Rep. Jones Outlines Long-Term Joint Plan For Healthy Economy

Congressman James R. Jones (D-Oklahoma) outlined a bipartisan effort in the House of Representatives "to set in motion an overall game plan to revitalize the economic and industrial base of this country." His comprehensive discussion of the group's strategy for tax and fiscal policy was delivered at a luncheon session of the National Taxpayers Conference on April 22 in Arlington, Virginia. Among the members of the bipartisan coalition, Jones said, were the Democrats Ed Jenkins (Ga.), Ken Holland (S.C.), Andrew Jacobs, Jr. (Ind.), Cecil Heftel (Hawaii), and Sam Gibbons (Fla.); and the Republicans Barber B. Conable, Jr. (N.Y.), Bill Frenzel (Minn.), and Willis D. Gradison (Ohio).

Jones told the representatives of the state taxpayers' research organizations who comprise the NTC's membership that the coalition is seeking to develop three major policy areas.

First, they are working on the competitive position of the U.S. in world trade. "The kind of economy and the kind of growth that we give to the next generation of Americans," he said, "...will depend to a great extent on our competitive ability in world markets." One success the Tax Foundation Tax Index climbed 39 index points, or 13 percent. At the same time, prices rose 9 percent and real output by just over 2 percent.

Generally, during the last two decades, the Tax Index has outpaced both the rise in prices of goods and services and real output of the private business sector. This divergence has been especially pronounced since 1975, according to Tax Foundation researchers. From 1975 to 1979 the Tax Index jumped 65 percent, more than twice the 30 percent rise in prices, and over three times the 21 percent rise in the real output of the private business sector.

In the future, the Tax Foundation Tax Index will be computed on a

A new fiscal yardstick has just been unveiled by Tax Foundation economists—the Tax Foundation's Tax Index. The Index is designed to provide a continuing measure of trends in taxes, on a basis comparable to official indexes for other segments of the economy.

In this instance, the Foundation's researchers have charted the course of Federal, state, and local taxes as measured against general prices and real output of the private business sector. The news is not good.

Based on 1967 as 100, the Tax Index reached 336.4 in 1979, while the price index stood at 209.4 and the output index at 144.0.

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In the future, the Tax Foundation Tax Index will be computed on a

(Continued on page 2)

Taxes, Prices, and Output Index Numbers, 1967 = 100

<table>
<thead>
<tr>
<th>Year</th>
<th>Tax Index</th>
<th>Price Index</th>
<th>Output Index</th>
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<tr>
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<td>100</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>1965</td>
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<tr>
<td>1975</td>
<td>300.0</td>
<td>300.0</td>
<td>300.0</td>
</tr>
<tr>
<td>1979</td>
<td>336.4</td>
<td>209.4</td>
<td>144.0</td>
</tr>
</tbody>
</table>

Note: Tax Foundation's Tax Index, covering Federal, state, and local taxes, stood at 336.4 in 1979, based on 1967 as 100. The Price Index reached 209.4 in 1979, and the Output Index, 144.0.

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The Front Burner

By Robert C. Brown
Executive Vice President
Tax Foundation, Inc.

“Social Security Rollbacks—The Wrong Moves for the Wrong Reasons”

Election years being what they are, it will be truly surprising if we emerge from 1980 without a tax cut. Despite balance-the-budget rhetoric, the economy is pinching the average taxpayer too hard for the incumbents to resist the temptation to earn political brownie points with a highly visible tax cut. Social security payroll taxes are the most likely target, and therein lies the problem.

In 1981, both the base and the rate of OASDHI will increase. The base goes from $25,900 to $29,700, but the impact of this increase will be felt by relatively few taxpayers. The jump to 6.65 percent from 6.13 percent in the rate will hit everyone, and noticeably so. Hence, the political appeal of cuts in this area.

But such a reduction is the wrong move for the wrong reason.

• The benefit is largely illusory. Each 1 percent cut in the tax rate would give, on the average, less than $100 in tax relief to an individual taxpayer. At the same time, Congress and/or the White House would claim credit for $23 billion of tax cuts.

• A rollback in the maximum taxable base of the tax could be criticized as “regressive,” since it would benefit only relatively higher income earners.

