situations mandatory.

25 The fourth item is avoidance of capitalization through

1 a special allocation, where you have a tax shelter partnership
2 and the expenses paid to a promoter would be a capital item and
3 not deductible to the investors, that to create a deduction
4 for it, instead of paying them a promotion fee, just
5 allocate them some of the income from the partnership, and
6 that reduces the other partner's taxable income, effectively
7 converting a capital item, a non-deductible item, into an
8 ordinary income deduction, and this would prevent any
9 avoidance in that area.

10 The next item deals with tax-free like kind exchanges,
11 and there are two proposals in that area. One is that under
12 present law, exchange of securities, stock, or other
13 securities do not qualify for like kind tax-free exchange
14 treatment, that has gained recognition if you exchange stock
15 or securities. You can, however, under present law exchange
16 partnership interests and get tax-free treatment on that. So
17 you could have a burned-out tax shelter where the
18 partnership was at that point generating taxable income in
19 excess of cash flow, could transfer that in exchange in a
20 tax-free exchange for another partnership interest where it
21 was generating excess tax losses, and do that on a tax-free
22 basis. And this would apply to transfers of partnership
23 interests the same rule that applies in the case of stock
24 or securities, that it would not qualify for tax-free
25 exchange treatment.

1 to the end of a tax shelter and to avoid paying the tax that
2 has been deferred, have a swap of the partnership interest.
3 When there is really intended an exchange of real property, it
4 usually is an exchange of the property itself, rather than the
5 partnership interest. We have been concerned about the
6 avoidance of the tax shelter recapture, when you can swap a
7 partnership interest and therefore defer or avoid altogether
8 the deferred tax.

9 Mr. Brockway. This proposal also would deal with
10 deferred like kind exchanges where you offered to exchange
11 some property for--rather than getting property in exchange,
12 you have the option to either get property or cash payment at
13 any point in the future, and what the proposal would say is
14 that you can qualify for like kind exchange property, but
15 you have to designate the property that you are to receive in
16 exchange at the time of the first transfer of the property, and
17 it has to be completed within a three-month period.

18 The sixth item deals with market discount on bonds
19 presently on market discount as opposed to original issue
20 discount. The gain recognized on that as the bond appreciates
21 is treated as capital in nature, so that you can buy a market
22 discount bond, borrow money, you deduct the interest to carry
23 the discounted bond against ordinary income as you pay it, and
24 you do not pay any tax on the market discount bond until you
25 sell it, and that that point it is capital gain. This would

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2 has been deferred, have a swap of the partnership interest.
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22 discount bond, borrow money, you deduct the interest to carry
23 the discounted bond against ordinary income as you pay it, and
24 you do not pay any tax on the market discount bond until you
25 sell it, and that that point it is capital gain. This would

1 say that the market discount bond and the sale would be
2 treated as ordinary income.

3 Senator Bentsen. Mr. Chairman, could we have the revenue
4 estimates as to what would be gained from each of these
5 specific items as we go along, so we can have some under-
6 standing of the significance of them?

7 The Chairman. Do you have that by item? I assume you
8 have.

9 Senator Bentsen. You have given us the gross amount, so
10 obviously you must have it by item.

11 The Chairman. Yes, they have it. Why don't you back up
12 and give us the revenues for the ones you have explained,
13 without explainin them again.

14 Mr. Brockway. At the moment, they do not total quite,
15 because of the rounding and certain other problems, but the
16 first special allocations, item allocations over the four-year
17 period would be about .8--

18 Senator Bentsen. Which one are you starting with, Number
19 1?

20 Mr. Brockway. This is Number 1. The next item dealing
21 with retroactive allocations--.

22 Senator Mitchell. What was that number?

23 Mr. Brockway. That is Number 1 of the tax shelter items,
24 is about .8, .8 billion over the four-year period.

25 The retroactive allocation item is about .2, that is

1 Number 2.

2 The third item, dealing with contributions of appreciated
3 property, is another .2 billion.

4 The fourth item, dealing with allocation of capital
5 expenditures, is roughly .3 billion.

6 Senator Chafee. These are all over four years?

7 Mr. Brockway. These are over the four-year period, that
8 is right.

9 Senator Mitchell. Mr. Chairman, could I ask why did we
10 do it over four years, since the budget resolution we are
11 dealing with is only over three years?

12 Mr. DeArment. The reason that we decided to move to a
13 four-year time frame is that on both the spending side and the
14 tax side, it was very difficult to get savings in 1984. When
15 you look at where we are, we are already partially through
16 fiscal year '84.

17 Senator Mitchell. But if what we are dealing with is
18 whether we are going to bring this to the floor on a
19 reconciliation bill, that will deal with only three years. So
20 just from the standpoint of our information, could we have the
21 numbers over the three-year period, so we will know exactly
22 how much deficit reduction we are getting on the reconciliation
23 package that we would be voting on?

24 The Chairman. Yes, we could provide that.

25 Mr. DeArment. In fact, we have the three-year total

1 numbers, if you look at the summary sheet.

2 The Chairman. Could I just interrupt for a minute.
3 Senator Stafford is Chairman of the Environment and Public
4 Works Committee, and apparently, he would like to take away
5 about six Members of this Committee for five minutes. I
6 wonder if you could meet at, say, 10:45?

7 Senator Stafford. That would be most agreeable, Mr.
8 Chairman.

9 The Chairman. If we have more than you have, maybe you
10 could just come in here and do it.

11 (Laughter.)

12 Senator Stafford. If you let us vote in your Committee,
13 we might consider it.

14 But Mr. Chairman, if you could recess for five minutes
15 at 10:45, and the Members of the Environment and Public Works
16 Committee who are here could come up to the other Committee,
17 we have eight of the Presidential nominees that I do not think
18 are controversial, and we would like to vote them out. We
19 can do it en banc if you would allow the members to come
20 up there.

21 The Chairman. Well, we always like to accommodate other
22 Members, so at 10:45, we will have a five-minute recess for
23 people to check their hearts and other things in here, and then
24 we will come back. I am not sure whether Bill Roth will let
25 us convene beyond 11:30. That is why we need to sort of move

1 through these. But I think it is a good idea to give the
2 revenue estimates.

3 Bill, are you going to let us meet beyond 11:30?

4 Senator Roth. Yes.

5 The Chairman. Okay. So we will have until noon, anyway.
6 There is no problem. We can go on until noon, and then we have
7 tuition tax credits.

8 All right, Dave, have you given Senator Bentsen and
9 others all the figures down through Number 6?

10 Senator Bentsen. No. You did not give Number 6.

11 Mr. Brockway. No, I did not. And unfortunately, Number
12 6, the like kind exchange, is \$1.4 billion.

13 Senator Bentsen. Do you mean Number 5?

14 Mr. Brockway. I am sorry. I have my numbers wrong.
15 Number 5 is 1.4--we had not gotten to that--the market
16 discount--

17 Senator Mitchell. And that is over four years?

18 Mr. Brockway. It turns out the numbers I was giving you
19 were the three-year numbers, so that solves that problem
20 quickly.

21 Senator Grassley. Go back to Number 5. I did not get
22 that.

23 Mr. Brockway. Number 5 is the like kind exchanges.
24 That is \$1.4 billion.

25 Senator Chafee. Now, these are all three years?

1 Senator Boren. Four years.

2 Senator Chafee. Oh, we have had a change?

3 The Chairman. Let me say in defense of the staff, they
4 have been going night and day for about eight days, so we
5 can correct these little details.

6 Senator Mitchell. Do you mean whether the revenue is
7 \$44 billion or \$74 billion?

8 The Chairman. No, that is a four-year number. That is
9 not a detail.

10 Buck, what kind of numbers do you have?

11 Mr. Chapoton. Three years--I take it the numbers he
12 is reading are three-year totals, Mr. Chairman.

13 Mr. Brockway. On the special allocation, what I gave you
14 there was a four-year number, and that should be--.

15 The Chairman. You see, these are permanent changes, too,
16 and the others are three-year proposals.

17 Mr. Brockway. On the first item, that was a .6 rather
18 than .8 on a three-year basis.

19 And finally, on market discount, which is Item Number 6,
20 that is a .2.

21 The next item deals with deduction for charitable
22 contributions of appreciated property. This would provide
23 basically that in the case of nonmarketable property that is
24 not marketed on an exchange, that you have to hold that
25 property for five years in order to deduct the fair market

1 value rather than your basis. This deals with basically the
2 contributions of gemstones to the Smithsonian and that type of
3 situation. It also provides in these situations that if you
4 hold it for more than five years, the over-valuation penalties
5 that you adopted in TEFRA would apply if there was a substan-
6 tial over-valuation of the deduction.

7 Senator Danforth. How much?

8 Mr. Brockway. That item is .3.

9 Senator Danforth. Now, Mr. Chairman this does not just
10 cover gemstones. Would this cover stock, gifts of stock?

11 Mr. Brockway. No, stock would not be covered under this
12 because that is tradeable on an organized securities market.

13 Senator Danforth. But if somebody wanted to give a
14 painting--.

15 Mr. Brockway. That would be affected by it. You would
16 have to hold the painting for five years in order to deduct
17 the fair market value, rather than the price that you paid
18 for the painting.

19 Senator Danforth. But then, if there is a revenue
20 savings of .3, the meaning of that .3 revenue savings would
21 be about \$600 million less in value of such objects would have
22 been contributed during this period of time to art museums?

23 Mr. Brockway. No. I think that \$600 million less worth
24 of deductions would be claimed. I mean, I think the problem is
25 that there is a lot of property contributed with substantial

1 over-valuations, and very high deductions are claimed. And
2 certainly, the gemstone is a very good case. But that, I
3 think, happens throughout. When you have property that is
4 not tradeable on an exchange where you have a market quotation,
5 it is very difficult to establish the prices, and it is very
6 difficult to audit that transaction.

7 Senator Moynihan. Mr. Chairman.

8 Mr. Chapoton. Mr. Chairman, if I could add, this proposal
9 was part of a two-part approach, Senator Danforth, that was
10 supported by the President's Commission on the Arts, and the
11 concern--our concern and their concern--was that people were
12 giving charity a bad name, if you will, by making gifts
13 immediately after acquiring the property and claiming an
14 inflated price. So they were perfectly willing to do something
15 about that.

16 But I would hasten to point out the other part of their
17 program, which we supported, was they were concerned about
18 diminution in charitable giving and wanted to raise the 50
19 percent of AGI limit to 75 percent, and that was part of the
20 two-part package to which we agreed. Now, the other part
21 costs money, costs more than this picks up.

22 Senator Moynihan. Mr. Chairman, could I speak to that?
23 When we last met, I mentioned the President's Committee on
24 Arts and Humanities and the proposed changes, and I think
25 there was kind of an exchange with Treasury, which endorsed

1 their proposals. The first was that you could go to an AGI of
2 75 percent, and the second was that you would extend over
3 15 years the excess of the AGI. Then, there was the third
4 provision, which was to hold things five years before you
5 contributed them.

6 Are we going to be able to consider those first two
7 proposals, which in a sense are the exchange--.

8 The Chairman. Well, there may be some way to modify
9 those. I think we are just trying to shut of subsidized
10 charity here.

11 Senator Moynihan. My point, Mr. Chairman, was that the
12 President's committee, of which Mrs. Reagan is the honorary
13 chairman--.

14 The Chairman. "Chair."

15 Senator Moynihan. It says so right here. We have got
16 to watch that. Okay.

17 (Laughter.)

18 Senator Moynihan. They would hope to have the three
19 together.

20 Mr. Chapoton. Yes, sir. That is why I wanted to point
21 out that it was part of--I said a two-pronged package--but
22 you are right, the third part was extending the five-year
23 period over to fifteen years, which we also supported.

24 Senator Moynihan. Yes. We might just note that.

25 The Chairman. Yes, let's see if we cannot work out a

1 bundle there--or package. I think we already worked out a
2 "bundle."

3 Okay.

4 Mr. Brockway. The next set of items are accounting
5 abuses that were also dealt with in the hearings in the
6 Oversight Subcommittee--.

7 The Chairman. These are the ones that Senator Grassley
8 had hearings on.

9 Mr. Brockway. That is correct, and these are--the first
10 proposal here deals with deferred payments that right now, where
11 you have an original issue discount loan, where the loan is in
12 exchange for receipt of cash or marketable securities, that you
13 have to accrue that using an economic accrual notion rather
14 than straight line. You have to use compounded interest to
15 determine when the interest deductions are accrued to the
16 borrower and when the income is included in the income of the
17 seller. These rules do not apply in the case of indebtedness,
18 original issue discount indebtedness where the indebtedness is
19 incurred in exchange for nonmarketable property. This would
20 apply the original issue discount rules also in that situation
21 and require an inclusion of interest and a deduction of
22 interest using the OID rules. However, these rules would not
23 apply to individuals in these transactions, but would only be
24 where there are non-individuals in those rules. Also, on the
25 present imputed interest rules where you have a deferred payment

1 sale, those rules are computed using straight-line interest
2 rather than an economic accrual, and the proposal would be
3 again to conform that and require economic accrual rules.
4 That total package would be a revenue item of \$1.7 billion
5 over the three years.

6 The Chairman. Now, you are talking about 1 through--.

7 Mr. Brockway. This is B-1.

8 The Chairman. Oh, just that one?

9 Mr. Brockway. Just that one, correct. The second part
10 of this is sort of the flipside, and that is where you have a
11 payment for a tax basis payor where you have a payment that
12 you prepay an expense that you really do not owe, or where
13 the service or goods, you are not going to receive until a
14 substantial period in the future, and you deduct it now,
15 even though you are not going to receive the service until a
16 later year so you can accelerate your deduction. This would
17 say that where the payment is for a property to be received
18 more than three months after the year and in excess of
19 \$10,000, that you could not deduct it until the period where
20 you received the property.

21 That item would be a .5 pickup.

22 Senator Bentsen. You would put a limit on that of
23 \$10,000. That would only apply above \$10,000 items; is that
24 right?

25 Mr. Brockway. Yes.

1 The Chairman. Would Treasury comment?

2 Mr. Chapoton. I think the more important question here is
3 the three-month period. You do not want to affect normal
4 transactions. You want to affect transactions where the
5 payment is made, but for tax avoidance, and therefore the
6 services are not to be performed or goods are not to be
7 received for some months.

8 Mr. Brockway. The next item on the list is interest-free
9 loans that at present--.

10 Senator Grassley. Would you wait just a minute in regard
11 to that one? How does it affect agriculture where you might
12 be paying for fertilizer or seed that would actually be not
13 received until, we will say in my State, planting time, and
14 putting the crop in, which would be in April, which would be
15 after the three-month period of time?

16 Mr. Chapoton. One it would catch is the cattle feeding
17 shelters, the cattle feeding tax shelter arrangement, where--.

18 Senator Grassley. But not the normal crops--.

19 Mr. Chapoton. Well, I think you would want to deal with
20 that in a three-month period. If that were not long enough
21 to cover normal transactions, you would want to extend the
22 three-month period.

23 What you are trying to prevent is major prepayments--.

24 Senator Grassley. I think it is just a matter of life
25 that if you were a good businessperson, you would be making

1 those decisions in the fall and could be paying for them then
2 or in the spring, but you actually would not be receiving the
3 goods until about the time to do the work in the field.

4 Senator Bentsen. The other thing is, you can get a
5 discount if you pay in advance that way, and whoever is
6 sellin the fertilizer and insecticide gives you' an
7 economic benefit for paying.

