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THE VETO: A POSITIVE RESPONSE
TO ECONOMIC EMERGENCY

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February, 1981

... I believe it is clear our Federal Government is overgrown and overweight. Indeed, it is time for our government to go on a diet... . Government programs exist at the sufferance of the American taxpayer and are paid for with money earned by working men and women. Any program that represents a waste of their money - a theft from their pocketbooks - must have that waste eliminated or the program must go, by Executive Order where possible, by Congressional action where necessary... . I will not accept the excuse that the Federal Government has grown so big and powerful that it is beyond the control of any President, any administration or Congress. We are going to put an end to the notion that the American taxpayer exists to fund the Federal Government. The Federal Government exists to serve the American people and to be accountable to the American people. On January 20, we are going to reestablish that truth. ¹

THE 1980 ELECTION MANDATE

If the 1980 election was a mandate for anything, it was a mandate for an end to excessive government spending and "government regulations that work against rather than for the interests of the people."² During the campaign and since his inauguration, President Reagan has repeatedly pledged to use the full power of the Presidency to achieve these goals. It is clear that these issues were decisive in the outcome of the election.³

However, as the New York Times headlined its post-election summary, "Always, Winning Washington Is Easier Than Running It."⁴ To achieve the promised cutbacks in spending will require not only reductions in the amounts budgeted for particular programs, but also, at least in some cases, the elimination of entire programs and agencies. During the campaign, the departments of Energy and Education were mentioned as possible targets for abolition. Whether or not these departments are eliminated, it is likely that the abolition of at least some other programs⁵ will be sought by the

Reagan Administration and Congressional advocates of economy.⁶

The economy rhetoric, however, often overlooks the difficulty involved in the termination of a program. Obviously, to abolish a program is a more drastic step than merely to reduce its funding. But there are other reasons why abolition is more difficult to achieve in Congress than a reduction in funding. One is the fear that abolition will set a precedent that will be applied precipitately to other agencies or programs. Another and more effective deterrent is the pressure from economic or ideological interest groups that benefit from the program threatened with abolition. In the 97th Congress, the Republicans enjoy only a 53-47 majority in the Senate, while the House of Representatives is Democratic by a margin of 51 seats. It is true that House Republicans and some conservative Democrats are seeking to form a coalition to press for spending cuts and tax reductions.⁷ Nevertheless, it is far from certain that the Reagan economic program will be translated into effective Congressional action. This is particularly true with respect to the abolition of entire agencies. Given the modest Republican margin in the Senate and the precarious nature of any conservative coalition that might be formed in the House, the needed majority votes for abolition will be difficult or impossible to achieve in many cases.

THE PRESIDENTIAL ROLE IN THE LEGISLATIVE TERMINATION OF PROGRAMS

It is too narrow a view, however, to measure the prospects for abolition of programs merely in terms of the attainability of majority votes in Congress. The legislative process is broader and includes a significant Presidential role. One issue that

must be faced is what is the proper role of the President in cases where he sees the abolition of a program as clearly required by the public good and his electoral mandate and yet where the majority votes for abolition are not attainable in Congress. This question is particularly acute in cases where the failure of Congress to vote for abolition appears to be a response to interest group pressures or other motivations unrelated to the merits of the issue. The purpose of this essay is to suggest that the solution to this problem will be found in a constructive use of the Presidential veto. Too often, the veto is wrongly regarded as a merely negative device, indeed as a form of obstruction. Perhaps one good effect of the current economic crisis will be an increased appreciation of the veto as a positive power designed by the Framers to provide an opportunity for constructive leadership to deal with the sort of emergency we face.

The Constitution provides that the President "shall from time to time give to the Congress information of the state of the union, and recommend to their consideration such measures as he shall judge necessary and expedient."⁸ Article I, Section 7 of the Constitution provides for the Presidential veto:

Every bill which shall have passed the house of representatives and the senate, shall, before it become a law, be presented to the president of the United States; if he approve he shall sign it, but if not he shall return it, with his objections to that house in which it shall have originated, who shall enter the objections at large on their journal, and proceed to reconsider it. If after such reconsideration two-thirds of that house shall agree to pass the bill, it shall be sent, together with the objections, to the other house, by which it shall likewise be reconsidered, and if approved by two-thirds of that house, it shall become a law. But in all such cases the votes of

both houses shall be determined by yeas and nays, and the names of the persons voting for and against the bill shall be entered on the journal of each house respectively. If any bill shall not be returned by the President within ten days (Sundays excepted) after it shall have been presented to him, the same shall be a law, in like manner as if he had signed it, unless the Congress by their adjournment prevent its return, in which case it shall not be a law.

Every order, resolution, or vote to which the concurrence of the Senate and House of Representatives may be necessary (except on a question of adjournment) shall be presented to the President of the United States; and before the same shall take effect, shall be approved by him, or, being disapproved by him, shall be repassed by two-thirds of the Senate and House of Representatives, according to the rules and limitations prescribed in the case of a bill.

THE SEPARATION OF POWERS

The President's role in the enactment of legislation can be assessed only in the context of the general separation of powers. The Constitution divided the powers of government among three branches through a formal separation of powers, reinforced by a system of structural checks and balances. The framers saw that "The accumulation of all powers, legislative, executive, and judiciary, in the same hands, whether of one, a few, or many, and whether hereditary, self-appointed, or elective, may justly be pronounced the very definition of tyranny."⁹ However, as James Madison noted, "a mere demarcation on parchment of the constitutional limits of the several departments, is not a sufficient guard against those encroachments which lead to a tyrannical concentration of all powers of government in the same hands."¹⁰ "The great ordinances of the Constitution," in the words of Justice Oliver Wendell Holmes, "do not establish and divide fields of black and white. Even the more specific of them are found to terminate in a penumbra shading gradually from one extreme to the

other.... . When we come to the fundamental distinctions it is still more obvious that they must be received with a certain latitude or our government could not go on.... . It does not seem to need argument to show that however we may disguise it by veiling words we do not and cannot carry out the distinction between legislative and executive action with mathematical precision and divide the branches into watertight compartments..."¹¹

Through the system of checks and balances, each branch was given specified extraordinary powers, extending beyond the ordinary reach of its formal powers. These extraordinary powers, such as the Presidential veto, the requirement of Senate confirmation of some Presidential appointees and others, were designed as checks against possible encroachments by the other branches.¹² This limited overlapping of powers is essential to the constitutional scheme and is not at all inconsistent with the basic separation of powers. It is only where "the whole power of one department is exercised by the same hands which possess the whole power of another department," that, in Madison's view, "the fundamental principles of a free constitution are subverted."¹³ Discussing the principle of the separation of powers, the Supreme Court in Springer v. Philippine Islands¹⁴ observed that, "The existence in the various (state and federal) constitutions of occasional provisions expressly giving to one of the departments powers which by their nature otherwise could fall within the general scope of the authority of another department emphasizes, rather than casts doubt upon the generally inviolate character of this basic rule."

LEGISLATIVE POWERS OF THE PRESIDENT

The Constitution gave to the President certain specified powers which are legislative in nature: to provide Congress with information on the state of the Union; to recommend legislative measures which he believes are necessary and expedient; to convene or adjourn Congress under special circumstances; and to approve legislation prior to its taking effect, unless it is repassed by a vote of two-thirds of both Houses.¹⁵ These powers were given to the President because of the Framers' fear of abuse by the legislature. "In 1776 the complaint was with the Crown" and the "doctrine of separation of powers was seen as a means of controlling executive power."¹⁶ By 1787, however, "as a reaction to legislative excesses in the interregnum period, a true separation of powers doctrine emerged" as a means of checking abuses of the legislative power.¹⁷ "The legislative department," wrote Madison, "is everywhere extending the sphere of its activity and drawing all power into its impetuous vortex."¹⁸ "We have seen," warned the Federalist, "that the tendency of republican governments is to an aggrandizement of the legislative at the expense of the other departments. The appeals to the people, therefore, would usually be made by the executive and judiciary departments."¹⁹ As one modern commentator observed,

It had been the unrestrained conduct of the popular branch of the "omnipotent" state legislatures of the 1780s that, by and large, had brought together the framers of the Constitution of the United States. Might not the popular branch of a national legislature, Congress itself, also run riot? So the framers adopted the executive veto, lifting the provision from the constitution of Massachusetts which contributed so largely to the national Constitution.²⁰

It is true that the Constitution imposed on the President the primary duty to execute the laws once those laws are enacted.

"In the framework of our Constitution," wrote Justice Hugo Black for the Supreme Court, "the President's power to see that the laws are faithfully executed refutes the idea that he is to be a law-maker."²¹ Furthermore, "The Constitution does not subject this lawmaking power of Congress to presidential... supervision or control."²² This is obvious: the President is duty bound to carry out enacted laws. But a more pertinent issue is raised in the present economic crisis by the constitutional grant to the President of power to participate to a limited extent in the enactment process itself.

WHAT THE FRAMERS INTENDED IN CONFERRING THE VETO POWER ON THE PRESIDENT

The veto is the most important legislative power possessed by the President. The legislative character of the veto is indicated by its position in Article I, the legislative article, rather than in Article II, the executive article. In approving or vetoing bills, "[T]he President acts legislatively under the Constitution," said the Supreme Court in 1931, "but he is not a constituent part of the Congress."²³ The veto authority is limited, in that the veto can be overridden by a vote of two-thirds of a quorum of each House.²⁴ The only situation in which the President has an absolute negative on bills is where Congress, by its adjournment, prevents return of a bill; here the Congress is given no opportunity to override and the President's inaction alone, his "pocket veto," prevents the bill from becoming law.²⁵

The primary purpose of the framers in placing "a limited authority in the president to preclude the effectuation of national

legislation"²⁶ was to enable the President to prevent legislative encroachments upon his power. In Alexander Hamilton's words, "[t]he primary inducement to conferring the power in question upon the Executive is, to enable him to defend himself."²⁷ "But," as Hamilton noted, "the power in question has a further use. It not only serves as a shield to the Executive but it furnishes an additional security against the enactment of improper laws. It establishes a salutary check upon the legislative body, calculated to guard the community against the effects of faction, precipitancy, or of any impulse unfriendly to the public good, which may happen to influence a majority of that body."²⁸ The "secondary" purpose of the veto power, then, "is to increase the chances in favor of the community against the passing of bad laws, through haste, inadvertence, or design. The oftener the measure is brought under examination, the greater the diversity in the situations of those who are to examine it, the less must be the danger of those errors which flow from want of due deliberation, or of those missteps which proceed from the contagion of some common passion or interest. It is far less probable, that culpable views of any kind should infect all the parts of the government at the same moment and in relation to the same object, than that they should by turns govern and mislead every one of them."²⁹

It is important to stress this point, that the veto was intended for use not only in case of "an immediate attack upon the constitutional rights of the Executive," but also where the President seriously disagreed with proposed legislation on prudential grounds, that is, "in a case in which the public good was evidently and palpably sacrificed... ."³⁰ The framers believed "that there would be greater danger of his not using his power when necessary,

than of his using it too often, or too much."³¹ One purpose indeed, of making the veto qualified rather than absolute seems to have been to encourage its prudent exercise:

But the convention have pursued a mean in this business, which will both facilitate the exercise of the power vested in this respect in the executive magistrate, and make its efficacy to depend on the sense of a considerable part of the legislative body. Instead of an absolute negative, it is proposed to give the Executive the qualified negative already described. This is a power which would be much more readily exercised than the other. A man who might be afraid to defeat a law by his single veto, might not scruple to return it for reconsideration; subject to being finally rejected only in the event of more than one third of each house concurring in the sufficiency of his objections. He would be encouraged by the reflection, that if his opposition should prevail, it would embark in it a very respectable proportion of the legislative body, whose influence would be united with his in supporting the propriety of his conduct in the public opinion.³²

THE HISTORICAL DEVELOPMENT OF THE VETO

From the start, it was evident that the veto was not restricted to cases where the President thought a measure unconstitutional. Rather its use extended to objections based on wisdom or expediency. Professor Edward S. Corwin summarized the development of the veto power in this respect:

Washington exercised the power twice, once on constitutional grounds, once on grounds of expediency. Neither Adam nor Jefferson exercised it at all. Of Madison's six vetoes four urged constitutional objections to the measure involved, two objections of policy. Summing the matter up for the first century under the Constitution, the leading authority on the subject says: "From Jackson's administration to the Civil War vetoes on grounds of expediency became more frequent, but they were still in a decided minority. Since the [Civil] War constitutional arguments in a veto message have been almost unknown." The latter statement applies moreover equally to more recent years, if exception be made for one or two vetoes by Presidents Taft and Coolidge, both of whom had a special penchant for constitutional niceties. The notion that revenue bills are not subject to veto was punctured by Mr. Roosevelt's veto of February 22, 1944,

mentioned a moment ago, although the veto in question was overridden. The precedent thus set was clinched by President Truman on June 16, 1947, and this time the veto stuck.³³

"The first half-dozen Presidents," observed another commentator, "used the veto power sparingly, mainly to strike down legislation they considered unconstitutional."³⁴ However, "A change came with the inauguration of Andrew Jackson, the first President to have been elected by practically universal white manhood suffrage. Thus fortified by what he considered the mandate of the American people, Jackson initiated the practice of the President's deliberately passing independent judgment on the wisdom as well as the constitutionality of acts of Congress. His veto of the legislation rechartering the Bank of the United States, for example, was based upon his conclusion that it was bad legislation. The Whigs denounced this as executive usurpation of the legislative power of Congress. The Jacksonians defended it as "the tribunative voice of the people speaking again through their executive." Thus Jackson started the trend which has converted the Presidency into a potential, when not actual, one-man third house of the national legislature."³⁵

Presidents Jackson and Lincoln were notable in their use of the veto to obtain public support and to force or prevent changes in impending legislation.³⁶ The Post-Civil War period was one of "Congressional supremacy," in Woodrow Wilson's phrase.³⁷ Until the end of the nineteenth century, "Just about the only effective tool chief executives could employ was the veto. Its use increased sharply during this period. While most vetoes were exercised against private pension bills, some were used to defend the president's authority from congressional encroachment and the president's

policy positions from congressional attack. Hayes, for example, negated six laws containing riders that would have restricted his powers as commander-in-chief. Cleveland vetoed several major authorization and appropriation statutes."³⁸ Woodrow Wilson recognized the importance of the veto as the President's major weapon. He argues that "[t]he President is no greater than his prerogative of veto makes him; he is, in other words, powerful rather as a branch of the legislature than as the titular head of the Executive."³⁹

There is no doubt that the veto is properly useable to block legislation which the President believes to be unwise and is not restricted to objections on constitutional grounds. In Woodrow Wilson's words, "no President has hesitated to use the veto when his own judgment of the public good was seriously at issue with that of the houses."⁴⁰ As the Supreme Court noted in 1952, the lawmaking powers of the President are limited to "the recommending of laws he thinks wise and the vetoing of laws he thinks bad."⁴¹ "In theory," wrote Theodore Roosevelt in his autobiography, "the Executive had nothing to do with legislation. In practice, as things now are, the Executive is or ought to be peculiarly representative of the people as a whole... . Therefore, a good Executive under present conditions of American Life must take a very active interest in getting the right kind of legislation in addition to performing his Executive duties..."⁴²

The potential of the veto as a tool of presidential leadership in legislative matters has been established beyond challenge in recent administrations. Franklin D. Roosevelt, in Professor Corwin's phrase "appears to have broken all records in this field of endeavor as in several others... ! In contrast to Cleveland,

who devoted his unfavorable attention to pension, military, and naval relief measures, the range of subjects drawing the adverse action of Roosevelt has been as wide as the activity of Congress. Nothing too large or too small has escaped the penetrating eye of the President and his advisers. The following indicate that range of vision: agricultural relief, general appropriations, adjusted service compensation for World War veterans, interstate commerce, alien deportation, judicial review of administrative tribunals, flood control, protection of fisheries, homestead administration, Indian relief, tax and tariff policy, national defense, Philippine independence, Memorial Day observance, cemetery approaches, shorthand reporting, homing pigeons, District of Columbia street designations, parking meters, credit for beer wholesalers, control of funerals, and the exemption of religious periodicals!"⁴³

One reason for the importance of the veto is that a veto is rarely overridden. From 1789 through 1976 there were 1,367 regular vetoes, of which only 92 were overridden by Congress. In addition, there were 993 pocket vetoes which are beyond Congress' power to override.⁴⁴ This effectiveness of the veto is one reason why "it is at times a positive instrument of (the President's) legislative leadership."⁴⁵ Most commonly, this leadership is exercised through the threat of a veto and, if the objectionable measure does win approval in Congress, through the veto message in which the President explains his response for disapproving the bill. "The veto message is used not so much for the instruction of Congress as for the education of the electorate. Publicizing the message, Presidents have increased their public and party support. Even the threat of a veto can be a presidential maneuver designed to focus attention on some objectionable aspects of the

bill. The President warns Congress of an impending battle and an avenue through which Congress can avert it. The effectiveness of the technique is dependent upon the ability of the President to convince Congress that he is not bluffing. When Congress believes that the President will actually exercise the veto, the proponents of the measure must weigh compromise against the disadvantages of a public fight with the President."⁴⁶ These techniques, incidentally, were used effectively in both the Nixon and Ford Administrations.⁴⁷

THE USE OF THE VETO TO TERMINATE AGENCIES OR PROGRAMS

It is well settled that appropriation bills are subject to the veto power.⁴⁸ It may be objected that while the veto may properly be used on appropriation bills that initiate new programs or expand existing ones, it ought not to be used to terminate a program. There is, however, no basis for such a distinction. On the contrary, there is no limit whatever as to the subject of the bill upon which the veto may be exercised. The veto may clearly be used even where the subject matter is specifically committed by the Constitution to the power of Congress. In Holtzman v. Schlesinger,⁴⁹ the Court of Appeals summarily rejected the contention that the veto power did not extend to the war making power, even though that power is specifically vested by the Constitution in Congress:

While the Constitution vests the war declaring authority in the Congress, the Founding Fathers also conferred the veto power upon the President. (Art. I, § 7, cl. 2). The suggestion that the veto power is impotent with respect to an authority vested solely in Congress by the Constitution is unsupported by any citation of authority and is hardly persuasive.⁵⁰

It is well established by historical practice that the veto may properly be used on bills providing for the continuance of existing programs as well as on bills initiating new ones.⁵¹ Incidentally, the legitimacy of a veto of a bill to continue a program, or of any other kind of veto, is not dependent upon whether the veto of that bill was sustained or overridden. Indeed, as Alexander Hamilton indicated, one purpose of the framers in conferring the veto power was to encourage the President to use it to force reconsideration of a measure by Congress. "The oftener the measure is brought under examination... the less must be the danger of those errors which flow from want of due deliberation, or of those missteps which proceed from the contagion of some common passion or interest."⁵² This purpose is fully attained whether Congress sustains or overrides the veto in that particular case.

If there had ever been any doubt about the propriety of using the veto to discontinue existing programs or agencies, it was conclusively settled by President Andrew Jackson's veto of the bill to re-charter the Second Bank of the United States. The charter of the Bank, issued in 1816, was due to expire in 1836. In the summer of 1832, Congress passed a bill to re-charter the Bank. President Jackson vetoed the bill, explaining his reasons in one of the longest veto messages ever sent to Congress.⁵³ The veto was sustained in the Senate.⁵⁴ In his veto message, President Jackson emphasized his disagreement with the bill on policy as well as constitutional grounds.⁵⁵ Jackson's veto having been sustained, the Bank went out of business in 1836.⁵⁶ Jackson's veto of the Bank, one of the most notable vetoes in the

history of the Constitution, therefore, established that the veto could be used to terminate an existing program or agency. It also established that the veto power could be exercised, in such cases as well as in all others, on grounds of wisdom and policy as well as for constitutional objections.⁵⁷

It is evident from all the foregoing that the President has the right to veto a bill providing for the continuance of a program when, in his judgment, that program must be terminated. His veto is not absolute. It has the effect of forcing reconsideration of the measure by Congress, subject to the limitation that the veto will be sustained and the program will be terminated if one-third plus one in either House shall concur in the President's judgment. If this seems a drastic power to lodge in the President, it must be remembered that the framers debated it at length, in every aspect, and settled upon this qualified veto as a device, not only to protect the executive against legislative encroachment, but as well to provide the people greater security against the enactment of unwise laws.

THE EFFECT OF A SUSTAINED VETO IN TERMINATING A PROGRAM

Where a bill providing for the continuance of a program is vetoed and that veto is sustained, the termination of that program will generally follow as a matter of course. The most common Congressional spending procedure involves two stages, the authorization and the appropriation:

"There are two basic types of legislation. Authorization bills merely provide the programs for which Congress

must still appropriate funds in an appropriations bill before the program can operate:

Legislative proposals when enacted and become law are referred to generally as "legislative authority."

Funds for carrying on the work of the Government pursuant to "legislative authority" are provided in general and special appropriation bills, which usually originate in the House.

Enactment of A Law, S. Doc. No. 35, 90th Cong., 1st Sess. 5 (1967).

Moreover, under established Congressional procedures, substantive law provisions must be placed in authorization bills; they would be ruled out of order in an appropriation bill. House of Representatives Rules, para. 21, § 2; Jefferson's Manual and Rules of The House of Representatives 464-65, 470-71 (1971). Thus Congress can indicate its intent that a program shall continue only through authorization bills."⁵⁸

As long as Congress has authorized a program and appropriated funds for it, the Administration is bound to follow the Congressional intent and spend the money for that purpose.⁵⁹ This was made clear in recent cases involving the Presidential impoundment of funds.⁶⁰ Congress, incidentally, has since provided that the Administration must follow specified steps, subject to Congressional control, in order to impound funds.⁶¹

While the Administration is bound to spend appropriated funds according to the intent of Congress, it is conversely true as a "General proposition of the law" that the Administration "cannot be forced to spend any funds which have not yet been appropriated."⁶² Moreover, a mere authorization of a program by Congress "does not necessarily mean that a program will continue. Congress, of course, may itself decide to terminate a program before its authorization has expired, either indirectly by failing to supply funds through a continuing resolution or appropriation, or by explicitly forbidding the further use of funds for the programs, as it did in the case of the supersonic transport."⁶³

The termination of a program will obviously occur where Congress has explicitly forbidden further use of funds for the program. The supersonic transport program was terminated in this manner.⁶⁴ Or, a program will terminate when there is simply no law appropriating further funds for it. For example, the state block grant program administered by the Law Enforcement Assistance Administration received no appropriation for Fiscal Year 1981 and, as of this writing, it is not included in the projected budget for Fiscal Year 1982.

If there is no money authorized and appropriated for a program, it is clear that the program must terminate. "Authorization bills merely provide the authority for programs. The Congress must still appropriate funds in an appropriations bill before the program can be operated."⁶⁵

This conclusion is dictated by the language of the Constitution itself, which provides that "No money shall be drawn from the treasury, but in consequence of appropriations made by law..."⁶⁶ There are some circumstances, however, in which the strict application of this rule may be waived. For example, where there is a multiple year authorization for a program, coupled with a practice of Congress making late appropriations for that program, the Administration is bound to continue that program until the appropriated funds run out.⁶⁷ But the general proposition is true, that no program can continue if there are no funds appropriated for it. Moreover, if an authorization is no longer in force, whether through its expiration or the sustaining of a Presidential veto of it, a later bill providing an appropriation for it would seem to be out of order "under established Congressional procedures."⁶⁸ So for a program to continue, it seems clear that there must be both an

authorization and an appropriation for it. A sustained Presidential veto of either an authorization or an appropriation for the continuance of a program would therefore have the effect of terminating that program unless funds were made available from other sources for the program. Incidentally, since there is no item veto, a President may feel obliged to veto a measure as a whole although he would have approved part of it had it been presented to him separately.⁶⁹ The possibility exists, therefore, that a President may divert funds from other sources to ensure the continuance of a program where the appropriation for that program had been part of a bill which he vetoed for other reasons. The President has authority for such use of funds to some extent.⁷⁰ Therefore, to terminate a program by a sustained veto, a President must decide not only to veto it but also to refuse to divert other funds to keep the program alive.