• Given the present social security benefit structure, cuts in the payroll tax could do little for the capital formation sector of the economy, where the real long-term reforms are needed.

• Divorcing the social security system even further from the payroll tax will only increase pressure for general funding of OASDHI and make these costly programs more uncontrollable and more subject to political influences than they already are.

Rep. Jones
(Continued from page 1)

group has achieved was the passing, “by an overwhelming majority,” of the multilateral trade agreement. A second was reorganization of the executive agencies to “try to bring under one roof the various functions of the executive branch of the Federal government which deal with import and export policy” within the Commerce Department as a step toward a “coordinated trade policy.”

Other trade-related items being worked on by the coalition include taxation of overseas Americans, the administration of the Foreign Corrupt Practices Act, and “the antitrust laws as they pertain to business conducted outside of the United States.”

Fiscal policy is the second major item on the Congressmen’s agenda, according to Rep. Jones, with top priority given to developing a balanced budget for fiscal year 1981.

Jones told the state taxpayer organization executives that the coalition hoped “to follow that up this summer (Continued on page 4)

• Finally, the increases were put in place to shore up a system in danger of bankruptcy. As Barber B. Conable, Jr., Ranking Minority Member on the House Ways and Means Committee, said at last year’s Tax Foundation Annual Dinner:

“You can talk about how terribly burdensome to the economy it is to have raised the rate of tax on employer and employee recently; but you can’t forget that that’s the only element in the refinancing of social security which adds to the soundness of the system, and something that must be considered when you’re talking about what you want to do with the payroll tax.”

I would go one step further and insist that, when talking about any kind of tax cut—indeed, about any kind of tax change—the “soundness of the system” must get top priority. Because it hasn’t, we now find ourselves enmeshed in a tax policy shambles from which our leaders seem powerless to extricate the nation.

Tax Index
(Continued from page 1)

quarterly basis, as data become available, and compared with various sectors of the economy.

Further research on the Tax Index is being conducted at the Foundation to reveal trends in underlying components of the Index—by level of government and type of tax. Preliminary estimates, for example, indicate that the index of Federal taxes on a 1967 base stood at 331.0 in 1979, while the index of state and local taxes was higher, at 347.5. The disparity between the two indexes, according to Tax Foundation economists, results from the fact that during the late 1960s and early 1970s state and local taxes rose far more rapidly than did Federal taxes. In the latter part of the 1970s, however, these trends were reversed. From 1975 to 1979, the index of Federal taxes rose 74.0 percent, while the index of state and local taxes rose much more slowly, by 50.4 percent.

The accompanying table and chart depict trends in taxes, prices, and output for selected years since 1960.

Taxes, Prices, and Output Index Numbers, 1967 = 100

<table>
<thead>
<tr>
<th>Year</th>
<th>Tax Index</th>
<th>Price Index</th>
<th>Output Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960</td>
<td>61.9</td>
<td>86.9</td>
<td>73.2</td>
</tr>
<tr>
<td>1965</td>
<td>82.9</td>
<td>94.1</td>
<td>92.9</td>
</tr>
<tr>
<td>1970</td>
<td>132.2</td>
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<td>1975</td>
<td>203.5</td>
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<td>1976</td>
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<tr>
<td>1979</td>
<td>336.4</td>
<td>209.4</td>
<td>144.0</td>
</tr>
</tbody>
</table>

*All series are on a calendar year basis, compiled by Tax Foundation from national income accounts data published by the U.S. Department of Commerce. The Price Index is the GNP price deflator, and the Output Index covers GNP originating in the private business sector, in constant dollars.

Now Available

**Capital Depreciation Approaches Examined in latest "Evaluator"**

The need for change in the current tax treatment of capital depreciation and the leading alternatives open to Congress to achieve this goal are analyzed in the second issue of Tax Foundation's new "Federal Tax Program Evaluator." The "Evaluator" was started by the Foundation's tax policy section in January to provide a systematic analysis of proposed Federal tax legislation and major programs affecting the capital formation sector.

Current tax treatment is guided by accounting methods applied to asset lives that have a 20 percent plus or minus margin. These guidelines, called Asset Depreciation Ranges (ADR), contain more than 100 classifications. They are highly complex to administer and inadequately reflect replacement costs in a highly inflationary era. Depreciation reform is also a potentially powerful tool for increased capital formation and increased productivity since almost 50 percent of gross private savings come from depreciation deductions.