8 Mr. Brockway. One option we might look at is some
9 notion where if you actually are consuming the property
10 yourself in an active farming business, then some longer
11 period, as opposed to the cattle feeding shelters, for
12 example, where some limited partner is getting the accelcrated
13 deduction. That might be a way of trying to deal with the
14 farmer who actually does not receive delivery until spring
15 planting time, in the ordinary course of business.

16 Senator Bentsen. I really think you ought to give some
17 consideration to what the Senator is talking about on agricul-
18 ture, because that is a very common practice, and to be able
19 to pay it and take your discounts is very important to the
20 farmer.

21 Mr. Chapoton. And to lock in the price at that time.

22 Mr. Brockway. The next item deals with interest-free
23 loans. Under the present law, at least in the case of a
24 demand loan, it is possible for a parent to transfer income,
25 interest income, or other passive income, to--.

1 Senator Grassley. Where does this fit in to the case
2 before the courts now? There is something on appeal on this
3 right now.

4 Mr. Brockway. There is. This would provide a vehicle
5 for dealing with the situation of interest-free loans that
6 would provide fairly substantial de minimus exceptions and then
7 tax treatment where the interest-free loan is--.

8 Senator Grassley. Well, if we follow what you suggest
9 here, would that short-circuit the appeal?

10 Mr. Brockway. It would not, because this would only
11 apply on a prospective basis, and so that that case is
12 going to be decided on its own merits.

13 Senator Symms. What is the justification for the govern-
14 ment to make a decision--if somebody wants to loan money to
15 somebody interest-free, what justification does the government
16 have to intervene in it?

17 Mr. Brockway. Well, I do not think the intent here,
18 really, is to intervene, but the situation might be that if
19 the parent is in an upper income bracket, and obviously, the
20 child would be in a lower income bracket, what the parent could
21 do is make an interest-free loan to the child, and then the
22 child turns around and invests it. But it is a demand loan,
23 so the parent can get the principal back. What, effectively,
24 you have done is taken the passive income of the parent and
25 moved it on to the dependent's tax return, and obviously, then,

1 you go through the rate practice. Now, this would permit that
2 transaction, as long as the loan was less, on an average
3 daily basis throughout the year, less than \$10,000, and then
4 to the extent it was between \$10,000 and \$100,000 per
5 dependent, you would only have a tax to the parent to the
6 extent the child was getting an interest-free loan and
7 earnin some passive income with respect to that. So it would
8 allow the transaction to go forward, but in effect, treat it
9 as if there was a gift of the foregone interest and then the
10 interest payment back to the parent, which is the economics of
11 the transaction.

12 In addition, you have the situation where you might have
13 an employee who that you can transfer income--a compensation
14 employee or a shareholder--you might transfer dividends, in
15 effect, the economic equivalent of a dividend, through an
16 interest-free loan.

17 Mr. DeArment. So, for example, one of the areas of
18 concern, suppose a parent wants to loan a child \$20,000 so
19 that they can make a downpayment on a house. That would not
20 be put into passive income investments, and this proposal
21 would not affect it to the extent that the child does not have
22 passive income.

23 Mr. Brockway. It is sort of a backstop to the traditional
24 assignment of income notions. This rule is presently the
25 law in the case of term loans, but in the demand loan case,

1 there is some case law that would support the notion that you
2 can enter into these transactions and avoid any consequences,
3 even though you were making an economic benefit transfer to
4 the borrower.

5 Mr. Chapoton. Senator, if I might say, people have
6 just woken up to the fact that the tax results of either a
7 gift or compensation can be changed if you do not actually
8 transfer the money, but you transfer it in the guise of an
9 interest-free loan. So that the intent of this is to stop
10 that transaction, but not to stop a family, intra-family
11 loan, for a purpose other than transferring income to a lower
12 bracket, with no gift tax and the income tax savings. So if
13 you made a loan for tuition, for a house, for a car, it would
14 not be affected, but the others would be.

15 Senator Symms. Well, thank you. If I could just ask one
16 more question, Mr. Chairman, in accord with what you just
17 said, then, Buck, on point (b) back on the first page, where we
18 went by the contingent revenue increases, if you have a sur-
19 charge, then, of 2 percent imposed on taxes over \$6,300,
20 and 5 percent on taxes over 22 percent, then you compound--you
21 are really working against yourself. If you want to accomplish
22 what you were just talking about here, to avoid the
23 interest-free loans, then you would have to say that the
24 surcharge just makes the incentive for people to try to
25 look for places' to do that.

1 Mr. Chapoton. No doubt about it, when tax rates go up,
2 people search for ways to transfer income to lower-bracket-re-
3 lated parties.

4 Senator Heinz. Mr. Chairman.

5 The Chairman. Senator Heinz.

6 Senator Heinz. Thank you.

7 Buck, we may well want to do some--we may want to do all--
8 of these, but these come under the title here, "Accounting
9 Abuses," at page 3 and 4, the six items here. How many of
10 these could be done by the Treasury Department administratively?

11 Mr. Chapoton. I think none of them. These are concerns
12 that if we had been able to take care of them, we would have.
13 The interest-free loan is a good case. We have been wrestling
14 with that and have not been able to do anything about it.
15 The cases are being litigated, but we have not been successful.

16 Senator Heinz. Well, the Treasury Department's position,
17 I assume, in that instance is you do have the authority to do
18 something about it, someone is disagreeing with you, and you
19 are in court; is that correct?

20 Mr. Chapoton. I think that is correct. In the income
21 tax area, that is definitely correct. And the gift tax case,
22 as we pointed out earlier, is now on appeal to the Supreme
23 Court.

24 Senator Heinz. But just so I understand the Treasury
25 position with respect to these, are there any where you have

1 not asserted that you do not have the authority to make the
2 necessary changes?

3 Mr. Chapoton. There might be, Senator. One was just
4 suggested to me. One of the rules is the imputed interest in
5 general transactions, not related party transactions. It is
6 now simple interest. This would provide that it would be
7 compounded interest imputed. I think we probably could
8 do that by regulation, though I would be very reluctant to do
9 so without the blessing of Congress at this late stage.

10 Senator Heinz. I may have mis-asked my question, or you
11 may have misunderstood it. Is my understanding correct,
12 though, that the Treasury Department has asserted in each of
13 these six instances at some point that you do have the
14 authority to make these changes?

15 Mr. Chapoton. No.

16 Senator Heinz. No.

17 Mr. Chapoton. We have not asserted that.

18 Senator Heinz. But you have asserted that with respect to
19 interest-free loans.

20 Mr. Chapoton. With respect to interest-free loans, that
21 is correct. We have taken the position in certain factual
22 situations--.

23 Senator Heinz. But in no other instance of these six
24 here have you taken that position?

25 Mr. Chapoton. It might be, Senator. I would have to go

1 back through them.

2 Senator Heinz. Well, would you please find out for us?

3 Mr. Chapoton. Okay.

4 Senator Heinz. I need to know where you have asserted
5 that you do have the authority to make any of these changes under
6 current law.

7 Mr. Chapoton. And whether that assertion has been rejected
8 or not--.

9 Senator Heinz. And the status of that assertion; that is
10 right.

11 Mr. Chapoton. Okay.

12 The Chairman. I think that would helpful. I think the
13 point is, though, if we are going to have a tax package--and
14 we have had hearings on these loophole areas--the most painless
15 thing for us to do is to make certain we close some of these.
16 There are going to be modifications, without question. That is
17 why we wanted the Members to have access. And I think it is
18 no secret these have been out, have been discussed and kicked
19 around ever since the hearing.

20 Senator Bentsen?

21 Senator Bentsen. Mr. Chairman, could you give us the
22 values on 2 and 3?

23 Mr. Brockway. The interest-free loan, which is Number 3,
24 is .3, and the prepayment item, Number 2, is .5.

25 Senator Bentsen. And what was 1?

1 Mr. Brockway. That was 1.7.

2 The Chairman. Okay, let's try to move on. We are going
3 to have difficulty finishing everything if we do not move a
4 little faster.

5 Mr. Brockway. The next item deals with related party
6 transactions when you have--.

7 Senator Moynihan. Mr. Chairman, would you mind--.

8 The Chairman. Oh, yes, I guess I had agreed to a five-
9 minute recess--so just leave your proxy, and you do not have
10 to come back at all.

11 (Laughter.)

12 The Chairman. We will be in recess for five minutes.

13 (Short recess.)

14 The Chairman. Now, as I understand, we want to go
15 through the balance of these proposals, and then you have
16 another package that the Members have an interest in. I
17 think on those, we could just distribute those to Members, and
18 if they have any questions on those, they could be raised
19 tomorrow morning.

20 What we would like to do is to go through all the
21 revenue provisions, and then this afternoon, have Joint
22 Committee staff, Treasury, our own staff on each side, meet
23 with Members' staff to further go over these, and then maybe
24 later today, we can get back together as a Committee. But we
25 still need to go over the spending restraints in addition. So

1 I would hope we could just go through these--you are still in
2 the accounting area--finish those, and then we will speak
3 briefly about the Members' add-ons, and then move on to the
4 spending.

5 Senator Baucus. Mr. Chairman, when do you expect to do
6 spending, then?

7 The Chairman. I hope by 11:30.

8 Senator Mitchell. Mr. Chairman, should we have our staff
9 at that meeting, or should our staff be meeting with all the
10 lobbyists who will be affected by each of these provisions?

11 The Chairman. Well, I assume the lobbyists will be
12 available.

13 (Laughter.)

14 The Chairman. I mean, I am sure that they are all here,
15 public-spirited, wanting to reduce the deficit. Most of them
16 have told me that--but not in their area.

17 (Laughter.)

18 Senator Boren. Mr. Chairman, I wonder, because of floor
19 action and some other action on the natural gas bill, I may not
20 be able to be here through all of the presentation. Has Mr.
21 Chapoton indicated yet whether or not the Administration
22 supports the broad outline of the tax increases that have
23 been proposed, because as you know, I had the distinct
24 feeling, which led me to go on to other business that I could
25 conduct, from the Secretary of Treasury last week, that the

1 Administration opposed a tax increase package like that, and I
2 just wondered, do they endorse the \$74 billion of tax
3 increases in this package?

4 Mr. Chapoton. Senator Boren, I think our position is
5 unchanged from that as stated by the Secretary last week--that
6 is, that we want to see the spending cuts before the taxes.
7 I think the Chairman is attempting to address that problem by
8 making the taxes contingent upon the spending cuts being in
9 place. We have not addressed that approach of this bill.

10 The Chairman. I might say to the Senator from Oklahoma
11 earlier, I indicated as we went through the list, that with
12 one or two exceptions, every one of these measures were at
13 least recommended in some form by the Administration, of course,
14 being contingent on spending restraint.

15 So I think we could probably play that game forever,
16 whether Tip O'Neill is onboard, or Howard Baker, or the
17 President, but I would hope that the Committee can at least
18 indicate our support for deficit reduction before we leave
19 here this week. It would be my hope that if we could do it
20 tomorrow, we might still have a chance to put it on
21 reconciliation.

22 Senator Mitchell. Mr. Chairman, could I follow up
23 on a question, just so I understand what Mr. Chapoton said
24 explicitly.

25 What you just said was that notwithstanding the fact that

1 in his budget, the President proposed tax increases of \$59
2 billion, \$46 billion of which was contingent upon spending
3 increases and \$13 billion of which was not contingent in any
4 way--

5 Mr. Chapoton. That is correct.

6 Senator Mitchell. --notwithstanding that--and Senator
7 Dole has attempted to address this by proposing a package of
8 revenue increases that are contingent upon achieving spending
9 cuts, that you still are not prepared to say that you will
10 support these tax increases if enacted as part of a package
11 that makes them contingent upon the spending cuts proposed
12 here.

13 Mr. Chapoton. No, I am not prepared to say that, Senator
14 Mitchell. The question is--the President's proposal was
15 tax increases contingent upon spending cuts as proposed by the
16 President--or along the lines. I do not think it had to be
17 item for item, but it was in the nature of the President's
18 proposals. And that has been a matter of some discussion,
19 what would the nature of these spending cuts be as compared
20 to the President's proposal. That would be one aspect of it.

21 The other aspect is whether the cuts are, in fact,
22 obtained. I think there is considerable concern at our end
23 of the street on whether spending cuts are real or not, and
24 that is a matter of what baseline you are using.

25 So those have to be analyzed by us before we could support

1 the tax increase.

2 Senator Mitchell. So you are saying that you do not
3 support this effort. Let me go one step further. You
4 are aware of the spending reductions that are proposed. They
5 are before you in printed material distributed by the Committee
6 at the Chairman's request. With that knowledge, then, do
7 you oppose this effort?

8 Mr. Chapoton. Senator, I am simply not able to say. I
9 think there has been discussion of this problem, a lot of
10 discussion of the spending area in the Administration, but the
11 Administration has not taken a position on whether these types
12 of spending restraints meet the conditions of the President's
13 original budget, and that is the question.

14 Senator Mitchell. You are aware, are you not, Mr.
15 Chapoton, that the Majority Leader and the Speaker have
16 established as a target for Congress to include the present
17 Session as of this Friday?

18 Mr. Chapoton. Yes, sir.

19 Senator Mitchell. And so in effect what you are saying
20 is that you do not know what the answer is, which means that
21 you are not at any point prior to then, or in time for some
22 meaningful action, as the Chairman is trying to accomplish,
23 going to take a position on this.

24 Mr. Chapoton. In all candor, if the Congress adjourns on
25 Friday, I would doubt that there would be a position on it by

1 then.

2 The Chairman. But let me say--I do not think Mr. Chapoton
3 --he is a very good person, but he is not the one who is going
4 to make the final decision--and he is probably thankful for
5 that--but I think we are making progress. I am an optimist.
6 I see a lot of indications around this town that other people
7 are looking at deficit reduction, and I think as long as this
8 Committee is pushing or pulling, whichever, I think we are
9 finally going to end up with some resolution. What I do not
10 want is to have to go to the floor and have the Budget
11 Committee take over the responsibilities of this Committee--and
12 I did not vote for the budget resolution, but here is a chance,
13 if you want to really vote for taxes, you may get a chance
14 before noon. There is \$57 billion, and they do not even have
15 the provisions drafted yet. I mean, I do not know how they
16 are going to offer them.

17 Senator Mitchell. Well, I just want to say, Mr. Chairman,
18 that as you know, I respect and admire what you are doing, but
19 for you to say that you are an optimist has got to be the
20 understatement of the year. The President has said "No"; the
21 Secretary of Treasury has said "No"; and now--

22 The Chairman. And the Speaker has said "No".

23 Senator Mitchell. Yes, the Speaker has said "No." And
24 what is your title, Mr. Chapoton?

25 Mr. Chapoton. I am an Assistant Secretary right now.

1 Senator Mitchell. And now, the Assistant Secretary of
2 Treasury has said "No."

3 (Laughter.)

4 Senator Mitchell. If they are not going to be the ones to
5 make the final decision, who are you referring to when you say
6 we have not heard from the person who is going to make the
7 final decision?

8 The Chairman. Well, there are a lot of ways to
9 interpret "No"--

10 (Laughter.)

11 The Chairman. --and I have listed all three of those as
12 "Undecided."

13 Okay--and Bill Roth is coming around, too.

14 (Laughter.)

15 Senator Roth. Mr. Chairman, I think I have been around
16 this circle several times. I would like to ask the Assistant
17 Secretary a few questions myself. Now, over the next three
18 years, as I understand this proposal, we have roughly \$20
19 billion worth of theoretical cuts between 1984 and 1986; is
20 that correct?