ENTITLEMENTS AND WIND-UP FUNDS

No matter how a program is terminated, whether by express statutory prohibition or by a lack of further appropriations, there may arise a question of vested rights, or entitlements, and there may be a necessity for "wind-up" funds to close down the operation of the program. With respect to entitlements, it is possible for a grantee of funds under a program to acquire a constitutionally protected right to continued funding. This would depend on the intent of the governing statutes and on the contractual intent of the parties.⁷² For example, the plaintiff grantee claimed it was entitled to continued funding despite the abolition by statute of the funding requirement. In National Consumer Information

Center v. Gallegos, the court ruled that the grantee had "always received its grants on a year to year basis and grants made on this basis, even over a period of years, cannot create more than a 'unilateral expectation' of continued funding which is not entitled to constitutional protection."

An examination of the entitlement issue is beyond the scope of this study. The object of this study is to explore the legitimacy of the use of the Presidential veto as a device to terminate programs. It is not intended at all to suggest here that the termination of a program, by veto or otherwise, could interfere with further funding to which grantees have become entitled as a matter of constitutional right. If a program is terminated, vested entitlements must still be honored through legal action in the courts or separate appropriations or the use of such funds as are available for the discretionary use of the President.⁷² Even where there is no constitutionally vested entitlement, there may be a moral right in a grantee to further funding. This study is not intended to suggest that the veto should be used to terminate any program so as to interfere with either legal or moral entitlements to further funding. Similarly, funds necessary to "wind-up" a program must be provided despite the abolition of the program.⁷³ "Thus when Congress orders that a program go forth and later changes its mind, it is for the Congress in the responsible exercise of its legislative power to make provisions for termination."⁷⁴ However, the issues of entitlements and wind-up" funds are peripheral to the main concern of this study, which is the role of the President in effecting the actual termination of programs.

THE VETO AS A PRESENT DUTY

"While emergency does not create power," said the Supreme Court during the Depression of the 1930s, "emergency may furnish the occasion for the exercise of power."⁷⁵ It is difficult to imagine a more compelling occasion for the prudent exercise of the veto to terminate programs than the present economic emergency. The people have responded to that emergency with one of the clearest election mandates in history - a mandate for economy and for less government. But the execution of that mandate may be frustrated by inertia and the pressures of interest groups which are themselves both a cause and a result of the enormous increase in the size and profligacy of government. Yet the reality is that the economic survival of the nation requires that those pressures be subordinated to the public interest. To this end, President Reagan has undertaken a moral duty to use the legitimate powers of his office to their full extent.

In his address accepting the Republican Presidential nomination, Governor Reagan pledged, using the words of Franklin D. Roosevelt, that, "as an immediate program of action, we must abolish useless offices. We must eliminate unnecessary functions of government."⁷⁶ The veto is a proper and important means to the fulfillment of that pledge. Indeed, the expressed willingness of the President to veto bills for the preservation of useless agencies or programs, will be likely to operate to induce Congress to do the necessary termination job itself. But to the extent that Congress does not effectively respond to the crisis, the veto itself must be used. This is not to suggest that the veto should be used to interfere with benefits to which persons have become entitled as a matter

of legal or moral right. It is, rather, to say that where the President is convinced that the termination of a program is urgently required by the public good and by his electoral mandate, and where he is convinced that Congressional support for the continuance of that program is prompted by reasons unrelated to the merits of the program, in that case the President may properly conclude that he has not only a right but a moral duty to veto the continuance of that program. In accepting the Republican nomination Governor Reagan said, "I ask you not simply to "trust me," but to trust your values - our values - and to hold me responsible for living up to them."⁷⁷ It is clear that the prudent exercise of his veto power is part of that responsibility assumed by the President.

FOOTNOTES

1. Ronald Reagan, Address accepting the Republican Presidential nomination; New York Times, July 18, 1980, p. A8, col. 1 .
2. Ronald Reagan, televised address; New York Times, Oct. 25, 1980, p. 10, col. 3 .
3. New York Times, Nov. 9, 1980, p. 1, col. 1; Chicago Tribune, Feb. 6, 1981, Sec. 1, p. 1, col. 4 .
4. New York Times, November 9, 1980, Sec. 4, p. 11, col. 1
5. For convenience, the term "programs" will be used in this analysis in the broad sense to include entire agencies as well as particular projects conducted by those agencies. Except where otherwise indicated, the legal analysis with respect to the President's legislative role is basically the same with respect to both programs and agencies.
6. This paper is not intended to discuss the merits of particular programs or to suggest which ones ought to be eliminated. However, several programs have been mentioned by observers as possible candidates for elimination. Action is one example, see Lambro, How Sam Brown Is Politicizing Action, Human Events, March 24, 1979, 10; for a discussion of abuses in the administration of the Comprehensive Employment and Training Act, see Wall St. Journal (editorial), June 23, 1980; Washington Post, September 29, 1979, p. A22, col. 1; Washington Post, August 2, 1980, p. B1, Col. 1; see also the column of Nicholas von Hoffman, Chicago Tribune, January 17, 1981, sec. 1, p. 9, col. 1, urging elimination of taxpayer support for the Public Broadcasting Service; and see New York Times, February 4, 1981, p. 1, col. 7, discussing the reported intent of President Reagan to eliminate the Urban Development Action Grant program.
7. N.Y. Times, Jan. 7, 1981, p. A15, col. 7
8. Constitution, Art. II, Sec. 3
9. James Madison, The Federalist, No. 47
10. James Madison, The Federalist, No. 48
11. Springer v. Philippine Islands, 277 U.S. 189, 209-11 (1928) (Holmes, J., dissenting)
12. See discussion in Stewart, Constitutionality of the Legislative Veto, 13 Harv. J. on Leg. 593, 598 (1976)
13. James Madison, The Federalist, No. 47 (Emphasis in original)
14. 277 U.S. 189, 202 (1928)
15. Constitution, Art. II, Sec. 3, Art. I, Sec. 7; see Boesch, The President and the Item Veto: A Proposal, 18 St. Louis Univ. L. J. 407 (1974)

16. Levi, Some Aspects of Separation of Powers, 76 Colum. L.Rev. 371, 374 (1976)
17. Dixon, The Congressional Veto and Separation of Powers: The Executive on a Leash, 56 No. Car. L.Rev. 423 (1978)
18. James Madison, The Federalist, No. 48
19. James Madison or Alexander Hamilton, The Federalist, No. 49
20. Binkley, the President as Chief Legislator, in Congress and the President: Allies and Adversaries (Moe, ed., 1971), 63
21. Youngstown Sheet and Tube Co. v. Sawyer, 343 U.S. 579, 587 (1952)
22. Id. at 588
23. Edwards v. U.S., 286 U.S. 482, 490-91 (1931)
24. Missouri Pac. R. Co. v. Kansas, 248 U.S. 276 (1919); see discussion in Zinn, The Veto Power of the President (U.S. Government Printing Office, 1951), 25-26
25. See Kennedy v. Sampson, 511 F.2d 430 (D.C. Cir., 1974); Comment, The Veto Power and Kennedy v. Sampson: Burning a Hole in the President's Pocket, 69 N.W.U.L. Rev. 587 (1974)
26. Statement of Professor Philip B. Kurland, in Joint Hearings on S.373 Before the Ad Hoc Senate Subcommittee on Impoundment of Funds, 93rd Cong., 1st Sess. (1973), 400; see discussion in Salomon, The Case Against Impoundment, 2 Hastings Const. L.Q. 277, 288-89 (1975)
27. Federalist, No. 73; see discussion in Watson, Congress Steps Out: A Look at Congressional Control of the Executive, 63 Calif. L.Rev. 983, 1030-32 (1975)
28. Ibid
29. Ibid
30. Ibid
31. Ibid
32. Ibid
33. Corwin, The President: Office and Powers, 1787-1957 (1957), 279, quoting from Mason, The Veto Power (1891)
34. Binkley, The President as Chief Legislator, in Congress and the President: Allies and Adversaries (Moe, ed., 1971) 63)
35. Id. at 63-64
36. Wayne, The Legislative Presidency (1978), 11, 12
37. Id. at 13

38. Id. at 12-13
39. Wilson, Congressional Government (Meridian edition, 1956), 173
40. Wilson, Constitutional Government in the United States (1908), 73
41. Youngstown Sheet and Tube Co. v. Sawyer, 343 U.S. 579, 587 (1952)
42. Theodore Roosevelt, Autobiography (New York: Macmillan, 1913), 292
43. Corwin, The President: Office and Powers, 1787-1957 (1957), 281-82, quoting from Note, George C. Robinson, 36 Am. Pol. Sci. Rev. (Feb., 1942), 76
44. Report, Senate Library, Presidential Vetoes, 1789-1976 (U.S. Government Printing Office, 1978, ix)
45. Corwin, The President: Office and Powers, 1787-1957 (1957), 282
46. Boesch, The President and the Item Veto: A Proposal, 18 St. Louis U. Law Rev. 407, 414 (1974)
47. Wayne, The Legislative Presidency (1978), 159
48. For an enumeration of vetoes exercised against appropriations, see Report, Senate Library, Presidential Vetoes, 1789-1976 (U.S. Government Printing Office, 1978), 469-70
49. 484 F. 2d 1307, 1314 (2nd Cir., 1973)
50. 484 F. 2d at 1314; see discussion in Note, Constitutional Law - Justiciability - Veto Power - Standing, 15 Harv. Int. L.J. 143, 151-53 (1974)
51. See, for example, President Jackson's veto of S. 147 (22nd Cong., 1st Sess.) a bill

"To modify and continue the act entitled
"An act to incorporate the subscribers
to the Bank of the United States."

(See the Veto Message on S. 147 in Gales & Seaton's Register of Debates in Congress (22nd Cong., 1st Sess.), Vol. VIII, Part I, 1220 (July 10, 1832)) (Veto sustained); President Pierce's veto of H.R. 392 (33rd Cong., 2nd Sess.), a bill "making appropriations for the repair, preservation, and completion of certain public works, heretofore commenced under authority of law." (See the Veto Message on H.R. 392 and President Pierce's later explanation of that message at Messages and Papers of the Presidents (1897), Vol. VI, 2789-90) (Veto sustained); President Andrew Johnson's veto of H.R. 613 (39th Cong., 1st sess.), a bill "To continue to force and to amend an act entitled "An Act to establish a Bureau for the relief of Freedmen and Refugees, and for other purposes." (See the Veto Message on H.R. 613 at Cong. Globe, July 16, 1866, 3849-50) (Veto overridden); President Eisenhower's veto of S. 3158 (85th Cong., 2nd Sess.), a bill "To extend for one year certain programs established under the Domestic Tungsten, Asbestos, Fluorspar, and Columbium-Tantalum Production and Purchase Act of 1956." (See

the Veto Message on S. 3186 at Cong. Rec., Aug. 12, 1958, 17056)
(Veto unchallenged)

52. Federalist, No. 73
53. See Senate Jour., July 10, 1832, 433-46; see Messages and Papers of the Presidents, 1789-1908 (Richardson, ed. 1909), Vol. II, 576-606; see Buell, History of Andrew Jackson (1904), Vol. II, 264
54. S. Jour., July 13, 1832, 463
55. See Chitwood and Owsley, A Short History of the American People (1945), Vol. I, 450-51; Harlow, The Growth of the United States (1943), Vol. I, 384
56. See Chitwood and Owsley, A Short History of the American People (1945), Vol. I, 450-54; Buell, History of Andrew Jackson (1904), Vol. II, 294-328
57. See discussion in Corwin, The President: Office and Powers, 1787-1957 (1957), 279
58. Local 2677, American Fed. of Gov. Emp. v. Phillips, 358 F. Supp. 60, 74-75 fn. 15 (D.C., D.C., 1973); However, "Funds are made available to a number of federal programs, most usually those requiring long term commitment of funds for capital improvements, in a somewhat different manner. Authorization is followed by an issuance of "contract authority," which permits federal agencies or recipient state or local agencies under their supervision to make contracts and incur obligations payable at a later time, but does not give the Treasury authority actually to pay out any funds. As these obligations fall due, Congress then routinely appropriates funds for their payment." (Comment, Impoundment of Funds, 86 Harv. L.Rev. 1505, 1505, fn. 1 (1973))
59. Kendall v. U.S. ex rel. Stokes, 37 U.S. (12 Pet.) 524 (1838); U.S. v. Louisville, 169 U.S. 249 (1898); "Except as otherwise provided by law, sums appropriated for the various branches of expenditure in the public service shall be applied solely to the objects for which they are respectively made, and for no others." 31 U.S.C., Sec. 628; Greene County Planning Board v. F.P.C., 559 F.2d 1227 (2nd Cir., 1977), cert. den. 434 U.S. 1086 (1978)
60. In Pennsylvania v. Lynn (501 F.2d 848 (D.C. Cir., 1974)), the court held that the Secretary of Housing and Urban Development had authority under the governing statutes to suspend certain housing projects. "Whether Congress gave the Secretary the discretion here claimed is preeminently a question of intent." (501 F.2d at 852); compare Guadamuz v. Ash, 368 F.Supp. 1233, 1242 (D.C., D.C., 1973), where the court ruled that:

"Congress has told the Director of the Office of Management and Budget and the Secretary of Agriculture through its authorization and appropriations that it intends REAP to continue. Until Congress changes that command,

the defendants are bound to honor it."