The Capital Cost Recovery Act of 1979 (H.R. 4646 and S. 1435), also known as the "10-5-3" plan, would establish a simple and mandatory depreciation schedule based on three categories of assets: (1) ten years for non-residential structures and structural components; (2) five years for equipment, including any tangible property not in the other two categories; and (3) three years for certain autos and light-duty trucks. This proposal has wide support in Congress, where, as of May 1980, it had 295 cosponsors in the House and 52 cosponsors in the Senate. The Department of the Treasury opposes the measure because of potential large revenue loss and because, Treasury claims, it represents a departure from a "true" corporate income tax.

The depreciation provision of the Tax Restructuring Act of 1980 (H.R. 7015) would replace the current rules for tangible personal property with a mandatory system simplifying the computation of depreciation and shortening the cost recovery periods. Eligible property would be classified in one of four accounts with recovery periods of 3, 6, 9, and 12 years. Eligibility for each account would be determined from the present ADR system with each asset assigned to the account with a recovery period at least 35 percent less than the midpoint of its current depreciation range. This proposal has not yet received much independent support or opposition because of its inclusion in the value-added tax legislation proposed by Chairman Al Ullman (D-Oreg.) of the House Ways and Means Committee.

Finally, any capital recovery system could be indexed for some measure of inflationary price changes, under an approach currently being discussed by economists but not yet incorporated in any bill before Congress. Each taxpayer would simply total his depreciation deductions and multiply by an index number for the depreciation period. This calculation could be made for any number of individual asset classifications or asset groups.

The economic impact of indexing depends on actual inflation rates and on the rates anticipated for future years. Indexing would influence the level of current investment by removing the future risks associated with inflation's erosion of the value of future depreciation deductions. Obviously, the lower the expected inflation, the less indexing will affect investment decisions.

The accompanying table highlights the comparison of alternative capital recovery systems by showing the discounted present value of tax deductions for a $10,000 investment in three types of assets and at various rates of inflation.

The key points in evaluating alternative capital recovery systems are:

- The structural changes of the Capital Cost Recovery Act greatly add to its appeal, particularly its simplicity in application which simultaneoulsy eliminates any remaining attachment to the "useful life" concept for tax depreciation purposes and provides many small businesses with a system they can use.

- No known analysis indicates that these depreciation proposals could pay for themselves in terms of Treasury revenues in the short term. In fact, they result in substantial Treasury losses, even with "feedback" figured in; but because capital consumption allowances make up such a substantial part of our gross savings, any changes in overall depreciation treatment obviously will ripple through the whole economy with major impact, encouraging private investment.

(Continued on page 4)

<table>
<thead>
<tr>
<th>Asset ($10,000 investment)</th>
<th>Current treatment</th>
<th>Capital Cost Recovery Act</th>
<th>Ullman proposal in H.R. 7015</th>
<th>Indexing</th>
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</thead>
<tbody>
<tr>
<td>Vehicle (3 yrs.)</td>
<td>$4,585</td>
<td>$4,869</td>
<td>$4,834</td>
<td>$4,815</td>
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<td>Office Equipment (6 yrs.)</td>
<td>4,686</td>
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<tr>
<td>Commercial Bldg. (40 yrs.)</td>
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<td>3,532</td>
<td>2,065</td>
<td>2,901</td>
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<tr>
<td>Vehicle (3 yrs.)</td>
<td>$4,453</td>
<td>$4,724</td>
<td>$4,700</td>
<td>$4,819</td>
</tr>
<tr>
<td>Office Equipment (8 yrs.)</td>
<td>4,386</td>
<td>4,823</td>
<td>4,700</td>
<td>5,278</td>
</tr>
<tr>
<td>Commercial Bldg. (40 yrs.)</td>
<td>1,128</td>
<td>3,158</td>
<td>1,633</td>
<td>2,944</td>
</tr>
<tr>
<td>Vehicle (3 yrs.)</td>
<td>$4,333</td>
<td>$4,627</td>
<td>$4,576</td>
<td>$4,823</td>
</tr>
<tr>
<td>Office Equipment (8 yrs.)</td>
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<td>4,614</td>
<td>4,567</td>
<td>5,289</td>
</tr>
<tr>
<td>Commercial Bldg. (40 yrs.)</td>
<td>916</td>
<td>2,922</td>
<td>1,353</td>
<td>2,985</td>
</tr>
</tbody>
</table>