21 Mr. Chapoton. According to the sheet handed out, yes,
22 sir.

23 Senator Roth. Isn't it correct that the Congressional
24 budget resolution increased spending by roughly \$32 billion
25 over that three-year period?

1 Mr. Chapoton. Senator, I do not have that figure before
2 me, but it did increase domestic spending. I think, as I
3 recall, that is correct.

4 Senator Roth. Over the present figure. So that if you
5 take these figures here and assume that they are real cuts--and
6 I will address that later--what you are really doing is not
7 cutting spending, but you are merely reducing the rate of
8 growth that was voted upon in the initial budget resolution;
9 isn't that correct? You said you think that is correct, \$32
10 billion increased spending. This proposes something like
11 \$20 billion in tax cuts--I mean, in spending reductions.

12 Mr. Chapoton. Yes, sir, I think that is correct. I
13 have to say, Senator, as I think you know, that I spend my
14 time on the income side, not the outlay side.

15 Senator Roth. Let me ask you this question. Assuming
16 those figures are correct--and I understand you do not know
17 it--is that really a spending cut?

18 Mr. Chapoton. If these cuts are from the Congressional
19 budget resolution, they would not be spending cuts, no, and I
20 have made that point to the staff, and I think to the Chairman,
21 that the cuts would have to be from baseline before they
22 would be real cuts.

23 Senator Roth. Now, isn't it true that the President has
24 said that he is not going to consider anything unless they are
25 real spending cuts?

1 Mr. Chapoton. That is correct. We have said that, and the
2 President has said that, yes, sir.

3 Senator Roth. Now, let me ask you this question. We
4 show over that three-year period something like an 8.3 savings
5 in health. How much will those health programs actually
6 increase, or are projected to increase, over the next three-year
7 period?

8 Mr. Chapoton. I do not have that figure, but--.

9 The Chairman. I think the next group will have that,
10 Bill, when we get into the--.

11 Mr. Chapoton. I am afraid you need to address that,
12 Senator, to the--.

13 Senator Roth. Well, I would just like to make the obser-
14 vation. I think that the projections from the CBO, that
15 those health programs are going to double--are going to
16 double--in the next three years, and I just do not--the point
17 I want to make is I do not see where this package is really
18 concerned about deficits and the impact it is having on our
19 economy. You have really got to address spending, the
20 spending side. And would you agree the only way--

21 Mr. Chapoton. Yes, sir, we agree with that, definitely,
22 and I think you are making a very important point, Senator,
23 and that is the point I tried to make a minute ago, that
24 one of the aspects when you talk about the contingent taxes
25 is whether the spending is real, is in place--that is, whether

1 it is enacted, that is one aspect, and two, whether it is the
2 type of spending cuts the President wants--that is the second
3 question--and the third question is whether it is a cut from
4 baseline--and by "baseline," I mean present level of
5 services. The Congressional budget resolution in many of
6 these areas would call for increased services and therefore
7 increased spending. That would not be a cut if you cut from
8 the Congressional budget resolution increased spending.

9 Senator Roth. Well, I would just like to conclude,
10 because I know the Chairman does want to move on. But in the
11 contingency proposed by the President, that was based on that
12 taxes would only go in if we reduced the deficit to a certain
13 percentage of gross national product, isn't that correct?

14 Mr. Chapoton. It would go in only if the spending
15 reductions were made in line with the President's budget
16 and in spite of that fact, that on July 1 of 1985, the fiscal
17 '86 projected deficit exceeded 2-1/2 percent of GNP.

18 Senator Roth. And it is not the equivalent to argue
19 that if we take the Congressional budget resolution, which
20 is higher, means real savings?

21 Mr. Chapoton. If you cut from the Congressional
22 budget resolution, it does not mean real savings, no.

23 Senator Symms. Would the Senator yield?

24 Mr. DeArment. Buck, it makes a difference when you are
25 talking about the Congressional budget resolution. The

1 Congressional budget resolution has a current services baseline
2 and then it has the budget resolution projected spending. The
3 Congressional budget resolution's current services baseline
4 is very similar to the CBO baseline. It differs from the
5 Administration's current services baseline in that the Admini-
6 stration's is fattened up on the defense side as a projection
7 of current services.

8 Otherwise, measured on a current services basis, they are
9 somewhat similar, other than--.

10 Mr. Chapoton. When I think of the Congressional budget
11 resolution, I think of the budgeted outlays for the future
12 years. Current services is where the starting point ought to
13 be for both of us when we look at spending cuts.

14 Senator Roth. That is where we are proposing to measure
15 these from, not from the--.

16 Mr. DeArment. We are measruing from the current
17 services--.

18 The Chairman. That is what you have done, isn't it?

19 Mr. DeArment. That is correct.

20 The Chairman. Senator Moynihan?

21 Senator Moynihan. Thank you, Mr. Chairman.

22 Just at the risk of repeating what I said before, could I
23 ask Mr. Chapoton, for whom this Committee has very great
24 respect, as he knows, and these are not adversarial
25 questions, but I would like to get the record straight here--in

1 the first 1,000 days of this Administration, you have added, I
2 believe, \$457 billion to the national debt, plus or minus.
3 Would that not be the case?

4 Mr. Chapoton. Senator, the deficit has risen by approxi-
5 mately that amount, I think that is correct. But let me take
6 exception to the "you have added" label. I think the
7 Administration deplores deficits as much as the Members of
8 this Committee and the Members of the Senate do. The
9 disagreement or the concern on our part is that the deficit
10 problem should be addressed on the spending side.

11 Senator Moynihan. I would make the point that it took
12 from Alexander Hamilton to Donald Regan to get to \$970
13 billion in debt, plus or minus, and in 1,000 days, you have
14 gone halfway farther again. I mean, in 2,000 days, you
15 would double what took 200 years--at this rate.

16 Mr. Chapoton. That is correct, and that is a major
17 concern.

18 Senator Moynihan. And is it not the case, sir, that at
19 this moment, the Federal budget, Federal outlays, as a
20 proportion of gross national product, are the highest they
21 have ever been since the Second World War?

22 Mr. Chapoton. That is correct.

23 Senator Moynihan. They are the highest they have ever
24 been. So we have the biggest government we have ever had,
25 and the biggest incursion of debt. And would it not be the case

1 that also, apart from the Second World War, the deficit is the
2 highest proportion of GNP we have known?

3 Mr. Chapoton. That is also correct.

4 Senator Moynihan. Well, I know it is in no way any
5 of your doing, but you have added more debt than any Administra-
6 tion in history; you have the largest government in any
7 Administration in history, save World War II, and you have
8 the highest deficit. And is it not the case that at some
9 level, those of us who keep hearing about spending having to
10 be cut back from baseline are not irrational in our estimate
11 that there has been an anticipation that this kind of crisis
12 would arise?

13 I do not ask you to answer that, sir. It is not a fair
14 question. But I say to my friends opposite that this crisis
15 has been created, and until some measure of acknowledgement
16 on that score comes forward, we are not going to find the
17 progress we need.

18 Senator Danforth. Who would you like to acknowledge it?

19 Senator Moynihan. Sir?

20 Senator Danforth. Who would you like to make the
21 acknowledgement?

22 Senator Moynihan. I would take any two--

23 Senator Danforth. Would you take it from me?

24 Senator Moynihan. With more than normal respect, because
25 you know the respect in which I hold you.

1 Senator Danforth. I will be happy to acknowledge it, that
2 during this Administration the national debt will have increased
3 by 79 percent. This Administration is going nowhere right
4 now in dealing with the deficit. My hope is that they will
5 come around. I am not in any great hurry to leave here.

6 Senator Moynihan. And may I say I think you are right.

7 Senator Danforth. I think this business about people
8 saying, "Well, we only have one thing that we should do, and
9 that is increase the debt ceiling, and that is all, and then
10 we should go on a vacation for more than two months," I think
11 that that is unconscionable. And I think before we extend the
12 debt ceiling, we should do something about getting the
13 deficit under control.

14 I voted to extend the debt ceiling. I was one of the 39
15 who fell on that sword. I have always voted to extend the debt
16 ceiling.

17 Senator Moynihan. As was your friend from New York.

18 Senator Danforth. I am not going to do it again. I am
19 not going to vote "Yea" on the motion to reconsider, and I would
20 urge others not to either, until we have something by way of
21 progress--even if we fail--some attempt, at least, that is
22 meaningful, on the floor of the United States Senate to
23 reduce the deficit. And I am not hard to satisfy. Any
24 reasonable proposition, I would be willing to listen to, but
25 what I will not listen to is silence. And that is exactly what

1 we have gotten from the Administration. We have had
2 silence on the question of the deficit. This is President
3 Reagan's deficit, and it does not do for him to blame the
4 Congress. We in the Congress are busily blaming the
5 President and saying, "We cannot do anything without the
6 President." The President is busily blaming us and saying
7 that it is all the fault of Congress.

8 The buck stops nowhere around here. We are shipping it
9 back and forth the length of Pennsylvania Avenue, with the
10 speed of light. And I would hope--this is kind of a leisurely
11 proceeding this morning, I am sorry to say, but I am more
12 leisurely with respect to the debt ceiling extension than
13 anybody could be with respect to reconciliation.

14 So my hope is that there is still time to act and that
15 we will be able to regain in this Committee the leadership
16 which we were assuming two weeks ago. It was a remarkable
17 spirit in this Committee, remarkable--bipartisan. I would say
18 more than half of the Democrats were joining maybe eight
19 of the Republicans to do something meaningful and tough
20 with respect to the size of the deficit, and then the President,
21 through the Secretary of the Treasury, did everything he could
22 to throw cold water on our efforts. And it is my hope that
23 despite that, we will regain the leadership which we had two
24 weeks ago. It is my hope that the time is not too late. But
25 I would say to the Administration that as far as this Senator

1 is concerned, if you really believe that it is urgent to
2 extend the debt ceiling, we had better do something about this
3 deficit before we extend the debt ceiling.

4 The Chairman. Senator Symms.

5 Senator Symms. Well, Mr. Chairman, I would just like
6 to make one real very quick point, and will not belabor your
7 progress here this morning, but I think it is well and good
8 what my colleagues from New York and Missouri are mentioning
9 here, but the problem with it is that in reality, there has
10 been nothing suggested to change the rate of spending of the
11 Federal government, and until the rate of spending is
12 changed dramatically, you cannot raise taxes fast enough to
13 cover up the rate we are spending money. And we went through
14 this kind of nickel-and-dime thing with TEFRA, and what we got
15 was a \$100 billion more deficit as a result of it. We did not
16 get those spending cuts that we were supposed to get.

17 And the problem--and I think the President is correct
18 in blaming the Congress, and the Congress to some degree can
19 be correct in blaming the President, in my opinion, because
20 there is enough blame to go around in this town for all parties
21 of how we got in this mess we are in--but the fact is that
22 for years and years and years here in Washington, people
23 have been buying votes with somebody else's money, and we have
24 got ourselves in the situation where 44 percent of the
25 budget, for example, goes to senior citizens programs. Nobody

1 wants to touch it. Tip O'Neill doesn't want to touch it--.

2 Senator Boren. Will the Senator yield at that point?

3 Senator Symms. I would be happy to yield.

4 Senator Boren. I have heard this three-for-one number
5 thrown around a variety of places. Where was this agreed to
6 by the United States Senate?

7 Senator Symms. I do not think I just mentioned the
8 three-for-one number, but I think we were supposed to, in the
9 budget reconciliation of 1982, get a three-for-one--.

10 Senator Boren. Where did it say that?

11 Senator Grassley. Senator Dole, in his opening statement
12 on the floor on TEFRA referred to 76 percent of the package
13 coming from tax increases.

14 Senator Boren. Where did it say that in arriving at the
15 bill that we voted on?

16 Senator Grassley. Well, the Chairman said--.

17 Senator Boren. It did not say it anywhere. This has
18 been one of the numbers that has floated around in the last
19 year that has not been based in any kind of reality, and I
20 think that to argue that therefore we have to cut deeper in
21 spending because of some agreement is ridiculous.

22 Senator Symms. I think, Bill, the point that you bring
23 up is really not relevant to the point I am making. We still--.

24 Senator Boren. You do not think we should cut spending
25 three dollars for every dollar we raise taxes?

1 Senator Symms. I think we should cut spending right now
2 enough to get the budget and the income--.

3 Senator Boren. But does anybody else agree with you on the
4 three-for-one figure? I do not see anybody rallying to your
5 position.

6 Senator Symms. I did not say three-for-one. When did I
7 say it? I did not say it here this morning. My point that I
8 want to make is that we voted for TEFRA a year ago, or a little
9 over a year ago, with the intention that it was going to be a
10 budget reduction program, but there was no spending reform.
11 There is no rate of spending reform. These programs are
12 still going right on their merry way. So the game is
13 played. We reduce spending, but we reduce spending from a
14 projection of higher spending, so there is no real reduction
15 in any program. Everything, instead of growing 18 percent, is
16 growing 15 percent. And I think until the Congress is willing
17 to come to grips with that and the Administration, we are
18 wasting our time.

19 Senator Bentsen. Mr. Chairman, I have been asking for
20 recognition.

21 The Chairman. Senator Bentsen.

22 Senator Bentsen. Mr. Chairman, I want to congratulate
23 Senator Danforth on a highly responsible statement. I want to
24 say I have never been as deeply concerned about the economic
25 future of my country. And to see these kinds of deficits

1 compounding themselves, one on top of another, and talking
2 about one that will be in excess of \$280 billion in 1989, to
3 see a situation where we would again double the national
4 debt, and to have a Secretary of the Treasury come before us--I
5 am not speaking about you, Mr. Chapoton; I am talking about the
6 Secretary of the Treasury--and when we talk to him about
7 cutting spending and raising taxes, and he says, "Well, we are
8 for standby taxes, but not until 1985," and I said, "Well, if
9 the problem is now, then why don't we deal with it now?" and
10 he said, "Because 1984 is an election year--need I say more?"
11 Absolutely more should be said. We ought to respond to the
12 problem now.

13 I congratulate the Chairman on trying to approach this
14 problem, but I would also say in trying to achieve these kinds
15 of sums and make this kind of progress in the last couple of
16 days of a session will lead to some things that will be
17 unanticipated and is not the way we should be passing major
18 tax legislation, and I am quite prepared to stay here--and I
19 much prefer Texas--but I am ready to stay here, if that is
20 what it takes to try to address this problem. But this is
21 something that should be shared by a President of the United
22 States. He cannot sit behind those doors and say, "Bring me
23 the completed package." It reminds me of the fellow who,
24 when they were storming the gates of the Bastille, and the
25 crowd surged by, he said, "I must follow them because I am

1 their leader."

2 You have got to get out front on these things and be a
3 part of the process, and the President should be a part of it.
4 And if we are ready to put ourselves on the line, he should be
5 right there with us, and we should approach this in a responsi-
6 ble manner, and we ought to stay here and get the job done.

7 The Chairman. Senator Chafee?

8 Senator Chafee. Well, Mr. Chairman, I agree with much
9 that has been said here this morning, and it seems to me that
10 we have gotten the President's position outlined. We wish he
11 would take the leadership in this. We wish the Speaker would
12 jump into it, but apparently, neither will. So therefore, it
13 seems to me, Mr. Chairman, that it is up to us, as we talked
14 about three weeks ago, we said we were going to tackle this
15 problem. And I hope we will. I hope that you, Mr. Chairman,
16 will continue your leadership of this Committee and that we
17 will proceed--I do not think we are going home Friday. I think
18 we are going to adjourn and come back on the 29th. And even if
19 we do adjourn Friday, I think if we have taken some significant
20 steps here, it will be a major signal to the nation.