In *State Highway Commission of Missouri v. Volpe*, 479 F2d. 1099 (8th Cir., 1973), the court held that the Secretary of Transportation could not impound funds except as Congress had authorized his exercise of such discretion. See also Decision B-156510 of the Comptroller General (Feb. 23, 1971), discussed in Local 2677, *AFGE v. Phillips*, 358 F. Supp. 60, 77 fn. 19 (D.C., D.C., 1973), in which the Comptroller General stated that the governing statutes did not authorize the Surgeon General to close all public health service general hospitals.

61. Budget and Impoundment Control Act of 1974, Public Law 93-344, 88 Stat. 297; see Hopkins, *Congress Controls Presidential Impoundments*, 60 ABAJ 1053 (1974); Salomon, *The Case Against Impoundments*, 2 Hastings Const. L. Q. 277 (1975)
62. Local 2677, *AFGE v. Phillips*, 358 F. Supp. 60, 73 (D.C., D.C., 1973)
63. Local 2677, *AFGE v. Phillips*, 358 F.Supp.at 75
64. Pub. L. No. 92-7, 85 Stat. 12; see discussion in Local 2677, *AFGE v. Phillips*, 358 F. Supp. 60, 75 (D.C., D.C., 1973)
65. *Guadamuz v. Ash*, 368 F. Supp. 1233, 1239 fn. 26 (D.C., D.C., 1973)
66. Constitution, Art. I, Sec. 9
67. "The clear Congressional intent of the multiple year authorization was that the program continue, especially in the light of the late appropriations process that has been detailed earlier. The multiple year authorization enables the Congress to evidence its intent to continue to fund a program (with the option to terminate it if it so pleases) without being forced to make that intent known by appropriating funds before the end of the fiscal year." Local 2677, *AFGE v. Phillips*, 358 F. Supp. 60, 75 (D.C., D.C., 1973)). See discussion in Comment, *The President's Constitutional Obligation to Maintain Congressionally Funded Programs and Agencies*, 8 Urban Law Annual 323 (1974)
68. Local 2677, *AFGE v. Phillips*, 358 F. Supp. 60, 74-75 fn. 15 (D.C., D.C., 1973)
69. Boesch, *The President and the Item Veto: A Proposal*, 18 St. Louis U.L.Rev. 407 (1974)
70. Fisher, *President and Congress: Power and Policy* (1972), 110-27)
71. 549 F2d 822, 828 (D.C., Cir., 1977)
72. For a discussion of Presidential discretion over expenditures through lump-sum appropriations, contingency funds, transfer authority

between classes of appropriations, transfer authority as to the time of expenditures and reprogramming, see Fisher, President and Congress: Power and Policy (1972), 110-27)

73. When Congress terminated the supersonic aircraft program, for instance, funds were appropriated "[f]or expenses, not otherwise provided for, necessary for the termination of development of the civil supersonic aircraft and to refund the contractors' cost shares, \$97,300,000, to remain available until expended." Pub. L. No. 92-18, 85 Stat. 40
74. Local 2677, AFGE v. Phillips, 358 F. Supp. 60, 79 (D.C., D.C., 1973)
75. Home Bldg. and Loan Ass'n. v. Blaisdell, 290 U.S. 398, 426 (1934)
76. N. Y. Times, July 18, 1980, p. A8, Col. 1
77. N. Y. Times, July 18, 1980, p. A8, Col. 1

February 27, 1981

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**AN ANALYSIS OF THE
REAGAN ECONOMIC PROGRAM**

INTRODUCTION

President Reagan's economic program, unveiled February 18, is remarkably consistent in both its practical and philosophical reliance on the free market. The tax package, based on the belief that individuals and corporations will respond to altered incentives, does not attempt to channel resources into favored activities, but instead relies on the market to direct the funds to the highest uses. Many of the spending cuts were advanced to eliminate or reduce federal programs which are properly in the province of the private sector: for example, the Export-Import Bank, Amtrak, the synthetic fuels program. Following a dictum of Adam Smith, the Administration also advocates reducing federal spending \$2 billion by assessing users fees for inland waterways, airports and Coast Guard services.

A more subtle, but equally important affirmation of the market is the Reagan Administration's decision to take a longer term perspective. The taxing and spending powers of the federal government will not be used in attempts to counter short-term economic fluctuations. Rather, the intent is to create a climate in which the government minimizes the distortionary effect of tax and spending, regulatory, and monetary policies on economic decision-making.

There are essentially two avenues of criticism of the Reagan proposals. The first is that the shift in perspective is ill-advised. Opponents would argue that traditional demand management policies are both adequate and necessary. Due in part to the dismal economic performance of the 1970s, this view is held by a rapidly dwindling minority. The position taken in this paper is that the private sector is inherently stable and that the longer term perspective is the correct one.

The second major area of inquiry concerns the composition, mix, and timing of spending and tax cuts. At issue are: 1) specific elements of budget and, more particularly, tax cuts and 2) the relative strength of the two forces, their effect on the deficit, and its effect on the economy. This paper addresses these questions.

THE REAGAN PROGRAM

President Reagan calls for FY 1982 outlays of \$695.5 billion, receipts of \$650.5 billion and a \$45 billion deficit. Included within these aggregates are \$41.4 billion in spending reductions, \$53.9 billion in individual and corporate tax cuts, and \$2 billion in proposed users fees. Another \$5.7 billion in off-budget cuts are outlined.

The program also contains \$4.4 billion in current fiscal year budget cuts and \$8.9 billion in tax cuts. Fiscal year 1981 spending would total \$654.7 billion with a \$54.5 billion deficit.

Table 1
CURRENTLY ESTIMATED BUDGET OUTLOOK
WITH PRESIDENT'S BUDGET SAVINGS AND TAX REDUCTION PROGRAM
(dollar amounts in billions)

	1981	1982	1983	1984	1985	1986
Target outlay ceilings	654.7	695.5	733.1	771.6	844.0	912.1
Estimated receipts after tax reduction plan	600.2	650.5	710.2	772.1	850.9	942.0
Target deficit (-) or surplus	-54.5	-45.0	-22.9	+0.5	+6.9	+29.9
<u>Share of GNP</u>						
Outlays	23.0	21.8	20.4	19.3	19.2	19.0
Receipts	21.1	20.4	19.7	19.3	19.3	19.6

It is not correct to compare the Carter Administration's FY 1982 budget numbers, submitted in January, with the Reagan proposal because the latter was based on decidedly more optimistic economic assumptions. The variance in forecasts affects the base from which the changes are calculated.

Because the Reagan program depends so much on supply-side tax cuts and changes in expectations, concepts which are overlooked or more difficult to measure in most econometric models, there was some disagreement within the Administration about the impact of the economic package. In a compromise, the forecast

anticipates real growth rates of 4.2 percent, 5.0 percent, 4.5 percent, 4.2 percent, and 4.2 percent from 1982 through 1986. The consumer price index will fall from 11.1 percent this year to 8.3 percent in 1982 and 6.2 percent in 1983.

Table 2
ECONOMIC ASSUMPTIONS
(Calendar Years)

	1981	1982	1983	1984	1985	1986
Nominal Gross National Product (billions)	\$2,920.0	\$3,293.0	\$3,700.0	\$4,098.0	\$4,500.0	\$4,918.0
(Percent Change)	11.1	12.8	12.4	10.8	9.8	9.3
Real Gross National Product (billions, 1972 dollars)	1,497.0	1,560.0	1,638.0	1,711.0	1,783.0	1,858.0
(Percent Change)	1.1	4.2	5.0	4.5	4.2	4.2
Implicit Price Deflator	195.0	211.0	226.0	240.0	252.0	265.0
(Percent Change)	9.9	8.3	7.0	6.0	5.4	4.9
Consumer Price Index* 1967 = 100	274.0	297.0	315.0	333.0	348.0	363.0
(Percent Change)	11.1	8.3	6.2	5.5	4.7	4.2
Unemployment Rate (Percent)	7.8	7.2	6.6	6.4	6.0	5.6

*CPI for urban wage earners and clerical workers (CPI-W).

ANALYSIS

The following analysis will be divided in two parts. The first will be an examination of the program elements designed to alter the economic incentives to work, save, and invest. These consist primarily of tax cuts and changes in programs, such as unemployment insurance and trade adjustment assistance. The second portion of the analysis will focus on the proposed spending cuts, their efficacy, and completeness.

ECONOMIC INCENTIVES

The Tax Proposal

President Reagan's tax proposal is a sweeping plan to return much economic decision-making to the purview of the free market. The proposal differs from tax cuts of recent years in that it is not aimed at stimulating aggregate demand through changes in the average tax rates. Rather, it is designed to increase work,

savings, and investment through changes in the marginal tax rates. The general philosophy behind this type of tax cut is that the many artificial relative price distortions make it better to lower marginal rates and decrease all biases rather than attempt to chip away structurally at each one individually.

If the plan is adopted, marginal tax rates for personal income will be cut by 5 percent, starting on July 1, 1981. In 1982 and 1983, these will be cut by an additional 10 percent per year, and in 1984 the plan calls for a final 5 percent cut.

There was debate as to whether the maximum tax on unearned income should be dropped immediately from 70 percent to 50 percent. Due to political circumstances, the decision was made not to effect that change immediately. However, when the plan is fully implemented, marginal tax rates will range from 10 percent to 50 percent.

Table 3
THE ADMINISTRATION'S PROPOSED TAX RATE SCHEDULES
FOR 1981, 1982, 1983, AND 1984

JOINT RETURNS

Taxable income bracket (dollars)	Present Law Tax Rate on income in bracket (percent)	Administration Proposal			
		1981 Tax Rate on income in bracket (percent)	1982 Tax Rate on income in bracket (percent)	1983 Tax Rate on income in bracket (percent)	1984 Tax Rate on income in bracket (percent)
\$ 0 - 3,400	0%	0%	0%	0%	0%
3,400 - 5,500	14	13	12	11	10
5,500 - 7,600	16	15	14	12	11
7,600 - 11,900	18	17	15	14	13
11,900 - 16,000	21	20	18	16	15
16,000 - 20,200	24	23	21	19	18
20,200 - 24,600	28	27	24	22	21
24,600 - 29,900	32	30	27	24	23
29,900 - 35,200	37	35	31	28	27
35,200 - 45,800	43	41	37	33	32
45,800 - 60,000	49	47	42	38	36
60,000 - 85,600	54	51	47	42	40
85,600 - 109,400	59	56	50	45	43
109,400 - 162,400	64	61	55	49	47
162,400 - 215,400	68	65	58	52	49
215,400 and over	70	66	60	53	50

The depreciation proposal is a slightly revised version of the Capital Cost Recovery Act of 1979, introduced by Congressmen Barber Conable (R-New York) and James Jones (D-Oklahoma). Under the President's plan the useful life concept is scrapped and the following categories and write-off periods would be established.