*Discount factor 3 percentage points above the inflation rate and corporate rate at 46% in all cases.*

Source: Arthur Andersen & Company.
by amending the Budget Act itself to limit Federal spending to a percentage of gross national product." He said such a limit would signal international money markets "that we're serious about sound fiscal policy"; that it would encourage the Federal Reserve Board to lower interest rates by clearly demonstrating "that Congress is willing to do its part on fiscal policy"; and that it would have great psychological value "to all levels of our society."

"If the Federal government sets the load," he explained, "and says, in effect, 'We do have to tighten our belts; we do have to begin living within our means,' the example will be followed to a great extent by all levels of our society." He said that such an example would have "a great anti-inflationary impact."

"The use of tax policy to revitalize the economic and industrial base of this country" constitutes the third part of the "overall game plan" outlined by Jones.

The Oklahoma Congressman discussed in detail the sharp decline in investment in the private sector of the U.S. economy, pointing out that "we are almost at the bottom of the list." Lack of investment means "lower plant capacity or older plants," he said, and a continued falling behind competitors. "From 1973 to the present," he maintained, "we have had zero growth in productivity."

In the 1978 Tax Reduction Act, Congressman Jones said, the legislators established three principles which they hope to build on in the future: 1) "We opted for simplification." 2) "...the individuals who pay the taxes should get the tax relief"; and 3) "the Tax Code should be an incentive for investment, for capital formation." He outlined specific steps the bipartisan coalition has taken in each of these areas.

"This year," he said, "the focal point of what we're trying to do is a tax bill that will deal with internally generated capital," going on to describe the so-called "10-5-3" accelerated depreciation bill being sponsored by himself and Rep. Barber B. Conable, Jr. (R-N.Y.) in the House and by Gaylord Nelson (D-Wis.), Lloyd Bentsen (D-Tex.), Robert Packwood (R-Oreg.), and John Chafee (R-R.I.) in the Senate.

To this "second step on the road to capital formation," Jones linked the need for a limit "on the amount of money, on the percentage of the gross national product the Federal government can spend."

He described how, based on projections from the Congressional Budget Office, his spending limitation act (H.R. 5371) would enable a balanced budget and "a surplus of about $50 billion in fiscal year 1982," and a "balanced budget and a surplus of approximately $100 billion" in fiscal year 1983. The bill would also allow for an increase in Federal spending of "approximately 9 percent in FY 1982 and 1983," he said.

"If we're going to do the things that are important to rebuild our economy through the private sector, we're going to have to put some artificial restraint on that portion of the gross national product which is sopped up in government spending," he told the NTC members.

The National Taxpayers Conference is an association of 34 state tax research organizations joined together to facilitate the exchange of information and coordination on problems of common concern.

Congressman Jones's talk was part of the NTC's annual Washington Conference held from April 21 to April 23. During the conference the state taxpayer organization executives addressed themselves to a broad range of questions, including Federal tax issues, intergovernmental relations between state and national governments, spending limitation, unemployment compensation, and state and local pensions.

Other featured speakers at the Conference were Senator Harry F. Byrd, Jr. (I-Va.), Representative Al Ullman (D-Oreg.), and Richard Hite, Deputy Associate Director for Intergovernmental Affairs of the Office of Management and Budget.

**Depreciation**

(Continued from page 3)

investment in more productive assets.

- The structural changes in the Ullman proposal are not as extensive as in the Capital Cost Recovery Act, but they do represent a break from attempts to define appropriate "useful life" guidelines and provide comparable relief to the Capital Cost Recovery Act for shorter-lived assets.

- With inflation in the 5 percent to 7 percent range, indexing of depreciation could have more potential tax benefit than the Ullman proposal but less than the Capital Cost Recovery Act. At 10 percent inflation, indexing and the Capital Cost Recovery Act produce very similar results. With an inflation rate up to 14 percent over time, indexing could provide greater potential tax benefits.

Copies of the May 5 "Federal Tax Program Evaluator" are available at no charge from the Tax Foundation.