21 So therefore, fine, if everybody else came along and
22 helped, but apparently they are not, so it is down to us. And
23 I hope we will do it, and I hope we will do something, whether
24 it is spending cuts or tax increases--I do not care. I will
25 vote for either of them. But I think the proposal of a

1 balance between the two that has been suggested around here
2 makes a lot of sense--half and half. That seems to bring
3 everybody aboard, hopefully, although we have some people in
4 this Committee and in the Senate who will not budge a bit.
5 It has got to be all taxes, it has got to be all spending
6 cuts. It seems to me we ought to find a common ground, and
7 perhaps half and half is the way, so that we can get on with
8 this program and send a signal and do something.

9 The Chairman. Senator Pryor?

10 Senator Pryor. Mr. Chairman, I would like to ask Mr.
11 Chapoton this question, and that is, if we get to the point,
12 let us say, Friday, on the debt ceiling increase, and some
13 Member of this Committee or the Chairman or myself, or
14 Senator Symms, anyone else, would take the President's budget
15 that he submitted to the Congress and merely attach that
16 budget as an amendment to the debt ceiling legislation, would
17 the President support that?

18 Mr. Chapoton. Well, I think unquestionably, he would,
19 Senator Pryor. I think at this point, you have a--I am not sure
20 how that would work out in all the details, because things
21 have happened since the budget was presented--but certainly, he
22 is standing by not only the spending side of that, but the
23 contingency taxes, and I think the Secretary made that clear.

24 Senator Pryor. Now, should such a proposal be made, and
25 assuming that the Congress would adopt the President's budget,

1 what would that do to the deficit?

2 Mr. Chapoton. Well, it would reduce--under the
3 assumptions of the mid-Session review, it would reduce the
4 deficit next year to about \$175 billion. It would trim down
5 to about the \$80 billion, \$75 billion range for 1988. I do
6 not have the figures before me.

7 Senator Pryor. I am just trying to see if there is any
8 way we can extract from the Department of the Treasury any
9 solution or any point of starting where the President might
10 cooperate with the Congress and this Committee in this matter.
11 That is the purpose of this question.

12 Mr. Chapoton. Well, I appreciate the frustration of the
13 Committee on cooperation in this effort. I think the
14 Secretary did make clear that the President is not backing away
15 from a standby tax, and indeed, that has been and is the
16 position of the Administration. The frustration, I think, that
17 is being felt here is what spending cuts would be acceptable
18 to the Administration so that we would support a tax, even on
19 a contingent basis. And I do not have the specific answer for
20 you on that. I think it is certainly a reasonable question, and
21 we have not addressed it in any detail since the original
22 budget proposals were made. As I say, I appreciate the
23 frustration of the Committee, though I can say unqualifiedly,
24 we are still supporting a contingency tax along the lines
25 we proposed.

1 Senator Pryor. Mr. Chairman, one final question to my
2 friend from Idaho, Senator Symms. You talk about spending
3 cuts. I wonder if our friend is willing to make significant
4 cuts; if so, how much, in the Department of Defense.

5 Senator Symms. Well, I think certainly that if you attack
6 the rate of spending on entitlement spending programs, many
7 of those are in the Defense.

8 Senator Pryor. I am not talking about entitlements. I
9 am talking about the Department of Defense.

10 Senator Symms. Well, the pension programs are in
11 Defense, for example; pay scales are in Defense. And yes, I
12 think Defense would have to take some cuts.

13 Senator Pryor. What amount?

14 Senator Symms. Well, I am not sure I could give you a
15 number right now, but I think that just to go out here and
16 chop out, say, an appropriation for buying a new tank or
17 something like that, that does not affect the long-term--if
18 you cut \$1 billion out of the Defense Department, that is not
19 like changing the rate of spending on a long-term pension
20 program where you get the benefit of it year after year
21 after year, and that is what is wrong with the budget here.
22 Nobody wants to really talk about what the problem is.

23 I did not vote for it, and did not support it, as Members
24 of the Committee know, but the Social Security reform that the
25 President and Tip O'Neill signed onto, nobody wants to touch

1 that now. I have heard the President say he will not touch it,
2 and Tip O'Neill says he will not touch it, so it is like that
3 is set aside. That is where the big dollars are going, is in
4 all these programs that are built into the system. And until
5 we are willing to attack that, we can cut a few billion out
6 of Defense, but it will not make any real savings in the long-
7 term, because if you cut out \$25 or \$30 billion out of
8 Defense, you would still have a \$175 billion deficit, and you
9 would just have a military that did not have spare parts,
10 did not have fuel, did not have tanks and trucks and so forth,
11 and that is the problem.

12 Senator Pryor. Thank you, Mr. Chairman.

13 The Chairman. Well, I am encouraged by this discussion.
14 I think it indicates that there is still some hope.

15 Senator Pryor. Mr. Chairman, you are an optimist.

16 The Chairman. I really believe that--I understand the
17 politics of it, and I understand that it is easy for this side
18 to say, "Well, where is the President?" and we can say, "Well,
19 where is the Speaker?" I think our responsibility is much
20 greater than that. I think we have to do what we can to lead
21 the way, and I intend to have a vote tomorrow to find out
22 who wants to cut the deficit and who does not want to cut the
23 deficit. And maybe this package is not perfect, but we had
24 a vote here about a month ago, 13 to 0, that we ought to do
25 something. And on that basis, it would seem to me we ought

1 to try it. Now, if we fail, then we will try again, but--.

2 Senator Mitchell. Mr. Chairman, I thought the vote was
3 we ought to try to do something.

4 The Chairman. Well, I know, and that is like voting on
5 the budget resolution. Now we see what awful things they
6 propose, when they get down to specifics, and I bet this
7 does not pass. We will see how many people who voted for the
8 budget resolution are going to vote for \$57 billion in taxes.

9 So we are dealing with the real thing in this Committee,
10 and I am not discouraged a bit. And I still believe there is
11 some hope for the Administration.

12 Senator Baucus.

13 Senator Baucus. Mr. Chairman, I would like to add just
14 another element to all this. Personally, it is with a little
15 bit of a sense of disappointment in these figures, because
16 they back off significantly from where we were up until
17 this morning. That is, we are talking in the neighborhood of
18 \$150 billion deficit reduction over three years--.

19 The Chairman. Four years, yes.

20 Senator Baucus. As I read these figures, we are backing
21 off very significantly from that. And I know the dilemma you
22 are in. If you are too daring, too bold, you start to cause
23 a lot of problems, and people begin to back off. On the other
24 hand, I think we have to be daring and bold to get some
25 momentum. And I frankly encourage you during these next hours

1 --maybe next days--to try to figure out ways of working with
2 other Members of this Committee to regain some of that daring,
3 some of that boldness that we were engaging in before, because
4 I think if we back off this much, as I read these figures--I do
5 not have the right totals here, perhaps--but as I look at the
6 figures, we are just backing off so much, we are losing some
7 steam, and it is back to business as usual again.

8 The Chairman. Well, if somebody has a better plan--in
9 fact, it is open to amendment as soon as we go through it--but
10 you have to deal with the realities, and the realities are that
11 Tip O'Neill will not touch COLAs and neither will Ronald
12 Reagan.

13 Now, we can vote in here to cut Social Security COLAs, and
14 I think that is do-able. I think there are enough votes in
15 this Committee, and that would give you substantial savings, and
16 you could even make it effective next year. You could put it
17 all into Medicare, which would prop up that fund. But I do
18 not think we backed off very far. I think we looked at what
19 we are going to pick up in '84 and decided that we had better
20 use four-year numbers rather than three-year numbers. But
21 certainly, if somebody has a better suggestion--we are getting
22 into some tough spending cuts when we get to that point, and
23 there are all kinds of ways you can raise taxes. We have tried
24 to be fairly consistent.

25 Let us go through the rest of these accounting areas and

1 then try to get to the Members' provisions. I am certain we can
2 pass those if we cannot pass anything else.

3 Mr. Brockway. If I might, Mr. Chairman, I will just list
4 the item, list what the item is and the revenue, and we can
5 come back to them, rather than going through full descriptions
6 of the proposals.

7 The Chairman. And I understand that there is no objection
8 to our meeting later this afternoon, and I have got to be on
9 the floor at noon to offer the Tuition Tax Credit Amendment,
10 and I know Senator Boren and Senator Chafee want to be there,
11 and probably others. So if we could go through these quickly,
12 and maybe then we could come back here--is it all right to
13 meet again at four o'clock, so the staff will have some time
14 to go over it with all your staff?

15 Mr. Brockway. The next item, Mr. Chairman, Number 4 in
16 Accounting Abuses, deals with a situation where we have
17 accrual basis partnership and a cash basis partner, and this
18 would provide that you have to use the same method of
19 accounting. That would pick up .4 billion.

20 The next item is the conformity rules, it would require
21 those be provided on a consolidated basis. That would pick
22 up .5.

23 The next item, the time value of money, premature
24 accrual, deals with situations where you accrue a liability
25 that you will not have to pay for many years in the future,

1 and it would limit it to a present value or a cash basis
2 method. That would pick up 3.8.

3 Senator Bentsen. Mr. Chairman, on that one, that obviously
4 gets, I suppose, to casualty companies, and that is what I
5 would think you would be dealing with.

6 Mr. Brockway. There is a ruling that applies. It is a more
7 liberal rule than a general rule, but it does affect casualty
8 insurance reserves.

9 Senator Bentsen. That is an industry that is awash
10 in red ink, and I think it is important that you do not further
11 compound the problem and the process here. But this is one
12 of those things that obviously had to be explored, and should
13 be.

14 Mr. Chapoton. Let me just add that, as I told the
15 Chairman and the staff, we want to look at the effect on
16 casualty companies more closely, too, Senator.

17 Mr. Brockway. That item would be a \$3.8 billion pickup.

18 Then, you have corporate reforms. These are some of the
19 items that were in the staff--.

20 Senator Symms. Before you go by that, could you just
21 comment. This is a whole new concept, back on this time value
22 of money on the accrual, isn't it?

23 Mr. Brockway. Well, it is similar to the notions that you
24 use in the original issue discount area of treating the actual
25 present value of the amount, but you either get that or you get

1 the cash deduction when you pay it, so you could do it that
2 standard way.

3 Senator Symms. But if you apply this principle to the
4 property and casualty companies--and I think I agree with
5 Senator Bentsen that they have enough problem without this--but
6 if that principle is applied, and then you apply it to everybody
7 else, wouldn't the government end up being the net loser?

8 Mr. Brockway. I do not--.

9 Senator Symms. Well, you are talking about if you, for
10 example, are a manufacturing industry on depreciation, and you
11 want to apply that same principle, then you would have to repay
12 them.

13 Mr. Brockway. Well, basically, what you have done in
14 depreciation is because of the same problem, that is one of the
15 reasons for ACRS and investment credit, because if you just
16 took the actual cash amount for depreciation, you would not
17 have gotten enough to take care of inflation.

18 Senator Symms. The point I want to make is I think this
19 deserves some very, very careful scrutiny before we enact it,
20 and I would think that there is a principle involved here
21 to start taxing the time value of money, that if you are going
22 to apply it all the way around, then you might end up that
23 the Treasury decided they did not want to get involved in
24 this.

25 Mr. Chapoton. Senator, I am not sure I understand your

1 point. Our concern has been a deduction of an item in a
2 current year that will not be paid for a number of years. Now,
3 we addressed that concern in other than the property and
4 casualty area, but we said--and I think certainly there is a
5 problem in the property and casualty companies, that their
6 system of establishing reserves is such that they create
7 losses when they have economic income. They also have
8 economic losses; they swing from year to year or from period
9 to period, dramatically.

10 Senator Symms. But they are setting aside those
11 reserves.

12 Mr. Chapoton. I think in our view, the reserves they
13 set aside are much larger than needed to fund the future
14 liabilities. But to deal with that problem is not so easy.
15 I am not positive this is the way to do it.

16 Senator Symms. But didn't GEICO just end up two years
17 ago or something where they were in a real bind, and what we
18 would be doing this--.

19 Mr. Chapoton. I think that the people in the insurance
20 industry pretty well feel there is too much capacity in
21 the property and casualty companies, and I think the tax
22 problems maybe contribute to that. That is, the tax benefits
23 are such that people are acquiring property in casualty
24 companies to use tax losses that are generated even when
25 there are not economic losses. They are also, from time to

1 time, having economic losses.

2 But I would emphasize the portion of this package that
3 does not apply to property and casualty. That is, when you
4 are accruing currently under the all events test, the full
5 dollar amount that will not be paid for ten years, that
6 overstates the current deduction.

7 Senator Symms. Well, would you be willing to reimburse
8 for the time cost of money if you taxed for it?

9 Mr. Chapoton. I am not sure--

10 The Chairman. We are going to get into all of this later
11 on in detail. Let's try to finish this list. I have got to
12 offer an amendment at twelve o'clock.

13 Senator Symms. We withhold money from the individual
14 taxpayer, but the government does not reimburse them.

15 Mr. Chapoton. That is right. We have a pay-as-you-go
16 system; it is paid throughout the year, both individuals and
17 corporations.

18 Senator Symms. Well, I know, but if the taxpayer comes
19 in at the end of a year and files a claim, and he's got it
20 coming, he does not get paid for the cost of the money when
21 the government had it all year.

22 Mr. Chapoton. Not for that year; he does if it is later
23 than the year. But no, that is right. The taxes are due on
24 an estimated basis throughout the year.

25 Mr. Brockway. This proposal generally would not apply to

1 situations where the delay in payment is within the following
2 taxable year, and so in that situation, it would not have
3 applied either, because you only have a one-year lag.

4 On the corporate reforms, these are generally items
5 dealing with conversion of ordinary income with the
6 capital gains, or short-term gains into long-term gains. The
7 first item--and a number of them turn on the 85 percent
8 dividends received deductions that a corporation can deduct
9 85 percent of the dividends it receives--the first item deals
10 with the situation where a corporation receives deductions
11 of which you can take the 85 percent dividends received
12 deduction, plus it does that with debt financing, so it
13 deducts the interest and excludes the dividends it receives.
14 That would be a pickup. We do not have a final number on
15 that, but roughly .1.

16 The next item deals with short sales, ability to convert
17 a short-term capital gain into an ordinary loss by entering
18 into a short sale in which you get a capital gain on the short
19 sale and deduct payment in lieu of dividend. That picks up,
20 again, something roughly in the .1 area.

21 The next item deals with situations where you have a very
22 large dividend of property, and there is no basis reduction
23 in the corporation's stock with respect to which the dividend
24 is distributed, so the corporation can get the dividend,
25 exclude 85 percent of it, and then sell the stock which paid

1 the dividend and get a capital loss on that. That item would
2 pick up .2.

3 The next item deals with the distribution of appreciated
4 property in the course of a dividend arising in liquidation,
5 and that would provide that gain would be recognized on that
6 transaction. That is a pickup of .1.

7 The next item, Item Number 3, deals with a situation
8 where a corporation distributes a partnership interest and
9 some taxpayers take the position that that is not an
10 exchange; the distribution of the partnership interest, so
11 that no recapture is required.

12 Senator Bentsen. Does that deal in a royalty trust?

13 Mr. Brockway. Yes. Item 2 would affect the royalty
14 trust, because that is a distribution of appreciated
15 property.