<u>Category</u>	<u>Write-off Periods</u>
o Automobiles and light trucks	3 years
o R & D capital	3 years
o All other machinery	5 years
o Public utility capital with a previous guideline life of under 18 years	5 years
o Owner-occupied non-residential structures	10 years
o Public utility capital with previous guideline life of over 18 years	10 years
o Other non-residential structures	15 years
o Low income rental housing	15 years
o Residential rental buildings	18 years

The 3-, 5-, and 10-year categories qualify for a super-accelerated write-off method involving an optimal combination of the "double declining balance" and "sum of the years digits" methods of depreciation. The 15- and 18-year categories must use "straight line" methods.

The 3-year category qualifies for a 6 percent Investment Tax Credit (ITC) and the 5-year category qualifies for a 10 percent ITC as does public utility capital in the 10-year category.

Structures in the 10-year category are considered to be section 1245 property for purposes of recapture, but the 15- and 18-year categories are considered to be section 1250 property. This permits the latter two categories to be subject to some capital gains taxation, as opposed to ordinary income taxation at the point of sale.

The Individual Cuts

The distinction between personal and business cuts is an artificial one. Individuals own all businesses and all business income accrues to individuals in one form or another. Thus, any tax change that affects personal saving affects businesses and any business tax cut will have an effect on personal well being.

The current tax code contains serious distortionary factors which lead to efficiency losses to society. Because of its multiple taxation of income from personal saving, the tax system creates a bias in favor of consumption and against saving. Less saving means less investment, which hampers economic growth.

High marginal tax rates on labor income artificially penalize the work effort. Once again, this causes an efficiency loss to society because the cost of working relative to leisure or non-market activity is distorted.

All economic decisions are made at the margin. That is, a worker makes his decision to work or not to work based on the tax treatment of additional dollars of labor income, not on the treatment of dollars earned in the past. If relative prices are distorted, it is only through changes in marginal tax rates that the distortions will be minimized.

What will the 30 percent across-the-board cut in marginal rates accomplish? Since the price of labor relative to leisure is exactly the after tax real wage rate, a cut in marginal tax rates on labor income will increase the marginal wage rate, thereby making work more profitable and leisure more costly.

The proposed individual cuts also indirectly attack the anti-saving bias in the tax code. In a manner similar to the effect on the work-leisure choice, the cuts in marginal rates will advantageously affect the save-consume decision. For example, the present tax rate on income from savings for a joint return of \$10,000 is 54 percent. By 1984, that will be reduced to 40 percent. Thus, for each one hundred dollars of savings incurred, the individual will retain an additional 14 percent.

Distortions, however, will still exist. There is still a multifold taxation of income from capital, including the taxation of interest income, dividends, and capital gains. Since the top marginal tax rate will be 50 percent, some of these distortions may be sizable.

A private investor in this bracket is taxed at the rate of 50 percent on new income. If he decides to invest some of his after-tax dollars, the return on his investment will also be taxed at the rate of 50 percent. Thus, the inherent bias against saving and investment continues, albeit at a diminished rate.

The individual cuts proposed by President Reagan are a good step in the right direction. Much more, however, remains to be done. Had the maximum tax on unearned income in the proposal been dropped immediately to 50 percent and had the reductions proceeded from there, the effects would be more positive.

The Depreciation Program

The President's proposed depreciation system is very close to being an ideal system. It accomplishes two things: 1) it

lowers the overall marginal tax rate on income from capital, and 2) it removes a very serious bias against investment in long-lived assets. Further, it diminishes much of the complexity and administrative burden associated with the present depreciation system.

By allowing firms to recover their capital more quickly, tax payments are deferred. Thus, the discounted value of these tax payments is lessened. For the same reason that double taxation of personal saving is distortionary, high marginal tax rates on the income from physical capital is distortionary. The current tax treatment poses a relative disincentive to investment in physical capital. Only the immediate expensing of capital assets will provide a climate in which investment decisions will be made irrespective of the tax system -- the desired, "neutral" result. Given political realities, the President's depreciation proposal approximates this desired neutrality.

It is firmly established in the economic literature that businesses are quite responsive to changes in marginal tax rates on income from capital. As a result of the new depreciation system we can expect new investment in productive, physical capital. A second major efficiency gain will come from the removal of a present-law bias against certain types of capital.

A major distortion that exists in the current tax code is the bias towards investment in short-lived assets at the expense of long-lived assets. By clinging to the "useful life" concept, present law insures that the relevant price of a long-lived asset relative to a short-lived asset is higher than would be the case in a non-tax world. This factor has contributed to a tax-induced shift of resources in our economy. It cannot be claimed that all the woes of the steel industry, for example, are to be blamed on this distortion, but certainly it has been a contributing factor.

This obsession with the useful life concept stems from the belief that depreciation for tax purposes must be matched with actual economic depreciation or the loss of value an asset suffers per accounting period. The traditional wisdom holds that such a system would be neutral with respect to assets of differing durabilities. Recent, more sophisticated analysis has shown that in the context of developments over time, the traditional wisdom is false and in fact discriminates against long-lived assets.

The proposed depreciation system will return the relative positions of short- and long-lived assets to their proper place. No longer will there a tax-induced incentive to favor investment in short-lived assets.

Critics argue that the Reagan tax proposal, by returning so much money to the private sector, will create a demand pull inflation. However, inflation occurs only if the rate of growth in the money supply exceeds the rate of growth of goods and services. Therefore, we need only worry about inflation if whatever deficit exists is funded through monetary expansion by

the Fed. As long as the Fed holds the line and follows a rational, steady, monetary policy, there will be no inflationary effects. The Reagan program specifies a desire for a gradual reduction in the money supply and credit growth rate to one-half the current levels by 1986.

The Administration also has indicated its support for the Federal Reserve policy of targeting money aggregates rather than interest rates. With deficits of \$54.5 billion in FY 1981 and \$45 billion in FY 1982, critics charge interest rates will skyrocket, thereby negating the beneficial effects of the tax cut.

The unprecedented change in the tax treatment of all forms of savings will, however, clearly increase the supply of loanable funds. Treasury Secretary Regan has estimated that as much as two-thirds of the tax reduction will be saved. The demand for loanable funds will also increase. It is possible that there might be some initial pressure on the capital markets. It should be noted that as interest rates rise, saving will become more attractive.

As new productive capacity comes on stream, output will expand and real interest rates will stabilize. Of course, if government spending is successfully cut, there would not be any initial pressure in capital markets. The best way to guard against any short-run increases in interest rates is to be vigilant on the spending side.

UNEMPLOYMENT COMPENSATION

Unemployment compensation has been designed to replace approximately 50 percent of a worker's former average weekly wage. The Federal-State Extended Unemployment Act of 1970, enacted to give additional assistance to unemployed workers during periods of high state or national unemployment, authorizes the extension of benefits at the regular weekly amount for an additional 13 weeks whenever the unemployment rate among insured workers (IUR) rises above some state or national "triggering" level. The state trigger takes effect when the state's IUR equals or exceeds, for a 13-week period, 120 percent of the average rate for the corresponding period in each of the previous two years and when such a rate is also at least 4 percent. A state also has the option to extend benefits if the state's overall unemployment rate is at least 5 percent for 13 weeks. When the national IUR reaches 4.5 percent, the national trigger is "on," and all states, even those with relatively low unemployment rates, become eligible for the extended benefits.

Unemployment compensation often has the adverse effect of making layoffs desirable for both employees and employers. Generous benefits and added leisure time often create significant work disincentives. An employer may be induced into laying off more workers during an economic downturn than he otherwise would

because the tax used to finance unemployment compensation is not always directly related to the unemployment experience of the firm. The extended benefits program adds to these distortions and generates even greater inefficiency.

The Reagan Administration has proposed restructuring the extended benefits program so that it would provide relief only to those areas plagued by high unemployment. The changes suggested are meant to achieve results analogous to tax cuts -- to restore work incentives by making employment relatively more attractive than unemployment. Specifically, the Administration's proposal would: 1) eliminate the national trigger; 2) change the way the state triggers are calculated; 3) raise the state trigger level from 4 to 5 percent of the IUR and, at state option, to 6 percent of the overall unemployment rate; and 4) strictly enforce the new rule requiring claimants to accept any reasonable job offer. Employment will be considered acceptable if it pays at least the minimum wage and can replace the individual's current unemployment insurance benefits. The first two changes will become effective July 1, 1981, while the third change would take effect only on October 1, 1982, thereby allowing necessary changes in state law. The 1980 Reconciliation Act already requires that the work test be applied to all extended benefits recipients after April 1, 1981. These modifications would save \$523 million in FY 1981 and \$1.2 billion in FY 1982.

Abolishing the national trigger would reduce costly unemployment insurance benefits in states that would otherwise not qualify for extended benefits. In addition, efficiency in the labor market would be enhanced by eliminating one of the sources creating work disincentives. When the national trigger is "on," benefits are extended in all states, even those with relatively low unemployment rates. Despite the considerably better job opportunities in such states, unemployment may rise as a result of increased work disincentives associated with the availability of more benefits.

The proposal would also exclude extended benefits recipients from the calculation of the IUR. The problem with using the IUR as a measure of unemployment for triggering purposes is that it creates an extended benefits program which becomes self-perpetuating. When the trigger is "on," all persons filing claims for benefits are included in the IUR. This results in exhaustees that normally would no longer be considered part of the labor force to be included in the IUR for an additional 13 weeks. On the other hand, when the trigger is "off," those same workers are excluded. Making this fundamental change would save substantial benefit payments in states that have already reached their triggering level. An even better approach, however, would be to use the overall unemployment rate in calculating the trigger because it would more accurately reflect job availability in the economy.

Raising the state trigger level is desirable because it would ensure that only those in genuine need receive assistance.

This, in part, is necessary to compensate for the changing composition of the labor force, which over the years has raised the natural rate of unemployment. Finally, strengthening the work test can eliminate much of the waste and fraud in the program.

Although the changes proposed are all desirable from an efficiency and equity standpoint, they do not go far enough. The extended benefits program should be eliminated entirely. The original purpose of unemployment compensation was to provide temporary relief. The program is not suited to correct long-term structural problems.

TRADE ADJUSTMENT ASSISTANCE

Trade Adjustment Assistance (TAA) was introduced in 1962 to assist workers suffering from increased imports, which were a direct result of government policies aimed at the liberalization of international trade. Today, however, the Secretary of Labor can declare workers eligible if imports have contributed significantly to unemployment and to a decline in the sales and/or production of the firm(s) in question. In other words, workers no longer have to prove that they are hurt by freer trade or that imports are the major cause of their injury. The primary purpose of the TAA program is to help workers adjust to changed economic conditions by easing the transition period between jobs. Assistance available to workers consists of: 1) trade readjustment allowances; 2) employment services; and/or 3) job search and relocation allowances. TAA benefits supplement unemployment insurance benefits by providing 70 percent of a worker's former average weekly wage, up to a maximum of the national average weekly manufacturing wage. Because unemployment insurance replaces only about 50 percent of gross earnings, TAA can be significant to the unemployed worker. In addition, these benefits are available for up to a year. In FY 1980, outlays on the program had grown to 1.7 billion dollars, which was more than six times as much as in the preceding year.

The major problem with TAA is that it compounds all the problems associated with unemployment compensation. The more generous benefits and the lengthier entitlement period exacerbate work disincentives. Greater benefits also discourage workers from seeking employment in more stable industries. Since employers pay no supplemental tax for laying off workers who would receive TAA benefits, an employer may find it profitable to lay off workers during a period of slack demand, assuming that relatively generous TAA benefits will induce a worker to wait to be rehired rather than actively search for a new job. Finally, TAA creates inequities by discriminating in favor of a select group of unemployed workers, those affected by imports.