16 Senator Bentsen. And what year would that take effect?

17 Mr. Brockway. That would take effect next year.

18 Senator Bentsen. In '84?

19 Mr. Brockway. Yes. And Item 1(c) would also affect that,
20 and that would apply to situations where the dividend was
21 after the date of enactment.

22 The Chairman. That is assuming that all this passes this
23 year.

24 Senator Bentsen. Well, but you have got a bunch of these
25 things that are not taking effect until '85.

1 Mr. Brockway. Well, if it is not as a dividend, it would
2 not be affected by this, so it is only situations where
3 it is paid out as a dividend, so the recipient gets to
4 exclude the income and then sells the underlying stock at a
5 loss, for example.

6 Senator Bentsen. That also means that you get this
7 Committee very much involved in some of the merger and
8 acquisition procedures taking place at this moment.

9 Mr. Brockway. It would affect certain transactions that
10 are ongoing, that is correct.

11 The partnership item would be .2 pickup.

12 The next item deals with mutual funds. One item deals
13 with the mutual fund, not a regulated investment company that
14 qualifies for tax-exempt status under the regular rules, but
15 a corporation that is widely held that invests in dividend-paying
16 stock and managed to eliminate its tax using the 85 percent
17 dividends received deduction. That would make it clear that
18 the accumulated earnings tax would apply, plus the 4(b) item
19 deals with situations where you have a capital gain dividend
20 with respect to a mutual stock, and the shareholder receives a
21 capital gain dividend and a short-term loss on the sale of the
22 stock, and that would match those two up. That item is a
23 .2 pickup.

24 Item 5 deals with transfer abroad of appreciated property.

1 certain recent court cases that have hindered the ability of
2 the Internal Revenue Service to policy transfers of appreciated
3 property to foreign corporations. That would pick up somewhat
4 less than .1.

5 Also, the final item would deal with the transactions in
6 the future, such as the McDermott transaction, where through a
7 glitch in the law, a U.S. corporation which managed to transfer
8 itself overseas without any tax liability, it would not affect
9 that transaction, but it would affect future transactions
10 like that.

11 The numbers are not going to add up to the total you have
12 on the basic sheet of each of these items, because there is
13 substantial interaction between these, and a number of them
14 affect the same transaction plus rounding errors. But it
15 should be roughly in the area of, I believe it is \$13
16 billion, over the four-year period--that is correct, it is
17 \$13 billion over the four-year period, and about \$8.4 billion
18 over the three-year period is what we have on the sheet.
19 Those are subject to some change, but it will be that
20 magnitude.

21 The Chairman. And we can discuss this later today, but
22 as I again understand Treasury, with the exceptions noted--.

23 Mr. Chapoton. Yes, and I wanted to note one final
24 exception on Number 5 on the final page. This mainly deals
25 with transfer of intangible assets abroad, and the classic case,

1 where the deductions in developing the intangible are taken
2 to the U.S., the intangible asset is then transferred abroad,
3 and the income from it is taxed abroad. It is a problem; I
4 am not confident that we--we need to look at the solution
5 much more closely.

6 The Chairman. Well, I think there are a number of questions
7 that have been raised on when they are--I think most of these
8 should be effective in '84. There might not be any reason to
9 get involved in the middle of a big corporate struggle
10 somewhere. But if it is loophole closing, we should not
11 wait until '85 unless there is some extraordinary reason.
12 There has been some question raised about property and
13 casualty companies, which I think must be resolved.

14 So I think the next thing we would like to turn to are the
15 additional items, and not go through all those, because they
16 are generally items that the Members have called to our
17 attention.

18 Have you got that packet, George?

19 Senator Mitchell. Mr. Chairman, could I ask one--not ask
20 a question, but merely request that something be prepared for
21 the four o'clock meeting?

22 The Chairman. Sure.

23 Senator Mitchell. We have a spreadsheet of the Budget
24 Committee deficit reduction plan that summarizes the spending
25 cuts and tax increases. I wonder if a comparable spreadsheet

1 could be prepared for what is now before us, and if it could
2 be prepared in a form that is directly comparable to the
3 Budget Committee's plan. One appears to cover four years, and
4 one covers three, so you get a different impression from the
5 aggregate levels.

6 The Chairman. Yes, that is a good idea. We can do that.

7 Mr. DeArment. It is just a matter of showing three-year
8 totals based on the summary we have in front of us.

9 The Chairman. But let's try to put it on one sheet,
10 so we just have one.

11 Senator Mitchell. I think it would be useful to be able
12 to look at the two, because I have some questions regarding
13 various provisions, that we can get to at four o'clock.

14 The Chairman. I guess the point being that if, in fact,
15 the Budget Committee's spending reductions are real, and we
16 could agree on our spending reductions or some other
17 combination--I am not wedded to any particular combination--we
18 would almost have the \$75 billion on spending restraints,
19 which would be real spendin restraint. We get some credit for
20 debt service, but that is real savings. And there would still
21 be a chance to bring those two together.

22 As I said earlier, I do not quarrel with the Budget
23 Committee, but I do not really believe they have drafted all
24 these tax proposals--at least, so far as we know, they
25 have not--so I do not know when they intend to offer that

1 amendment.

2 But the reason I say come back at four is that it will
3 give the staff time to meet with your staff, and some of the
4 questions that have been raised this morning, I think should
5 be addressed. Obviously, this entire package is subject to
6 change, and if anybody has a recommendation on how to make it
7 better, why, we would like to have those.

8 What time do you want to meet with staff--one-thirty,
9 one o'clock?

10 Mr. Brockway. One-thirty would be a good time, Mr.
11 Chairman.

12 The Chairman. Would that be all right with Treasury?

13 Mr. Chapoton. Yes, sir, that is fine.

14 The Chairman. So that would give them a couple of hours,
15 and then we could come back at four and go over the spending
16 side. And then, if members have any additions they want to
17 bring up--now, most of these, as I understand the additional
18 items, have been approved by Treasury?

19 Mr. Chapoton. Yes, sir. There may be one or two--well,
20 there are a few exceptions, but for the most part, we have
21 been over them all, and we agree with them.

22 The Chairman. And we have even had hearings or passed
23 these provisions before in this Committee. I think that was
24 part of the Long rule. And then the Joint Committee has--I
25 do not say "recommended"--but you have analyzed all these

1 provisions?

2 Mr. Brockway. We have analyzed them. I think there may
3 be one or two you have not had hearings on.

4 The Chairman. What is the total cost of the add-ons?

5 Mr. Brockway. I think in net, they may lose almost
6 \$2 billion.

7 The Chairman. So we need to find \$2 billion to pay for
8 the add-ons. We close some loopholes and open others, is
9 that it?

10 Mr. Brockway. Well, I am not sure that these add-ons are
11 loopholes.

12 The Chairman. Oh, probably not, but there may be one or
13 two in there that might be.

14 Senator Mitchell. Mr. Chairman, do we have a backup
15 document on the spending restraint, other than this piece of
16 paper?

17 The Chairman. Are those available for hand-out?

18 Mr. DeArment. Yes. Maybe we can go over those with the
19 staff at one-thirty, as well.

20 The Chairman. Okay, we will come back at four o'clock,
21 and thank you.

22 [Whereupon, at 12:00 o'clock p.m., the Committee was
23 recessed, to reconvene at 4:00 o'clock p.m. this same day.].

24

25

1 The Chairman. I apologize for being late.

2 We were having a meeting next door.

3 Have you had a chance during the--since noon to spend
4 some time with different staff members and also go over the
5 so-called add ons that members might have interest in?

6 Mr. DeArment. Yes, Mr. Chairman.

7 We have had two meetings, one to go over the tax items
8 and another meeting with the legislative assistants on the
9 spending side to go over the spending reduction proposals.

10 The Chairman. Are there any questions about any of the
11 add ons?

12 Mr. DeArment. There were questions.

13 The Chairman. Cannot believe it.

14 You mean there were not enough add ons?

15 I am sure we included every meritorious item.

16 Mr. DeArment. In our view, that is the case.

17 The Chairman. Probably some that were not meritorious.

18 Were there suggestions made--I know members are not here,
19 staff probably are. If there are areas that we did not
20 address that deserve serious consideration, then we ought to
21 be notified rather quickly. We are not trying to load the
22 bill up with add ons and then help to reduce the deficit.

23 There are not going to be two packages, one that does
24 not leave the Committee and one that does.

25 Have you had a chance to review all of the additions?

1 away. There is always that possibility.

2 Are you ready, Buck?

3 Why don't you note your objections to the specific
4 add ons and then we will have the person that is interested
5 in that particular amendment visit with Treasury between now
6 and tomorrow.

7 Mr. Chapaton. I will go over these quickly, going down
8 this list, and I will just do the ones that we were raising a
9 problem about.

10 The Chairman. We assume the ones you do not raise---

11 Mr. Chapaton. Are fine.

12 The Chairman. Then you would approve all of those you
13 do not raise.

14 Senator Chafee. Are we on this sheet, additional
15 items, non-statutory fringe benefits?

16 Mr. Chapaton. That is correct.

17 Senator Symms. Are we talking amendments?

18 The Chairman. No.

19 We are seeing what Treasury objects to.

20 Mr. Chapaton. On page 3, Number I, the bank loan loss
21 reserve. We have supported and continue to support staying
22 with the 001 percent rule. That is just a statutory rule.

23 Senator Symms. Excuse me.

24 I am back with Senator Chafee, non-statutory fringe
25 benefits.

1 The Chairman. What we are doing now is the Treasury has
2 no objection Number A, but--we are asking which ones of these
3 they have added on they object to.

4 Those would be open for amendment later.

5 Senator Symms. Could I ask Buck one question about A?

6 Don't you think it would be better tax policy if we
7 settled this thing on the fringe benefits and not have this
8 thing hanging over everybody's head, for if you want a
9 moratorium--I said the other day, let's have a moratorium for
10 ten years so it would be part of the tax code. It cannot be
11 good tax policy.

12 Mr. Chapaton. We have said that this is a question that
13 probably will have to be addressed in more of a whole or
14 major reform bill. We are not going to rush out with regula-
15 tions if the moratorium expires so we are not objecting to an
16 extension. The House has passed a bill that attempts to deal
17 with this, and I think the Committee will have to deal with
18 it.

19 Senator Symms. Senator Moynihan and Senator Matsunaga
20 and myself have introduced a bill and we---

21 Senator Packwood. Are you offering a ten-year mora-
22 torium?

23 Senator Symms. I said that facetiously. I said if we
24 are going to have a moratorium--let's have a moratorium is my
25 point. Our bill codifies into law by a list the current

1 business practices and addresses some of the college problems
2 where they have faculty housing, addresses those things, and
3 allows that to continue on. We simply do this to solve this
4 problem once and for all.

5 The Chairman. I do not think we have had hearings on
6 your bill.

7 Senator Symms. Yes, we have had hearings.

8 The Chairman. But not on your specific proposal.

9 Senator Packwood. I hope we would extend the education-
10 al fringe benefits that expire this year. If we are going to
11 get into it generally, I have a deep interest in this. I
12 would be happy to have a ten-year moratorium, but I have
13 strong misgivings and strong opposition to putting half on
14 or codifying or limiting fringe benefits that can be negotia-
15 ted between employers and employees without them being tax-
16 able.

17 Senator Chafee. As I understood the ground rules, he
18 was going to go through and show what he objected to. Now we
19 are stuck on A.

20 The Chairman. I know, but Senator Symms wanted to ex-
21 press an interest in that section. We wanted to hear those
22 that Treasury objected to.

23 Mr. Chapaton. On page 3, on the bank loan loss reserve,
24 we wanted to go to the 1 percent rule, rather than having the
25 rule suggested here, which would be the current year and two

1 previous years.

2 Senator Chafee. Can you give not only the page but the
3 letter?

4 Mr. Chapaton. That is Item Number I, Senator, on page 3.

5 Next is on page 5, Item P, multi-employer pension plan,
6 with draw liability. We have objected to this relief. This
7 is not really a Treasury subsidy matter. The PBGC has a con-
8 cern. We have concern that some of these plans will go under
9 and they will end up as a liability on the Federal government.

10 That is Item No. 5--page 5, Item No. P.

11 Senator Packwood. I have a question as to how that
12 affects an Oregon company.

13 Mr. Chapaton. We have objected to this. We objected to
14 that earlier.

15 Senator Chafee. You are saying to object to P, which
16 would give relief--

17 Mr. Chapaton. The subsidy question is whether there was
18 retroactive liability put on these plans and we have--we are
19 not re-examining that question. As I understand it, the
20 liability was imposed from the day the bill was introduced,
21 and so from the date of enactment, it was retroactive. Our
22 concern is the potential cost to the Federal government if
23 the plan--these plans go under and the employers who would
24 otherwise be employable or not, the liability would fall on
25 the Federal government.

1 Mr. DeArment. Your concern, isn't it, that we let these
2 plans that we cut out from under the liability--if they are
3 able to withdraw without this withdrawal liability, that the
4 pension plan that they would have paid that liability to
5 might collapse and then PBGC would then be required to pick
6 up the pieces.

7 The Chairman. Whoever offered that amendment knows that
8 there is a problem with Treasury.

9 Senator Danforth. This is really an eleventh hour pro-
10 blem.

11 We did this last year and there was no objection from
12 Treasury.

13 Senator Packwood. Did you have the same effective date
14 last year?

15 Senator Danforth. You did not oppose it last year.

16 Mr. Chapaton. Let me look at that again.

17 As I say, we are acting on this case under instructions
18 from the PBGC and the Labor Department. It is not a tax
19 matter. It is a PBGC matter.

20 The Chairman. Let's resolve these areas where Treasury
21 objects, but other than that?

22 Mr. Chapaton. The next one is Q on page 6.

23 That's basically a granting retroactive rollover treat-
24 ment, that a--it is private relief and we traditionally
25 object to private relief and particularly retroactive relief.

1 That arrangement did not meet the rules for a rollover and
2 this would give relief to a particular taxpayer. We object to
3 that.

4 Mr. DeArment. This is one that the Committee also did
5 last year.

6 The Chairman. Even though Treasury objects, may not mean
7 that we will object.

8 Mr. Chapaton. The next one is S on that same page, page
9 6. This has to do with repeal of the 30 percent of with-
10 holding taxes on investments by non-residents--by foreign
11 persons, non-resident aliens.

12 The Chairman. Do we have a revenue number on that?

13 Mr. Chapaton. Senator, we have supported the bill that
14 would exempt such portfolio investment. There is a disagree-
15 ment between our staff and the Joint Committee on whether it
16 is a slight revenue pick up or a slight revenue loss. The
17 proposal is not to have a total exemption, the total removal
18 of the 30 percent, but to leave a 3 percent tax on these
19 transactions. That would take away much of the differential
20 that is now available in the Euro dollar market.

21 We just would stand by our original position that there
22 should be no withholding whatsoever in these transactions. We
23 get involved here in the Netherlands Antilles case. This
24 proposal would put a 3 percent on loan facilities in the
25 Netherlands Antilles, and you would need to do that if you put

1 the 3 percent tax on all investments, portfolio investments
2 by foreigners. We would think that the better rule would be
3 no tax whatsoever and then we will continue our negotiations
4 with the Netherlands Antilles for what is left for them.

5 Senator Chafee. Mr. Chairman, as I understand what the
6 proposal is, this 3 percent that would apply to those bought
7 by foreigners directly, and those bought through the Nether-
8 lands Antilles--but you have a treaty with the Netherlands
9 Antilles. So how can you put a 3 percent on?