The Administration proposes to extend TAA benefits only to those workers who have exhausted their regular unemployment compensation and to limit the size of these benefits to levels no

higher than those under unemployment insurance. An unemployed worker will be allowed to receive benefits from TAA and unemployment insurance for up to a year. These changes will become effective October 1, 1981, and could reduce spending by \$1.15 billion in FY 1982 alone.

The limitations proposed on the availability of TAA benefits would improve efficiency within the program markedly. The results of several studies seem to indicate that reducing the availability of benefits would dramatically mitigate pernicious practices of employees and employers alike. One such study found that TAA recipients were much more likely to have experienced temporary unemployment than their counterparts receiving only unemployment insurance. Moreover, they were much less likely to have changed their industry or occupation. It can be said that "one of the surest ways to bring about adjustment is to provide no assistance, and assistance that compensated for every burden would leave no incentive to adjust."¹ The generous assistance payments seem to act as a deterrent to workers from seeking employment in new areas, thereby artificially generating too strong an attachment to a vulnerable industry. The proposed changes are needed to restore work incentives and to discourage misuse of the program.

Although the proposed changes in TAA would result in great savings and lead to a more efficient allocation of resources, the program would still have some shortcomings. Even greater savings could be realized if the eligibility requirements were made more stringent by requiring workers not only to show that they were displaced as a direct result of U.S. international trade liberalization but that it had been the single most important cause of their injury. To further this goal, the role of determining eligibility should be returned to the International Trade Commission. The Department of Labor has all too often demonstrated a bias in favor of organized labor, many of whose members are TAA recipients. This is important because there often is only a very tenuous link between layoffs and increased unemployment from imports. Is greater compensation then justifiable for workers who are laid off because their firms failed to modernize or because workers have demanded excessive compensation and, consequently, have effectively priced themselves out of the market? Automobile workers, for example, currently receive a large amount of supplemental benefits despite the ruling by the ITC that imports were not a substantial cause or threat of serious injury to the U.S. auto industry. Instead, the Commission found that the recession, rising costs of credit, high gasoline prices, and the resulting shift in demand for small cars harmed the industry more than imports. Moreover, since workers produce goods and services for local, regional, national, and international markets,

¹ J. D. Richardson, "Trade Adjustment Assistance Under the U.S. Trade Act of 1974: An Analytical Examination and Worker Survey," National Bureau of Economic Research, Working Paper 556, September 1980.

and all of these workers may be affected by unfavorable conditions, why should import-affected workers receive preferential treatment solely because they happen to produce for an international market? This would be especially true if increased imports were a result of greater competition rather than trade concessions granted by the government. Import-affected workers, however, are sometimes considered more deserving because their layoff is the result of promoting a socially desirable policy, i.e., one meant to achieve the greater benefits associated with free trade. Although this may be true, workers in other industries often are displaced for equally deserving causes. For example, stricter environmental controls, more stringent safety standards, and deregulation are just a few. Yet workers who become unemployed as a result of these policies receive no supplements beyond unemployment compensation.

Finally, the availability of TAA after 26 weeks of unemployment compensation renders it more like an extended benefits program. These payments should be reduced drastically, while expanding the availability of the adjustment services.

SPENDING CUTS

The tax proposal, unemployment insurance, and trade adjustment assistance programs are designed to increase incentives to work and invest. To free the resources for the private sector expansion, the Administration proposes \$41.4 billion in on-budget spending reductions, another \$5.7 billion in off-budget cuts, and \$2.0 billion in users charges. While these cuts are significant, staggering to some, there is considerable potential for even greater reductions. Following the Administration's breakdown, the remainder of this paper will examine the President's proposal and suggest some additional reductions.

Revise Entitlements to Eliminate Unintended Benefits

The major cuts within this section are reform of the food stamp program (expected to save \$1.8 billion in FY 1982), elimination of both the social security minimum payment (\$1.0 billion) and the adult student payment (\$700 million), and the establishment of a cap on federal Medicaid payments to the states (\$1 billion). The Administration also proposes to limit cost of living adjustments for the civil service retirement system to once a year (\$510 million).

Some additional changes not recommended by Reagan which could provide substantial savings include limiting veterans' compensation payments to veterans and survivors whose disabilities are traceable either to combat or job-performance, eliminating all pensions for veterans and survivors which are not "service-connected" and dismantling the VA health care system.² Many of

² See Cotton M. Lindsay, "Veterans' Benefits and Services," in Eugene J. McAllister, ed., Agenda for Progress: Examining Federal Spending (Washington, D.C.: The Heritage Foundation, 1981), p. 286.

those currently receiving such assistance would fall back on the less remunerative Medicaid system but, despite that shift, the changes outlined above could save \$8 billion in FY 1982.

Reduce Middle-Upper Income Benefits

The February 18 budget also outlines cuts of \$1.6 billion through the child nutrition program and \$800 million restructuring the Guaranteed Student Loan and the Pell grant programs. In addition, the Student Loan Marketing Association (Sallie Mae) would no longer have access to the Federal Financing Bank. The latter would reduce federal credit demands and promote approximately \$15 billion of off-budget savings over the next five years. These three changes are directed at benefits received by the middle and upper income levels.

Some additional policy changes which would reduce the benefits received by the non-needy include introducing cost sharing in the Medicare program and lowering the payment limitation for agricultural deficiency payments from \$50,000 to \$10,000.

Recover Clearly Allocable Costs from Users

To achieve \$2.0 billion in FY 1982 receipts the Administration proposes to charge inland waterway, airport and Coast Guard users fees through increases in barge fuel taxes, aviation fuel taxes, and boat and yacht owner fees respectively. Another fee which would not only relieve the federal government of fiscal responsibility but, also promotes greater economic efficiency would be to incorporate effluent taxes in the 97th Congress' reauthorization of the Clean Air and Water Acts.

Apply Sound Criteria to Economic Subsidy Programs

The Administration also anticipates FY 1982 savings of \$10.3 billion from changes in subsidy programs. These include reductions in dairy price supports and Farmers Home Administration lending, elimination of the Economic Development Administration, restructuring the synthetic fuels program and cutting back alternative energy supply programs. Further reductions are proposed in the Amtrak, Postal Service, and mass transit operating subsidies and Export-Import Bank direct lending. The largest savings will result from the phase-out of Titles II-D and VI of CETA (\$3.6 billion in FY 1982).

There are two criticisms of the cuts in subsidies. First, in most instances the entire subsidy should be eliminated. Secondly, there were several programs which could have been included. In the cut list the Overseas Private Investment Corporation, agricultural deficiency payments, and U.S. flagship subsidies are all excellent candidates for elimination.

Another possibility would be to terminate the Strategic Petroleum Reserve. The immediate decontrol of oil prices has

created the necessary incentive for the private sector to stockpile reserves. Because there are a number of oil companies, or even entrepreneurs, it is very likely that their summed expectations regarding a future embargo and its severity, will be more accurate than the government's. Thus, the stockpile will be more efficiently maintained by the private sector.

Stretch Out and Retarget Public Sector Capital Improvement Programs

The critical elements of this section are an 11 percent reduction in planned water resources projects, deferring municipal water treatment grants, cutting urban mass transit grants, and slowing down highway construction grants.

The criticism is not with what is cut but rather with what remains. Sewage treatment plants, mass transit grants, and even water resource projects are local and regional responsibilities. Rather than defer or stretch out these programs, an orderly termination should be enacted.

Improve Fiscal Restraint on Other Programs of National Interest

The \$3.2 billion in FY 1982 savings contained in this section is derived from a large number of relatively small cuts. Some of the more prominent include impact aid, vocational education, NASA, and foreign aid programs, such as PL 480 and multilateral development banks.

The programs contained within this heading offer a unique opportunity for experiments designed to increase both private sector contributions and more desirable outcomes. For instance, in scientific research the federal government could promote private involvement by changing the rules of appropriability, encouraging research associations, engaging in international cost sharing, and even offering a retroactive prize program.³ A greater reliance on market mechanisms could considerably enhance the efficiency of such programs while permitting reductions in federal spending.

Consolidate Categorical Grant Programs into Block Grants

To reduce administrative expenses and promote greater state discretion, the Reagan Administration proposes to consolidate 45 education programs into two block grants, one to the state, the other to the local education agencies. It is also proposed that 40 federal health and social services programs be consolidated into one or more block grants to the states.

³ See Richard Speier, "General Science, Space, and Technology," in McAllister, op. cit., p. 63.

Reduced Overhead and Personnel Cuts

To attain greater personnel and management efficiency, the Administration has proposed a number of cost savings measures. In defense, these include the increased use of contracting services, multi-year procurement, and annual cost of living adjustments for federal retirees. Also expected to offer substantial savings are the ceiling on federal civilian employment, and overhaul of the federal pay comparability standard.

Another defense efficiency measure would be to increase the term of first enlistment and curtail re-enlistments.⁴ By reducing accessions, the training costs could be reduced. In addition, less retention of first-term enlistees would reduce the retirement liability.

CONCLUSION

The Reagan program embodies the changes in economic perspective, tax policy, and federal spending necessary to bring about a more efficient and productive economy. There are two caveats, however. The first is that regardless of how Congress alters the plan or how it fares in the short run, the Administration should continue to pursue the current course. The reason is not only that the program is sound, but that consistency is essential to altering expectations.

The second warning is that should Congress fear the tax cut to be too large, it should cut spending even more deeply than the Reagan proposals, rather than drastically alter the tax proposal. It is critical that the marginal tax rate cuts and the accelerated depreciation schedule remain intact.

Peter G. Germanis
Policy Analyst/Economics

Eugene J. McAllister
Walker Fellow in Economics

David G. Raboy
Institute for Research on the
Economics of Taxation

⁴ See William Schneider, Jr., "Defense," in McAllister, op. cit., p. 1.

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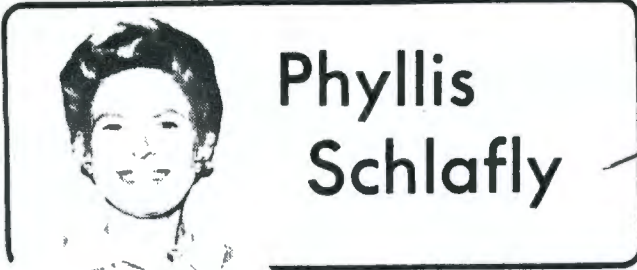
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Phyllis Schlafly

file Economic Program

Stockman's bold new program

By PHYLLIS SCHLAFLY
Copley News Service

Ronald Reagan's head of the Office of Management and Budget, Dave Stockman, faces the biggest and most immediate challenge of the new administration.

His goal is to reduce the Misery Index — the inflation rate, plus the unemployment rate, plus the interest rate. His problem is that the real gross national product is declining at the same time that federal outlays are rising with accelerating momentum.

The federal outlays which increase because of higher inflation include indexed Social Security and pension benefits, plus price re-estimates of Medicare, food assistance and defense fuel costs. The federal outlays which increase because of higher interest rates include interest on the national debt, student loans, rural housing programs and FSLIC.

The federal outlays which increase because of higher unemployment include unemployment insurance, trade readjustment assistance, assistance payments, Medicaid, food stamps and federal supplemental unemployment insurance benefits.

The increased federal outlays due to general economic conditions include Defense Department procurement, non-defense procurement, Small Business Administration disaster loans, Corps of Engineers, EPA sewer construction and VA construction.

Just as one illustration of how these federal outlays

are leaping forward at a frightening rate, the estimates for fiscal year 1981 trade adjustment assistance (to auto workers or others who lose jobs due to imports) exploded within six months from \$400 million to \$2.5 billion. This effect is what Stockman calls the automatic "coast-to-coast soup line" in the federal budget.

The credibility of our monetary system is eroding rapidly. It is now self-evident — and widely reported — that the high-interest-rate policy of the last months of the Carter administration not only failed to slow down inflation, but actually increased it.

Another accelerating problem is what Stockman calls the "ticking regulatory time bomb," that is, the quantum increase in the "regulatory burden" which will occur during the next two years unless immediate steps are taken. New environmental safety and energy compliance costs scheduled for the early 1980s are estimated at \$100 billion.