10 Mr. Chapaton. I think if the Congress put a 3 percent
11 on, it would override the 3.

12 Mr. Brockway. I think whether Euro bonds issued through
13 the Netherlands do or do not qualify under the treaty--this
14 would qualify that where a loan was issued by a few experts
15 through a foreign subsidiary and then reborrowed from a
16 foreign person--so it was routed through as a conduit, that
17 would be treated as if borrowed directly from a U. S. person.

18 Senator Chafee. If that can be done, I suppose you pick
19 up a little revenue.

20 So what is the argument for going to zero?

21 Mr. Chapaton. The argument for going to zero is we
22 wanted access to the Euro dollar market with no tax. It is
23 not--we often go to zero in treaties.

24 For example, the UK treaty. If a UK person invests in a
25 bond of a US company, there is no withholding at all,

1 interest paid to that person. We wanted unlimited access to
2 our market by the investors.

3 Senator Long. You object to this provision?

4 Mr. Chapaton. Yes.

5 We do not like the idea of putting a 3 percent tax on
6 there.

7 The Chairman. It might be something we might be able to
8 resolve.

9 I hope we could do it in consultation with those that
10 have an interest.

11 Senator Symms. Does the State Department agree with the
12 position Treasury has taken?

13 To me, this sounds like a real conflict on what we did
14 last year on the Caribbean Basin initiative. If I understand
15 the impact on the Netherlands Antilles, they say this will
16 cost, the way they have been attracting capital--it just
17 about cuts the tax base in half.

18 Mr. Chapaton. This proposal, which would, I am sure,
19 disturb the Antilles, as would our proposal--our proposal
20 would say you in effect--the company can access the Euro
21 dollar market without going to the Netherlands Antilles.

22 It might choose to do so anyway, but both routes would
23 be free of tax.

24 Senator Symms. This 30 percent--

25 Mr. Chapaton. We are proposing repeal of the 30 percent.

1 Senator Symms. If you repeal the 30 percent, would not
2 there be a drastic impact on the Netherlands Antilles?

3 Mr. Chapaton. The Netherlands Antilles is used by many
4 companies to avoid the 30 percent tax. So if you accept that
5 line of reasoning, Senator, you have to say that we want to
6 protect the Netherlands Antilles by allowing them to impose
7 a toll charge on our access to the Euro dollar market.

8 The Chairman. You are trying to eliminate a haven.

9 Mr. Chapaton. We are trying to allow directly what now
10 is allowed through the Antilles.

11 The Chairman. Go ahead.

12 Mr. Chapaton. The next one would be on page 9, Number
13 Z, both Z and the next one, AA. They are special relief
14 provisions, and we have proposed both of them, particularly
15 Z and FF.

16 The Chairman. Which one is Z?

17 Mr. DeArment. That is Mr. Symms' bill.

18 Mr. Chapaton. On FF you have several options.

19 The Chairman. What about page 9?

20 Do you object to Z and then AA?

21 Mr. Chapaton. Yes, sir.

22 The Chairman. Next is page 14.

23 Senator Chafee. Mr. Chairman, I wanted to ask about Z.
24 Z is not the generation skipping, is it?

25 The Chairman. No.

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Senator Chafee. Is that in here?

The Chairman. They have a modified proposal.

Is that in here?

Mr. Belas. The Treasury recently delivered to Congress a proposal which is part of this package.

The Chairman. Where is it?

Mr. Belas. CC.

The Chairman. You oppose that double F on the policy that it is special interest?

Mr. Chapaton. Yes.

Z is something we have considered and it would overrule--
-the IRS maintains a position and the Supreme Court supported that position, and it would go back and overrule that case now.

I should mention for the record, page 8, Number Y, the mortgage subsidy bond program, the Administration has opposed extension of the mortgage subsidy program, as I have said many times before this Committee. The extension was adopted, and in the House we do support the mortgage tax credit alternative that is part of that package.

The Chairman. As a package. You would not object to extension of the provisions?

Mr. Chapaton. Our position is that we object to the extension of mortgage subsidy bonds, but if it is going to be extended, and we recognize there is a lot of support for

1 extending, then we will support the other.

2 The Chairman. You still oppose the extension, but you
3 would support the extension on mortgage credit.

4 Mr. Chapaton. That is correct.

5 Then on private foundations, on FF, we are supporting
6 basically option Number 1.

7 The Chairman. What page is that?

8 Mr. Chapaton. Page 14.

9 Senator Symms. Before you go away from page 11, I am
10 sorry, Senator Warner was here and I got distracted, but I
11 just want to let the Committee know that I intend to offer an
12 amendment on that generation skipping that is supported by
13 the American Bar Association, the American Institute of
14 CPAs, the American College of Probate Counsel, the American
15 Bankers' Association, the Chairman's favorite association, the
16 New York State Bar Association, the California Bar, the
17 Illinois Bar, the Boston Bar and many others.

18 We are--I want to press that to a vote, and I would like
19 to let the Committee know that.

20 I want to repeal that tax. We heard a great deal of
21 testimony about that in the State Tax Committee.

22 The Chairman. That is something you are really interest-
23 ed in.

24 Senator Symms. Interested in it enough to vote for
25 \$150 million in new taxes.

~~R~~ ~~bing~~

1 The Chairman. Thought you were undecided.

2 On private foundations, I know there are a number of
3 members, and Senator Armstrong is not here, and Senator
4 Bentsen, Senator Moynihan, Senator Packwood for Senator
5 Percy.

6 Senator Matsunaga. What about page 13?

7 I understand you have no objection to anything on page
8 13, including Item EE.

9 The Chairman. That is yours.

10 I think we signed off on it.

11 Senator Matsunaga. Thank you very much.

12 Mr. Chapaton. Senator, you do raise a good point.

13 The Chairman. You were home free for awhile there.

14 Mr. Chapaton. Let me say this: if you are going to
15 extend--we have concerns about extension--exceptions to the
16 debt finance rules for charities in general, because in spite
17 of the arguments we have heard from some of the education
18 institutions, it does allow tax exempt investors to compete
19 with taxable investors, and we have serious concerns about
20 that. It does say that you can borrow money to put in the
21 real estate investment and not--in other words, not use your
22 assets, but just borrow money for an acquisition and the in-
23 come can be obtained tax free, which obviously can reduce the
24 debt much quicker, return--a higher return to the charity than
25 could be possible to a taxable investor.

1 We think there is a competitive problem there. If the
2 Committee decides to make some change in that area, as the
3 Senator has proposed, these types of limitations are the
4 type of limitations we support.

5 Senator Matsunaga. Thank you very much.

6 Let's go to page 14.

7 The Chairman. On the foundations, we know what happened
8 in the House, and we know every year we had them and they
9 take them off. Is there some generic approach to this without
10 identifying which foundations are in trouble?

11 Mr. DeArment. There could be a generic approach.

12 Actually, I thought Treasury would---

13 Mr. Chapaton. We were supporting 1 and 2. They are not
14 mutually exclusive. One would maintain present law and 2
15 would allow an exception for unusual situations where a good
16 faith effort--more time to dispose of excess business hold-
17 ings.

18 The Chairman. Who does that effect?

19 Mr. Brockway. That is the McArthur Foundation.

20 Mr. DeArment. There might be others, too.

21 Senator Moynihan. These things are all located somewhere
22 and they obviously go to the--all these foundations are
23 located somewhere, and in New York there is a foundation,
24 the Altman Foundation. It was established in 1909, I believe,
25 something like that, and it is in that same situation. It

1 was established in 1913, and they are quite willing to comply
2 with the law, but they got caught in the 1969 legislation
3 which gave fifteen years to a group with 75 percent of oper-
4 ating businesses control, and twenty years to the others, and
5 that sort of caught them.

6 They do not know why there is that difference. They
7 could live with one and not the other. I do not think you
8 have any interest in putting these people out of business.

9 Mr. Chapaton. No.

10 In each case it has to do with the extent of their
11 holdings in 1969. Some--the longest period was twenty years
12 to get rid of excess business holdings. If you held 100
13 percent--above 95 percent in '69, and if they were lower--if
14 they were at another level, they had fifteen years to dispose
15 of it, between 75 and 95 percent. Well, they have had a long
16 time to know that they had to meet this disbursement require-
17 ment. Our concern has been in the area where a large gift
18 was received and it really appeared that the magnitude of the
19 gift made it difficult to dispose of the property within five
20 years for new gifts that the law allows.

21 We thought some relief ought to be provided there. But
22 for the pre-'69 cases, we have taken the position that there
23 should be no way for these foundations that had notice for
24 this long what the law was--we have opposed revisiting those
25 questions.

1 Senator Moynihan. You say you have proposed?

2 Mr. Chapaton. Opposed visiting those.

3 Senator Moynihan. Number 2 would give you the opportun-
4 ity to permit additional time if you thought there was ground
5 for it.

6 Mr. Chapaton. I am not sure that would apply to Altman
7 because this would only apply to post-'69 holdings acquired
8 by gifts.

9 Senator Moynihan. This goes back to 1913.

10 Mr. Chapaton. The foundation can be in existence a long
11 time, but this applies to when the gift was given.

12 Senator Moynihan. Mr. Chairman, I think there are a
13 number of person who are concerned about foundations other
14 than just McArthur.

15 Do you want to pass over this until they are here?

16 The Chairman. Obviously, those who have an interest we
17 want to protect.

18 As I understand it, Treasury would go as far as retaining
19 the present law with that exception in Number 2.

20 Anything else we adopt would be over your objection.
21 That is how we have done it in the past. We will come back
22 to that.

23 Mr. Chapaton. I have listed all of them that we have
24 concern with, Mr. Chairman.

25 The Chairman. Now, I wonder if we could move--why don't

1 we move to--if Sheila could come up and explain the standing.

2 Senator Chafee. On one that I had submitted and was not
3 in the list--actually, I submitted several that are not on the
4 list. But the airline pilots, the mandatory retirement and
5 the problems under ARISA, that is probably not your area, but
6 the problem is, they have to retire at sixty.

7 Are you familiar with that?

8 Mr. Belas. Yes, Senator Chafee, yes, we have reviewed
9 that with the Joint Committee and Treasury, and there was
10 objection to that.

11 The specific problem was dealt with specifically in
12 TEFRA where, in conference, the conferees decided to modify
13 the Senate rule to say that you could not reduce below
14 \$75,000 actuarially for early retirement. The judgment of the
15 conferees last year was that \$75,000 was sufficient at age
16 55 as protection for people who had to retire at an early age
17 and on that basis Treasury objected, and we did not include
18 that on the list.

19 Senator Packwood. That is if they voluntarily retire.

20 We have forced the pilots to retire at an early age.

21 Mr. Belas. Whether or not they are forced to or not--
22 -the reason they are forced to is because they are not totally
23 disabled. They certainly can, in most situations, get an
24 additional job if they retire at an earlier age.

25 Senator Packwood. A sixty-year old pilot goes out and

1 gets another job?

2 Mr. Belas. They are not totally disabled and do not have
3 to rely totally on their pension benefits.

4 Senator Packwood. You are more optimistic than I am.
5 They are trained as a pilot and have flown for thirty years
6 and now we force them to retire and then penalize them in the
7 tax code because we force them to retire.

8 Mr. Belas. We force them to retire from commercial air-
9 lines. That does not mean they cannot fly another aircraft
10 for hire.

11 Senator Chafee. To be realistic--to be forced out--I
12 think it is a Federal law that puts them out.

13 Senator Packwood. They can go to work for General Motors
14 as a corporate pilot if there is a job at age sixty, and I
15 realize you cannot discriminate on the basis of age, but we
16 are forcing them out of their customary job and then penaliz-
17 ing them.

18 Mr. Chapaton. The question is whether they should be
19 able to fund the same level of pension payable beginning at
20 an earlier age, which means they get a larger pension than
21 those whose pension can be funded at age 65.

22 Senator Packwood. For those who retire voluntarily.

23 Mr. Chapaton. If you have a ceiling and the ceiling
24 begins at 65, the same ceiling begins at an earlier age---

25 Senator Packwood. I do not think pilots would object if

1 we forced them to retire at 65.

2 Mr. Chapaton. Valuewise, they are getting something for
3 a longer period of time.

4 Senator Packwood. I think they are getting an unfair,
5 double-whammy.

6 Senator Chafee. We will take another look at it.

7 The Chairman. Can I ask Karen to explain one little
8 thing we need to correct before the end of the year, other-
9 wise there would be a loop in Social Security for Hill em-
10 ployees, and that might not be viewed too well with other
11 Social Security people that have to pay.

12 Karen will explain to me what that is.

13 Ms. Weaver. Under the Social Security amendment, if
14 Hill employees sign up for Civil Service during the month of
15 December, they will be establishing an exemption from Social
16 Security come January. That was intended. What was not in-
17 tended was the possibility that they could be temporarily
18 laid off in, say, January and be hired back by their Senator
19 or Congressman, and then be excluded from both Social Security
20 and Civil Service.

21 The Chairman. If they have one day off?

22 Ms. Weaver. There is a provision that encourages--that
23 allows you to be out of your Federal employment for up to
24 365 days.

25 The Chairman. How do we close the loophole?

1 Ms. Weaver. Simply require that you be under one or the
2 other.

3 The Chairman. Anybody object to that.

4 Senator Grassley. Tax is under a separate bill.

5 Senator Packwood. If we are going to do that, I hope we
6 take care of the error about taxing public employment contri-
7 bution systems of all the employees in the State, which was a
8 drafting error on our part, and I think both Treasury and the
9 Joint Committee support going back.

10 The Chairman. Are you familiar with that?

11 Ms. Weaver. George Pealer was taking a look at that.

12 The Chairman. I do not think we want to create a loop-
13 hole for people on our staff.

14 Is there any objection to reporting out that little
15 measure separately?

16 Senator Packwood. Could we correct that? The error?

17 Mr. DeArment. We could report this as a Committee
18 amendment to one of the House-passed bills.

19 The Chairman. We used that little bill this morning for
20 tax credit. We are going to use it later for something else.
21 That is a good little vehicle.

22 Is there any objection to that? And if the other is
23 non-controversial---

24 Senator Packwood. It is on the House bill, and Treasury
25 supports it.

1 Mr. Chapaton. I am not sure which one you are talking
2 about.

3 Senator Packwood. The technical correction.

4 Senator Moynihan. I wonder if I could raise this ques-
5 tion of covered options and our new straddle rule?

6 The Chairman. That has been called to our attention by
7 the American Stock Exchange.

8 Senator Moynihan. The various groups think they have
9 worked out a proposal that would satisfy us.

10 Staffperson. We do have to work it out yet. We are very
11 close to agreement.

12 Senator Moynihan. The best thing is to hold off.

13 Mr. Chapaton. I understand you could work that out.

14 Staffperson. I think we could come back with a proposal
15 to the Committee.

16 The Chairman. Today?

17 Staffperson. Tomorrow morning.

18 The Chairman. Is there any other area that we should be
19 certain we correct that we have not addressed?

20 There are other Social Securities matters but I do not
21 think they are as urgent as the one we have just addressed.

22 Senator Chafee. Senator Danforth had a question he
23 wanted to ask Buck.

24 The Chairman. Can you stay longer?

25 Mr. Chapaton. Sure.

1 The Chairman. How are we coming on insurance?

2 Who is working on that?

3 Mr. Chapaton. Our staff has been meeting this afternoon.

4 The Chairman. You are closing the gap?

5 Mr. Chapaton. I understand we might be closing the gap.

6 Senator Packwood. Are we going to take care of the
7 policyholder provisions when we pass that bill?

8 Mr. Chapaton. That will come up. That is in discussion
9 now. It is the revenue level. We have expressed concern
10 about the policyholder provision--would express concern about
11 changing the policyholder provision. We thought the House
12 bill, if anything, did not go far enough. We have concern
13 about the ability to draw funds that were not taxed on a
14 non-taxable basis.