For example, the already battered auto industry will be hit with \$10 billion to \$20 billion in additional capital and operating costs in order to comply with federal regulations which have modest to zero social benefits. These new regulations include new or tougher standards on air bags, tail pipes, bumpers, engine emissions, noise, warranties and compliance procedures and paperwork.

The expectation of high and permanent inflation has killed the long-term bond and equity markets. We

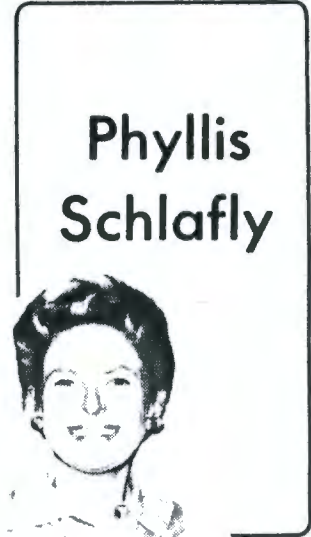
must build confidence that inflation will be checked if we are to regenerate a capital spending boom.

Such measures as a hiring freeze and small overall percentage budget cuts cannot make much of a dent in the tremendous economic problems. Vigorous capital spending can come only from tax cuts on the types of income that will go into investments, a dramatic rescission of the oppressive regulatory burden on business and a restoration of confidence in the future of our economy.

Stockman urges a bold 10 percent Kemp-Roth tax cut in 1981 and again in 1982, reduction of the top income tax rate on unearned income to 50 percent, a further reduction in tax rates on capital gains, and a substantial reform of corporate tax write-offs for depreciation.

Finally, Stockman recommends a specific list of items for his "stabilization and recovery program." These include a modest deferral of federal capital investments such as the spending on highways, airports and national parks, a careful pruning of overlap and abuse in food stamps, cash assistance, Medicaid, disability, heating and housing assistance, and unemployment compensation, and a cutback of low-priority programs such as NASA, CETA, the Community Development Program, urban parks, impact aid, ACTION, some Energy Department programs and the arts and humanities.

Stockman's proposals are bold — but the Misery Index demands bold action. We've suffered long enough at the hands of the Keynesian borrow-and-spend, deficit-and-inflation economists. It's time to give the reins to "supply-side" economists.



Phyllis Schlafly

SUPPORT FOR THE PRESIDENT'S ECONOMIC PACKAGE"BUSINESS" REPORT

To date, the Office of Public Liaison has conducted the following list of briefings/meetings with members of the business community in support of the President's economic package:

- a. Two Presidential outreach meetings.
- b. Nineteen White House briefings for coalitions.
- c. Forty follow-up meetings with (a) and (b) groups.
- d. Three OEOB 450 trade association and corporate maxi-briefings.
- c. Twelve speaking engagements.

The key active coalitions are providing unprecedented support for the President's economic package. There are currently 292 coporations which are active members of the Budget Control Coalition. This compares with the following levels of some earlier, successful efforts:

- a. 109 involved in the defeat of the Consumer Protection Agency.
- b. 143 rallied to assist in the defeat of Labor Law Reform.
- c. 137 backed the defeat of common situs picketing.

Like the effort by the conservatives, there appears little doubt that the business community lobbying will totally dwarf any earlier effort. The package contains several key items that the business community has been championing for a long time, most notably an accelerated depreciation schedule.

These coalitions, which have grown "light years" in sophistication over the past five years, are equipped with virtually limitless resources. This resources, as follows, can be brought into play when the business community is involved in issues that strike at the heart of the profitability:

- a. Direct lobbying by paid Washington lobby personnel and other staff.
- b. Personal CEO visits to M/C, supported by office visits of officers of these corporations; ie a day in Washington.
- c. Task forces of nationwide government relations personnel brought to Washington to focus on visits to key M/C.
- d. Phone call campaigns directed from grassroots PAC's.
- e. Use of association and company magazines, with the Chamber alone able to deliver a 2.1 circulation
- f. Messages to stockholders, especially those contained in the mailing of quarterly dividend checks. (Note: four of these are already underway.)

- g. Letter-writing campaigns supported and influenced within company employee organizations.
- h. Video-tape and live lectures to both employee organizations and the community.

While the actual number of groups involved would be too long list, several key coalitions are spear-heading the effort. For information, these are as follows:

- a. Budget Control Working Group (292 corporations).
- b. U.S. Chamber of Commerce.
- c. Business Roundtable
- d. National Association of Manufacturers.
- e. National Federation of Independent Businesses.

These groups have a self-interest in being involved, however they need a high level of involvement in order to justify the level of expense necessary to provide support of this order of magnitude. Your help and assistance is needed on a continuing basis in order to sustain this massive effort.

950: UNDISTRIBUTED OFFSETTING RECEIPTS
 (in billions of dollars)

	1982		1983		1984	
	BA	O	BA	O	BA	O
President Reagan's budget.....	-32.05	-32.05	-34.85	-34.85	-37.40	-37.40
Reestimates:						
Changes due to economic assumptions	-2.10	-2.10	-4.85	-4.85	-7.50	-7.50
Other reestimates.....	-0.05	-0.05	-0.30	-0.30	-0.60	-0.60
President Reagan's budget reestimated....	-34.20	-34.20	-40.00	-40.00	-45.50	-45.50
Chairman's recommendation.....	-34.60	-34.60	-40.20	-40.20	-45.60	-45.60
Chairman's recommendation adjusted 1/....			-34.20			

1/ For unattainable or double-counted administrative savings and unrealistic policy savings.						

Proposed efficiencies.....	-0.40	-0.40	-0.20	-0.20	-0.10	-0.10

The recommendation assumes savings through the resolution of audit findings by the various agencies. The estimate of this function represents receipts that cannot yet be assigned to a specific function or agency by GAO. This "cut" is not realistic.

DAVID MICHAEL STATON
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COMMITTEES:
COMMITTEE ON
INTERIOR AND INSULAR AFFAIRS
COMMITTEE ON
SMALL BUSINESS

Congress of the United States

House of Representatives

Washington, D.C. 20515

April 27, 1981

FYI
MCB
File
Economic
Package

Mr. Morton C. Blackwell
Special Assistant
The White House
Washington, D.C. 20500

Dear Mr. Blackwell:

In the discussions about President Reagan's Economic Recovery Program, two points escape notice. I wish to share them with you.

First is the matter of the Reagan multi-year, across-the-board tax cuts. They are opposed by the same people in Congress who brought us the present economic chaos. Their counterproposals will do more of the same. President Reagan needs the tax cuts that his program calls for, or economic recovery is endangered. Plus -- all Americans deserve a tax cut.

Second is the matter of inflation itself, how it developed, and why we cannot seem to get rid of it. Realizing that American ingenuity can solve any problem, the fact that we still have inflation points to the obvious conclusion that somebody wants it. Somebody benefits from it! Somehow, over the past decade, enough people profited from inflation so that there was insufficient incentive to halt it. Those who had the power to do something, did nothing to slow it. In fact, they helped it along! Many of them now oppose the tax cuts.

The attached sheets show the strong motivational forces which have encouraged inflation. President Reagan's Economic Recovery Program will neutralize those forces. That is the only way: We must take away the incentives for people to profit from inflation. At this critical crossroad in American history: (1) We either permit our government to borrow itself into bankruptcy, or (2) we use our national willpower to stop inflation.

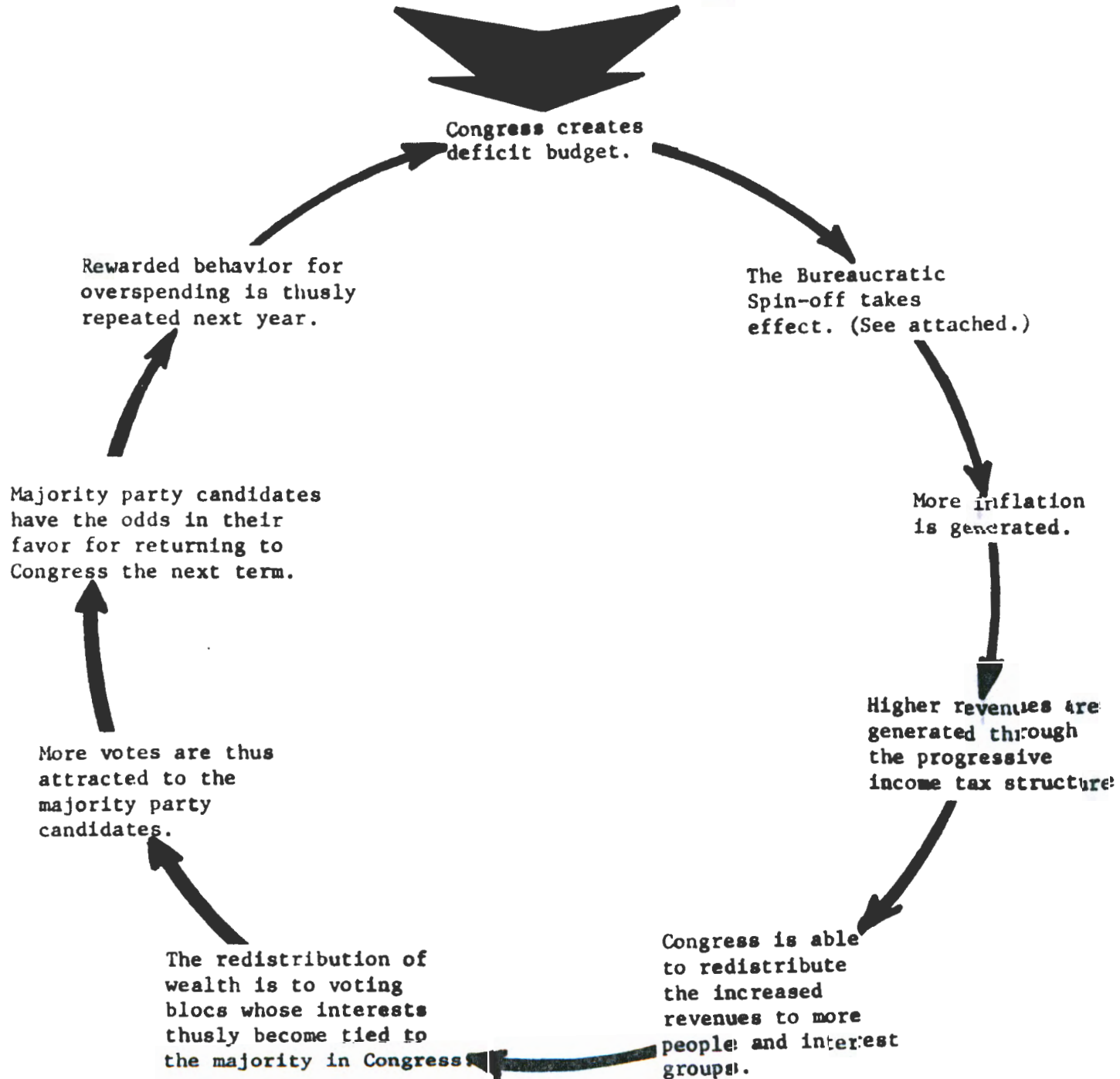
President Reagan has the will of the people behind him to take the second road. The people of America are committed to him. So am I.