15 Senator Packwood. If and when we get the insurance bill
16 I would like to offer changes substantially altering that.

17 The Chairman. That is part of the discussion.

18 Mr. Belas. We have been trying to find a middle ground
19 between the health bill and repeal.

20 The Chairman. You have a number of horror stories to
21 tell us about that, don't you?

22 Mr. Belas. There are a number of abuses.

23 The Chairman. Do we all have the document on spending
24 options?

25 Ms. Burke. Yes, Mr. Chairman, it should be before you.

1 The Chairman. Let me just say, early on--I think
2 Senator Long needs one.

3 Ms. Burke. You should have two documents.

4 The Chairman. One is explanatory.

5 Senator Danforth. On that hunger relief, it is my under-
6 standing that the Administration agreed to half of it relating
7 to farmers contributing.

8 Mr. Chapaton. Right.

9 The individual farmer would be given basically the same
10 treatment, even though he deducted the expense, would be
11 given the same treatment as a corporate donor.

12 Senator Danforth. That is not now on the list.

13 I wonder if that could be added.

14 The Chairman. Are you aware of that provision?

15 Mr. DeArment. Yes.

16 The Chairman. No objection?

17 Mr. Chapaton. We do not have any objection.

18 I think the staff may have some concerns.

19 The Chairman. Let me say on the spending restraint
20 option, I know there are a number of members who are prepared
21 to vote to change the COLAs some 2 percent, some 3 percent.
22 There are about 500 combinations you can put together. But
23 it became obvious to me that with both the Speaker and the
24 President indicating rather strongly, publicly, that they
25 would not go along with anything that touched Social Security

1 since we had fixed it earlier this year, we have to go back
2 and look at other options and the only thing that affects
3 Social Security is the same thing we did with tax indexing,
4 lower the COLA to the next lower whole percentage amount,
5 which picks up about \$5 billion, and it seems to me we can at
6 least do that, and that amount plus any other amount we save
7 in this package would go into the Medicare trust fund.

8 With that explanation maybe, Sheila, you can go ahead.

9 Senator Grassley. You only take from the savings from
10 Social Security COLA and put that into the fund. You are not
11 talking about applying it to other COLAs as well, like Civil
12 Service?

13 The Chairman. That is right, and it is going to be in
14 desperate need of funds.

15 Senator Chafee. What was the rationale in deferring it?

16 The Chairman. Did not have any votes.

17 Senator Chafee. I do not mean deferring the total COLA,
18 but I mean the wound down.

19 The Chairman. Do you mean from '84?

20 Mr. DeArment. One of the problems, Senator Chafee, is
21 that the Social Security Administration needs quite a bit of
22 lead time to make changes in the benefit checks to these
23 36 million beneficiaries. Unless we said right now we are
24 going to postpone probably for several months the COLA that
25 is scheduled to come in January---

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1 Senator Chafee. We have crossed that bridge.

2 Let us take the round down that we are proposing here,
3 going down to the nearest full percentage.

4 Mr. DeArment. Probably need somebody from the Social
5 Security Administration, but as I understand it, that poses
6 the same problem.

7 Senator Chafee. When are those COLAs paid, April or
8 June?

9 Mr. DeArment. No, January. We shifted from June to
10 January. So January 1st the adjustment would be made, and
11 they have already taken steps to do that.

12 Senator Chafee. Thank you.

13 Senator Moynihan. Does this comprehend changing the
14 January '84?

15 Ms. Burke. '85, Senator.

16 Senator Moynihan. I just ask the question--yes, of
17 course, beginning in '85.

18 You have no way of knowing where the decimal point will
19 come out?

20 Ms. Burke. We have estimates by the actuary of what the
21 rates of increase are.

22 Senator Moynihan. There is a certain normal increase.
23 This is not an estimate of what is going to happen?

24 Mr. DeArment. It is an estimate of where that is going
25 to fall, and because that last fraction of a percent is

1 probably the most volatile, because that is the finest point,
2 we know that in any year it is not going to be greater--it
3 will always be less than 1 percent and average out to .5
4 over time.

5 The Chairman. Let us move on to the others.

6 Ms. Burke. The two documents before you describe the
7 spending restraint option.

8 The first item, which was just discussed, was the COLA
9 provision.

10 Following that are provisions relating to the two health
11 areas, Medicare and Medicaid.

12 The first item on the health area is the proposal which
13 would modify a provision previously agreed to by the Committee
14 which would have held the part B premium to 25 percent of
15 program costs through 1986.

16 This provision, which was an Administration provision,
17 would allow the premium to increase to 35 percent of program
18 costs by 1988. That proposal would save, over a four-year
19 period of time, an additional \$4.2 billion in excess of what
20 had been previously achieved.

21 So, in total, it would be \$4.6 billion.

22 Item No. 2 is a provision again that has been previously
23 discussed, was an Administration proposal which would delay
24 until the month following the month of eligibility--that
25 proposal achieves a savings of \$1 billion.

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Item No. 3, described on page 2, is also an Administration proposal and would provide for restructuring Medicare cost sharing. It also provides for an application of co-payments on hospital days and provides for unlimited hospital days under the Medicaid program.

That approach achieved a savings of \$3.2 billion over a four-year period of time.

Item No. 4 on page 3 is a modification of a provision previously agreed to by the Committee. The Committee will recall for the Tax Equity and Fiscal Restraint Act, we provided for coordination, where an individual remained employed and had employment base coverage. This would modify that provision and have a savings of \$1.2 billion.

Item No. 5 on page 3 is a modification of a provision very recently agreed to by the Committee as part of reconciliation proposals. This would continue for one year the freeze which had been agreed to by the Committee on physicians' prevailing fees for those physicians who were unwilling to take assignment. The Committee might note that there are additional provisions which are not budget affected in this proposal which hopefully will create incentives for physicians to take assignment. Additional savings as a result of this proposal would amount to \$1.6 billion.

So the total proposal would save approximately \$3.2 billion.

1 Item No. 6, noted on page 5 of the document, is a modi-
2 fication of an Administration proposal and would provide for a
3 limit on the rate increase in hospital costs per case. The
4 rate of increase that would be provided for would be limited
5 to the market basket which is estimated to be about 6 percent
6 per year. Under current law the Committee may recall those
7 amendments are allowed to increase by the market basket plus
8 one percentage point.

9 So this would remove the one percentage point.

10 Item No. 6, which is noted on page 6 of the document, is
11 a modification of an Administration proposal and would extend
12 for two years the reduction in Federal payment to States
13 under the Medicaid program. The reduction rate would be to
14 3 percent for '85 and '86. This has a cost savings over a
15 four-year period of time of approximately \$1 billion.

16 The Chairman. They are on this sheet.

17 Now, again, I understand that some members feel we ought
18 to be bolder in our approach, and I am certainly willing to
19 listen to other suggestions on spending restraint. I would
20 even entertain any suggestions on COLAs, but I think as a
21 practical matter, if we want to accomplish the objective of
22 reducing the deficit--I just do not believe, even though I
23 would report it, if it went back into Medicare, I do not
24 really believe there is much hope for that, and I would like
25 to believe there is still hope for deficit reduction. But if

1 members have any ideas on how we can be more daring or bold
2 to spending restraint that will also pass the Congress, why,
3 I would be pleased to entertain any suggestions at this time.

4 We have gone over the list a number of times and Senator
5 Roth has been concerned that we are not making real spending
6 cuts.

7 These are real spending cuts, aren't they?

8 Ms. Burke. Yes.

9 In addition, at Senator Roth's request, we calculated the
10 change as a result of the provisions starting in 1982, with
11 the Reconciliation Acts. We have achieved approximately \$30
12 billion in savings out of the Medicare and Medicaid programs
13 as a result of those changes. The rate of growth in those
14 programs without spending reductions, would have been, over
15 that period of time, approximately 71 percent. The rate of
16 growth with the spending reductions, including the provisions
17 before you, is reduced to approximately 53 percent.

18 So there is approximately a change of 17 percent in the
19 rate of growth as a result of the spending cuts.

20 Senator Roth. One of my concerns, and I think some of
21 these are real cuts, I agree with you, but one of my concerns
22 is that---

23 The Chairman. They are really restraints on growth.

24 Senator Roth. The question I have is what is going to
25 happen to these programs over the next five or six years, both

1 if we do nothing and, secondly, if we do adopt these re-
2 straints.

3 That was one of the questions I have, what is going to
4 happen to these programs in the next several years?

5 Secondly, if we adopt these restraints.

6 Am I not correct that the Medicare and Medicaid in the
7 next three years will roughly double?

8 Ms. Burke. We expect to continue to see a rate of in-
9 crease in the Medicare program of about 15 percent. The
10 Medicaid program has a much slower rate of growth, and it has
11 been averaging 9 percent. That average rate of increase is
12 expected to continue in the near future.

13 That is correct, Senator.

14 The Chairman. I think Senator Roth has a point.

15 If, in fact, these were adopted and became law, do you
16 have any information on what impact that would have--we are
17 told by 1985 we are going to have \$400 to \$500 billion pro-
18 blem with Medicare.

19 Is that correct?

20 Ms. Burke. Correct.

21 The Chairman. We are told if we do not do something by
22 '86, we will have to raise payroll taxes by 43 percent or cut
23 them by 30 percent.

24 Now will doing any of these things delay that day of
25 reckoning?

1 Ms. Burke. The estimates I just provided you are of a
2 rate of increase of 53 percent through 1986. Those will be
3 estimates we were able to make on the basis of the spending
4 reduction proposals, because those are the years we had
5 numbers, too. We asked for numbers for the out years, or all
6 of those previous proposals.

7 But that 53 percent is up until 1986. So I would assume
8 that you would see continued trends in a reduction in what
9 would have been a rate of growth in those programs, but until
10 we get the productions, I cannot tell you the size of that
11 reduction.

12 Senator Roth. The figures I have are that Medicare and
13 Medicaid programs have increased from \$67.9 billion in 1982,
14 to an estimate \$117 billion in 1986.

15 Is that correct?

16 Ms. Burke. That is correct.

17 Senator Roth. The question would be: what would these
18 restraints do to that?

19 Ms. Burke. Without spending reductions in 1982, it
20 would have been \$68 billion. Up to 1986, one hundred and
21 nineteen.

22 Senator Roth. What I am really interested in is not so
23 much what we did in the past, but what we are talking about
24 doing now, and what will that do to the health budget?

25 Ms. Burke; The addition of the proposals we are dis-
cussing today would reduce--we look at the cumulative savings

1 because they also reduce that rate. But it reduces 1986
2 to \$102 billion versus \$118. So the rate of growth, if you
3 were to look over '84, '86, '86, including these provisions,
4 would be a rate of growth from '84 to '85 of 11 percent versus
5 16 percent, a rate of growth in '86 over '85 of 10 percent
6 versus 11.6 percent. So we continue to see a reduction in
7 the rate of growth in these programs as a result of the pro-
8 posals that are before you today.

9 Senator Durenberger. Mr. Chairman, may I respond to
10 that?

11 I think Bill's question is what are we doing here that is
12 going to convince us that the costs are going to go down and
13 Sheila gave you the paper shuffle.

14 That is not a disrespectful term. That is a statistic.
15 The reality is on this list I cannot see anything other than
16 Number 3, restructuring Medicare cost sharing, I think we
17 could do better, but that is the one that could give us--the
18 one that might have some impact, because that means once folks
19 get to catastrophic they will start shopping around.

20 But as far as the others are concerned, with the excep-
21 tion of DRGs and vouchers, and a couple of other things,
22 everything else is just passed on. This is not like the
23 Defense budget, where if you do not fund the B-1 bomber, you
24 do not get an airplane. If you cut back on doctors or
25 Medicare, we simply save some money, but the hospitals shift

1 the costs off toe Blue Cross or some employer or something
2 like that. So this bill is--there is nothing really in here,
3 I do not think, other than No. 3, I think I got the number
4 right, on the restruction, that is actually going to do
5 something to reduce the costs.

6 There are more important things we have done, like pros-
7 pective payments and other things in the future. All this is
8 trying to do is save some money here, but somebody else is
9 going to pay for it somewhere else.

10 The Chairman. The only real hope is--depending on how
11 prospective payments work with hospitals, whether you apply
12 it to the physicians, there are already all kinds of storm
13 signals, whether it will work for hospitals, even if it has
14 been in place for 60 days.

15 Congressman Pepper suggests we appoint a Commission. I
16 suggest we have one.

17 We are meeting right now. If we cannot solve it, I guess
18 then we will appoint a commission, and we will become a
19 ratifying agency and not a legislative branch.

20 Senator Grassley. Along that line, Senator Heinz had
21 some hearings in the Aging Committee, and all of the testimony
22 was pretty unanimous, that you would have to have this cost--
23 sharing before you would get enough interest at the grass-
24 roots to get anything major done.

25 So I think what we are doing is the necessary forerunner

1 to accomplish what Senator Durenberger wants us to accomplish.

2 The Chairman. Are there any members that have sugges-
3 tions for other spending restraints, COLAs or anything else
4 that they prefer to see in the package?

5 Senator Heinz. I have some problems with the Administra-
6 tion proposal on the so-called restructuring Medicare cost
7 sharing and unlimited hospital days. Apart from the fact that
8 this is supposed to do something to discourage utilization,
9 I would be more convinced that if the people did not have
10 Medi-Gap insurance that took care of these kinds of problems.

11 So I am not terribly convinced this does much in the way
12 of improving utilization, giving proper incentives for more
13 prudent habits. I do think that we ought to look at other
14 areas of waste in the Medicare program before we start simply
15 shifting costs onto consumers.

16 I sound like a broken record. I said this a week or two
17 ago, and I will say it again with the patience of my col-
18 league. We know we could do a lot more in just two areas I
19 mentioned, one, in clinical labs where we are setting the
20 premium disbursement at 55 percent rather than 60 percent.
21 GAO suggested that.

22 The Chairman. Did the Administration oppose that?

23 Senator Heinz. They are opposed to everything else we
24 are doing.

25 The Chairman. What will that save?

1 Senator Heinz. A fair amount of money, \$600 or \$700
2 million.

3 Is that about right?

4 Ms. Burke. Approximately a \$600 million savings if you
5 bid at 60 percent of prevailing and included hospital base
6 labs.

7 The Chairman. Why should not we do that?

8 Ms. Burke. We had originally recommended against that,
9 one, because the 50 percent number was thought to be too low.
10 In talking with GAO and the industry, we thought that because
11 we were going into an area where we were not sure of the data,
12 60 percent was an unreasonably low rate.

13 With respect to hospital based labs, they have not been
14 identified as part of the problem that we went after, and we
15 were concerned that we did not have available to us comparable
16 data on hospital base labs, but we are aware of those being
17 House provisions, and certainly something we could consider.

18 The Chairman. If it makes sense, we ought to do it.

19 Maybe 60 is too low, but 65 is too high.
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Senator Heinz. I will not go through what I think we ought to do on Part A or, for that matter, Part B on pacemakers. My friend and I have had our disagreements. But here we are, up against it, and if we all stick to our disagreements, we are never going to be able to do anything.

Thirdly, it strikes me that, although we do have a provision in here on doctors, they are getting off pretty light. And I am willing to support anything that is balanced, but I have got to tell you, Mr. Chairman, I do not think this is well-balanced. I think we are letting some of the people who are really making out--the labs, for one; the doctors, for another; the pacemaker people, for a third--I mean, that whole group of people who are profiting off a system that was invented ten years ago before the technology changed to high-tech and small pacemakers and shorter operations. I just think we have to do more there before I am going to support, in particular, III, here. I am not sure I like III, anyway.

The Chairman. What about--are there other options on physicians that we may have overlooked?

Ms. Burke. Senator, the concern when we were examining options with respect to physicians was the concern about assignment and whether or not further restrictions on physician payments would result in shifting to beneficiaries. We tried to look at ways of reducing the rate of growth of

1 physicians, those on the ceilings, which is why we chose
2 prevailing, rather than customary and prevailing.

3 The Chairman. I know, but if we could save anymore
4 money from physicians--.

5 Ms. Burke. We could, if we chose to freeze them at a
6 tighter rate, yes, sir.

7 The Chairman. I think the participating plan made some
8 sense to me, because I think it is now used by Blue Shield.

9 Ms. Burke. Blue Shield, yes, sir.

10 The Chairman. And it does give some reliability, and
11 if we provide a number of other additions, directories and
12 other things, so that people will know who is participating
13 in Medicare--but if Senator Heinz has a specific suggestion,
14 we should take a look at it, in addition to--.

15 Senator Heinz. Well, how about more than one year?
16 Everything else we are doing is for three years.

17 Ms. Burke. The freeze is currently for 18 months, and it
18 begins in January and continues for a year after July for
19 those nonparticipating.

20 The Chairman. Senator Chafee?

21 We will look at those others, John, particularly the labs.

22 Senator Chafee. Mr. Chairman, I have got a suggestion,
23 but it really is not a solution, and that is, every doctor I
24 have talked to in connection with Medicare has spent a good
25 deal of time on outlining the number of tests he subjects a

1 patient to, not so much solely for the patient's good, but
2 for defensive medicine on the part of the doctor. And they
3 are not anxious to do it, but the rules and regulations and
4 the cost of potential suits that they might undergo--you might
5 be an internist, but not a Board-qualified internist of a
6 certain nature, and thus, you must call in a Board-certified
7 one, or should a suit arise, then the possibility of being
8 subjected to a plaintiff's verdict is very good.

9 Now, I do not know how to solve that, and of course,
10 this is not the first time this has been mentioned around
11 here. But if somebody had some kind of a solution to deal
12 with this defensive medicine that they in fact are pretty
13 much required to practice, it would really dramatically reduce
14 the costs of physicians and ancillary services--mostly
15 ancillary services, I guess.

16 But I do not have a solution.

17 Senator Symms. Would the Senator yield?

18 Senator Chafee. Yes.

19 Senator Symms. I might just mention the fact that
20 Senator Matsunaga and I have a bill introduced and are
21 planning to have a hearing on that subject, and I think
22 Senator Matsunaga is more aware of what they are doing in
23 Hawaii to try to lower the cost of malpractice, which eventually
24 has to be paid for by the medical patient in one way or
25 another. And I think that there are some thing we could do

and we should do, and I do not think we could probably do it on this legislation, but I sure agree with you.

Senator Chafee. Sheila, do you have any thoughts on this particular area?

Ms. Burke. Senator, there are two issues, really. One, there are discussions going on with respect to almost a no-fault kind of insurance with respect to malpractice. There has been some interest in perhaps protecting against the extraordinary recovery costs in terms of some of the awards given in reducing the cost of malpractice insurance through that means.

With respect to the actual testing that is a result of defensive medicine, the Medicare actuaries or the Medicare folks tell us that malpractice is not a significant issue with respect to Medicare and Medicaid, that you do not see the kind of incidence of claims with that clientele that you do with younger individuals. But there has really been a great deal of discussion and very little resolution of how to stop people from providing services that they feel remove them from question when a final judgment is made, how you make the decision between what is a necessary test and what is a test, really, on the margin. And I do not think anyone has really come up with a solution as to how best to do that.

Senator Chafee. Thank you.

The Chairman. I think Senator Moynihan had asked for

1 recognition.

2 Senator Moynihan. Just a simple point of clarification.
3 And let me just be speculative for one moment, and I would not
4 dare bring any good news into this conference. But the
5 Social Security Actuary is now regularly reporting their
6 projected condition of the old age and survivors fund, OASDI,
7 and their latest projection is that the surplus of 1995 will
8 be \$477.7 billion. If we get through the next three or
9 four years, you start clicking up very fast. They project
10 by the year 2000 a surplus of \$1.2 trillion.

11 Senator Packwood. How much pay-out when you get to that
12 year? In other words, how long will that surplus tide you
13 over?

14 Senator Moynihan. Well, the surplus continues, according
15 to the Actuary--I do not want to have anybody laughing at me
16 here--to the year 2025, when it has accumulated \$13 trillion.
17 Then, for the first year, it goes down. And these are the
18 numbers we were working with last year.

19 So obviously, there is going to be money in the Social
20 Security System that we may be able to move around a bit.

21 Senator Packwood. The reason I ask--I have seen those
22 figures before, but I think you have to weigh them against how
23 much payout you have--.

24 Senator Moynihan. What proportion--is that a big surplus
25 or a small surplus.

1 Senator Packwood. In other words, could you cut your
2 taxes, could you cut off Social Security payments, and go five
3 or six years with no payments into the fund. And as I
4 recall, you could make it even in 1995, only about 17 or
5 18 months, and your money is gone.

6 Senator Moynihan. Well, why don't I get these numbers
7 translated? I think they will be of interest to this
8 Committee in terms of is this a 17-month supply or a three-year
9 supply.

10 But I just wanted to ask in that regard, taking the COLA
11 down to the nearest lowest round percent, that is a three-year
12 provision, you intend?

13 The Chairman. That is right.

14 Senator Baucus?

15 Senator Baucus. Mr. Chairman, back to Medicare. As I
16 think a little bit about particularly Item Number 3,
17 the restructure, it strikes me that perhaps there are some
18 problems with going in this direction. This is what I am
19 thinking. Senator Roth is certainly right in pointing out the
20 growth in Medicare and how the growth is going to continue
21 even with these cuts. But we all have to realize that the
22 reason for the growth is because health care costs are
23 rising generally in the country at a rate two or three times
24 CPI, anyway. Medicare is just caught in this rise. And it
25 seems to me, then, that fundamentally--and it is difficult to

1 do this here, obviously, to address some of the reasons for
 2 health care cost increases, and that goes to cost technology,
 3 it goes to medical malpractice, it goes to American
 4 constitutional rights, and it goes to one's desire to get
 5 made well when one is not well, and all that.

6 But my problem with Item Number 3 is this. The original
 7 purpose of this restructure, as I understand it, when it was
 8 first proposed not too long ago, was to discourage seniors
 9 from staying unnecessarily long in hospitals. That is one of
 10 the major premises of it. But we have already addressed some
 11 of that with the DRGs, because under the DRG prospective
 12 reimbursement system, there is going to be an incentive to
 13 hospitals to discharge patients a little earlier than is
 14 otherwise the case.

15 The real question, then, is is that additional incentive
 16 enough to coincide with the intended incentive in the
 17 restructuring in Item Number 3. And it may be that we are
 18 going too far. That is, if the incentives in the DRG
 19 proposal are to encourage people to not stay in hospitals
 20 very long, then we are penalizing those patients who are going
 21 to have to be in hospitals anyway, so there is no choice
 22 involved anymore, because the prospective reimbursement
 23 system is already discharging them.

24 So it seems to me the way to get at this in part is
 25 to work with DRG prospective reimbursement and get the data on

1 it--I know that is not going to solve it here and now, this
2 year--but maybe work to include physicians in DRGs, in
3 Part B, as well as Part A, and so forth, because those
4 incentives are there, are intended to be there, and it may be
5 overkill to try to penalize the senior citizens because
6 they are remaining two or three or four days, when already the
7 hospital is encouraged to discharge them earlier anyway.

8 I tend to think we should stay with DRGs and try to
9 crank that down, rather than doing so much with copayments
10 and so forth, which really is penalizing the patient who has
11 got to be there anyway. There is not much choice in the patient
12 decision.

13 Ms. Burke. Senator Baucus, if I might for just a
14 moment, in addition to that, you are absolutely correct that
15 that was indeed one of the intentions of the proposal. The
16 other was to perhaps move away from what is now perceived as
17 being catastrophic cost-sharing, that is, cost-sharing that
18 begins at the 60th day. Although a large percentage of
19 Medicare's beneficiaries do not in fact ever reach that point,
20 the current structuring really hits those people who are in the
21 longest and the sickest, and there is some desire to reverse
22 that and spread those costs over a greater population, so
23 that there were really two incentives. The one, as you
24 suggest, is to create at the margin that incentive to get out;

1 the second is really to reverse what is perceived as being
2 unreasonable cost-sharing at a point when you are least able
3 to do it. So there are really two factors there.

4 The Chairman. Senator Durenberger.

5 Senator Durenberger. Let me make one comment on
6 catastrophic, because if there really is an interest here in
7 doing catastrophic, I have another offer to make, in effect.
8 One of the things you do not see in the Administration's
9 catastrophic is the Part A and Part B, and you do not see any
10 income-testing, in effect. All you do is see everything paid
11 after the 60th day. But going back to Item Number 1,
12 the modifying timing in rate of increase in the Part B
13 premium, John Chafee made me go out here a couple of months
14 ago and try to come up with an income-testing proposal, and
15 if anybody wants to hear about how we might income-test Part B
16 of Medicare, I have a proposal that you can consider. I
17 designed it as a cost-neutral proposal. If you want to save
18 some money, you can make it un-cost-neutral. Very simply,
19 what it does is it takes--the current premium is 25 percent
20 of program cost, and this coming year, I think it will be
21 \$16.60 per month deducted from everyone's premium. What I
22 have suggested is drop that back down to 20 percent, back
23 down to \$13.30, so that you protect the poor, low-income
24 folks, who are qualified for Medicare. That costs us
25 \$1 billion. How do you pick up \$1 billion? Well, you pick

1 up \$1 billion by taxing all Medicare participants in Part B
 2 one percent of their adjusted gross income, and that is
 3 cost-neutral. You just get down to the bottom of your tax form,
 4 and there is an extra line there that says, "Fill in one
 5 percent of your adjusted gross income, up to \$550 a year," which
 6 is 90 percent of the program cost, and that is your income-
 7 tested repayment for the actual program cost to provide you
 8 with that Part B insurance. If we kept it cost-neutral just
 9 at the one percent, half of the people would not pay anything
 10 at one percent of adjusted gross income. The other half would
 11 pay somewhere between one dollar and \$550. It is a relatively
 12 simple formula, and all it needs is the decision to move in
 13 that direction. You can go to 2 percent, you can make \$1
 14 billion; you can go to 3 percent and make a little more money.

(Whereupon, Senator Packwood assumed the Chair.)

16 Senator Packwood. Any other comments on Dave's
 17 suggestion?

18 Senator Chafee. I think in Medicare, we have got to get
 19 some kind of a means-testing. We have heard the statistics
 20 here from Sheila on where it is going as far as cost-wise, and
 21 everybody sits around and comes up with proposals which, in
 22 essence, really, as Senator Durenberger said earlier, are
 23 just shifting the burden to somebody else.

24 Senator Packwood. Yes, but Chuck Grassley raised a good
 25 point, when you shift the burden to the public, and you are

1 starting to see it now in health care, for which we allow total
 2 non-tax benefits. Unions and businesses together and employees
 3 and employers are beginning to grasp the fact that they are
 4 going to have to start moving to some kind of co-insurance or
 5 deductibles, or the costs are going to go through the roof.
 6 When you look at how relatively little we lose in terms of
 7 lost revenue because of the tax-free fringe benefit, and then
 8 try to imagine what it would cost us if we were providing
 9 through the government, through either a Medicaid or Medicare
 10 kind of program, that kind of health coverage, managed by the
 11 government, it would cost us so much more. The private sector
 12 has a way of taking care of it, when the costs get to a place
 13 where they cannot afford it, and there is much to be said
 14 about shifting that and letting the private sector decide
 15 how they are going to work out the copayment schemes.

16 Senator Danforth. Sheila, when we discussed in
 17 connection with Social Security, taxing the Social Security
 18 benefits over a certain level, that was in effect means-testing,
 19 was it not?

20 Ms. Burke. Yes, sir.

21 Senator Danforth. And if we were to apply exactly the
 22 same formula to taxing the insurance value of people over a
 23 certain income, that would also be means-testing on Medicare,
 24 wouldn't it?

25 Ms. Burke. Yes, sir, if it was related to income.

1 Senator Danforth. So you would be doing the same thing.
2 You would pick up about \$7 billion in four years, and just
3 utilize exactly the same mechanism that was used for Social
4 Security.

5 Ms. Burke. Yes, sir.

6 Senator Packwood. We have a vote now on the Tower motion
7 to table the Humphrey amendment to reconciliation; sense of
8 the Senate that the State Department increase the security of
9 the Marines in Beirut. Any objection to increasing the security
10 of the Marines? Anyway, that is what we are voting on in
11 just a few minutes.

12 Senator Moynihan. I think Secretary Schultz would take
13 exception to that. He is a Marine.

14 (Laughter.)

15 (Whereupon, Senator Dole resumed the Chair.)

16 The Chairman. Did the package pass while I was out?

17 (Laughter.)

18 Senator Packwood. We went to income-averaging on
19 Medicare, as best I could tell.

20 The Chairman. I think we are going to have this vote
21 and then move into the debt ceiling this evening and an
22 amendment on a freestanding bill by Senator Armstrong and
23 Senator Long. So I do not see any reason to come back here.
24 I would like to move again tomorrow morning. Does that cause
25 you a problem?

1 Senator Packwood. No. I have cancelled the other hearing
2 I had set.

3 The Chairman. And I understand we are making a lot of
4 progress on the insurance. I have talked with Mr. Chapoton.

5 Senator Moynihan. And we seem to be getting along on
6 this covered option.

7 The Chairman. I know there are other matters. Lloyd
8 was not here earlier when we raised the foundations. That is
9 one that is still up in the air. Treasury would just make
10 one change; present law, with some exception, that would take
11 care of just the one foundation, as I understand.

12 Senator Moynihan. Well, that is what we said, that you
13 and some others wanted to talk about that.

14 The Chairman. I would just say this. I think Treasury
15 is going to be available this evening and our staff, the Joint
16 staff, Democrat and Republican. If there are other additions
17 that were not properly addressed in your view, I assume
18 you would just about have to do it this evening. I do not
19 know what is going to happen tomorrow morning. What I do not
20 want to do is, after weeks and weeks of work, is offer a
21 package and have it rejected either on party lines--or, if it
22 appears we do not have the votes, I am not certain that I would
23 want a record vote tomorrow. I think we are going out of here
24 Friday, and it would not serve any purpose in the cause of
25 deficit reduction to have what I consider to be a fairly

1 well-balanced package, if we can put it all together,
2 defeated two days before we leave. But I would like to meet
3 at 10:00 in the morning. Will that give staff enough time to
4 go back?

5 Mr. DeArment. Yes, we have the whole evening, Mr. Chairman.

6 The Chairman. Is there anything else anybody wants to
7 raise at this point?

8 Senator Heinz, would you give Sheila any more information
9 on labs and pacemakers and so on?

10 Senator Heinz. Yes, Mr. Chairman, we will try and do that.

11 (Whereupon, at 5:45 p.m., the Committee was adjourned,
12 to reconvene Thursday, November 17, 1983, at 10:00 a.m.)

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