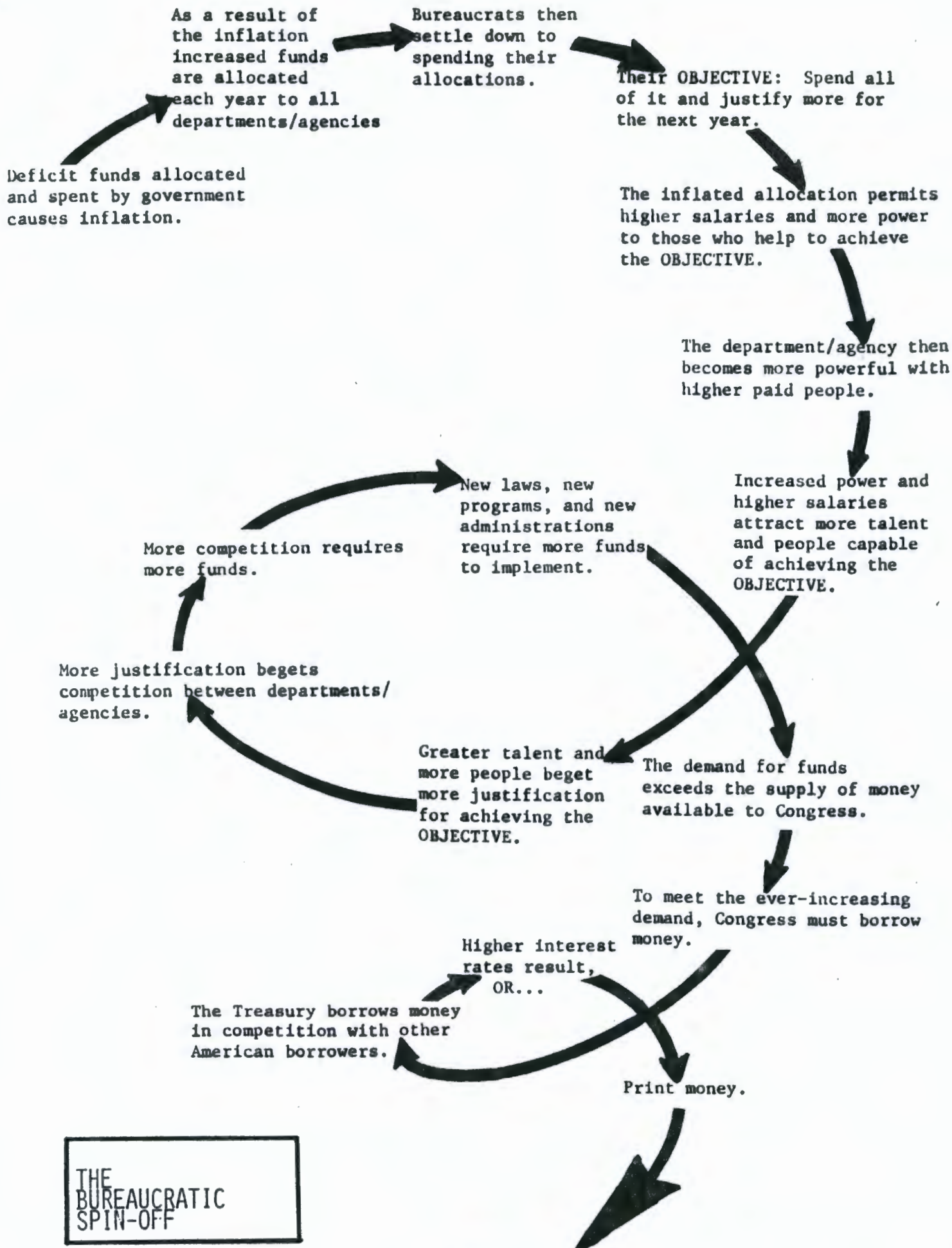
With best wishes for you, I remain

Sincerely yours,

David Michael Staton
Member of Congress

THE DRIVING FORCES OF INFLATION





THE
BUREAUCRATIC
SPIN-OFF

MORE INFLATION

BCD 4/17/81

THURSDAY, JULY 2, 1981

FOR RELEASE: WEEK OF MONDAY, JULY 6, 1981

CONTACT: BRYAN WIRWICZ, 202-225-4901 (O)
202-547-6684 (H)

SECOND ROUND OF TOWN MEETINGS INDICATES PEOPLE SUPPORT REAGAN PROPOSALS

One of the most frustrating things about Washington D.C. is the feeling there that elected officials know better than the people do what the people need and want. The town meetings I've been holding these past several weeks and those I held earlier this year have given me excellent opportunities to talk with hundreds of people from all across the district about a variety of problems and issues the Congress will be voting on later this year.

Despite shifting public opinion on other issues, support for the Reagan Economic Recovery Program remains overwhelming. The people just haven't bought the propaganda that many organizations are spreading that the poor, the handicapped and the elderly will be hurt by the president's program.

The people I've talked with have told me that if their taxes are cut, they'll put those dollars in savings accounts or other money-making ventures. That runs contrary to the "experts," who say everyone whose taxes are cut will run out and spend every last cent at shopping malls. That additional saving means jobs for carpenters, bricklayers and others in the housing construction industry -- an industry that has been hurt simply because there isn't enough money in banks and savings and loans for home construction or mortgage loans.

The people I've talked with have told me that they want government spending cut, so that they can spend more of their paychecks themselves -- rather than sending so much of their checks to Washington in taxes. In a loud and almost unanimous voice, my constituents tell me they want to see Austin and even Houston assume many of the powers and responsibilities Washington has possessed. The people feel closer to their state and city governments than to Washington -- and it's time we put the power back with the people.

These two elements -- lower taxes and less federal spending -- dominated this round of town meetings. Those were the same two issues that dominated my first series of town meetings. That tells me something. It tells me the people in this area support our president's economic recovery program, just like I do.

THE WHITE HOUSE

Office of the Press Secretary

For Immediate Release

September 24, 1981

ADDRESS BY THE PRESIDENT
TO THE NATION

The Oval Office

9:00 P.M. EDT

THE PRESIDENT: Good evening. Shortly after taking office I came before you to map out a four-part plan for national economic recovery: tax cuts to stimulate more growth and more jobs, spending cuts to put an end to continuing deficits and high inflation, regulatory relief to lift the heavy burden of government rules and paperwork, and, finally, a steady, consistent, monetary policy.

We've made strong, encouraging progress on all four fronts. The flood of new governmental regulations, for example, has been cut by more than a third. I was especially pleased when a bipartisan coalition of Republicans and Democrats enacted the biggest tax cuts and the greatest reduction in federal spending in our nation's history. Both will begin to take effect a week from today. These two bills would never have passed without your help. Your voices were heard in Washington and were heeded by those you've chosen to represent you in government. Yet, in recent weeks we've begun to hear a chorus of other voices protesting that we haven't had full economic recovery. These are the same voices that were raised against our program when it was first presented to Congress. Now that the first part of it has been passed, they declare it hasn't worked. Well, it hasn't. It doesn't start until a week from today.

There have been some bright spots in our economic performance these past few months. Inflation has fallen and pressures are easing on both food and fuel prices. More than a million more Americans are now at work than a year ago, and recently there has even been a small crack in interest rates. But let me be the first to say that our problems won't suddenly disappear next week, next month, or next year. We're just starting down a road that I believe will lead us out of the economic swamp we've been in for so long. It'll take time for the effect of the tax rate reductions to be felt in increased savings, productivity, and new jobs. It will also take time for the budget cuts to reduce the deficits which have brought us near runaway inflation and ruinous interest rates.

The important thing now is to hold to a firm, steady course. Tonight I want to talk with you about the next steps that we must take on that course, additional reductions in federal spending that will help lower our interest rates, our inflation, and bring us closer to full economic recovery.

I know that high interest rates are punishing many of you, from the young family that wants to buy its first home to the farmer who needs a new truck or tractor. But all of us know that interest rates will only come down and stay down when government is no longer borrowing huge amounts of money to cover its deficits.

MORE

These deficits have been piling up every year and some people here in Washington just throw up their hands in despair. Maybe you'll remember that we were told in the spring of 1980 that the 1981 budget, the one we have now, would be balanced. Well, that budget, like so many in the past, hemorrhaged badly and wound up in a sea of red ink.

MORE

I have pledged that we shall not stand idly by and see that same thing happen again. When I presented our economic recovery program to Congress, I said we were aiming to cut the deficit steadily to reach a balance by 1984.

The budget bill that I signed this summer cut \$35 billion from the 1982 budget and slowed the growth of spending by \$130 billion over the next three years. We cut the government's rate of growth nearly in half.

Now we must move on to a second round of budget savings -- to keep us on the road to a balanced budget.

Our immediate challenge is to hold down the deficit in the fiscal year that begins next week. A number of threats are now appearing that will drive the deficit upward if we fail to act. For example, in the euphoria just after our budget bill was approved this summer, we didn't point out immediately as we should that while we did get most of what we'd asked for, most isn't all. Some of the savings in our proposal were not approved; and since then, the Congress has taken actions that could add even more to the cost of government.

The result is that without further reductions, our deficit for 1982 will be increased by some \$16 billion. The estimated deficit for '83 will be increased proportionately. And without further cuts, we can't achieve our goal of a balanced budget by 1984.

Now, it would be easy to sit back and say, "Well, it will take longer than we thought. We got most of what we proposed, so let's stop there." But that's not good enough.

In meeting to discuss this problem a few days ago, Senator Pete Domenici of New Mexico, Chairman of the Senate Budget Committee, recalled the words of that great heavy-weight champion and great American Joe Louis just before he stepped into the ring against Billy Conn. There had been some speculation that Billy might be able to avoid Joe's lethal right hand. Joe said, "Well, he can run but he can't hide."

Senator Domenici said to me, "That's just what we're facing on runaway federal spending. We can try to run from it but we can't hide. We have to face up to it."

He's right, of course. In the last few decades we started down a road that led to a massive explosion in federal spending. It took about 170 years for the federal budget to reach \$100 billion. That was in 1962. It only took 8 years to reach the \$200 billion mark and only five more to make it \$300 billion. And in the next five we nearly doubled that.

It would be one thing if we'd been able to pay for all the things government decided to do, but we've only balanced the budget once in the last 20 years.

In just the past decade, our national debt has more than doubled. And in the next few days it will pass the trillion dollar mark. One trillion dollars of debt -- if we as a nation needed a warning, let that be it.

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Our interest payments on the debt alone are now running more than \$96 billion a year. That's more than the total combined profits last year of the 500 biggest companies in the country; or to put it another way, Washington spends more on interest than on all of its education, nutrition and medical programs combined.

In the past, there have been several methods used to fund some of our social experiments. One was to take it away from national defense. From being the strongest nation on earth in the post World War II years, we've steadily declined, while the Soviet Union engaged in the most massive military buildup the world has ever seen.

Now, with all our economic problems, we're forced to try to catch up so that we can preserve the peace. Government's first responsibility is national security and we're determined to meet that responsibility. Indeed, we have no choice.

Well, what all of this is leading up to is -- what do we plan to do? Last week I met with the Cabinet to take up this matter. I'm proud to say there was no hand-wringing, no pleading to avoid further budget cuts. We all agreed that the "tax and tax, spend and spend," policies of the last few decades lead only to economic disaster. Our government must return to the tradition of living within our means and must do it now. We asked ourselves two questions -- and answered them: "If not us -- who? If not now -- when?"

Let me talk with you now about the specific ways that I believe we ought to achieve additional savings -- savings of some \$16 billion in 1982 and a total of \$80 billion when spread over the next three years. I recognize that many in Congress may have other alternatives and I welcome a dialogue with them. But let there be no mistake: We have no choice but to continue down the road toward a balanced budget -- a budget that will keep us strong at home and secure overseas. And let me be clear that this cannot be the last round of cuts. Holding down spending must be a continuing battle for several years to come.

Here is what I propose. First, I'm asking Congress to reduce the 1982 appropriation for most government agencies and programs by 12 percent. This will save \$17.5 billion over the next several years. Absorbing these reductions will not be easy, but duplication, excess, waste and overhead is still far too great and can be trimmed further.

No one in the meeting asked to be exempt from belt-tightening. Over the next three years, the increase we had originally planned in the defense budget will be cut by \$13 billion. I'll confess, I was reluctant about this because of the long way we have to go before the dangerous window of vulnerability confronting us will be appreciably narrowed. But the Secretary of Defense assured me that he can meet our critical needs in spite of this cut.

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Second, to achieve further economies, we'll shrink the size of the non-defense payroll over the next three years by some 6-1/2 percent, some 75,000 employees. Much of this will be attained by not replacing those who retire or leave. There will, however, be some reductions in force simply because we're reducing our administrative overhead. I intend to set the example here by reducing the size of the White House staff and the staff of the Executive Office of the President.

As a third step, we propose to dismantle two Cabinet departments, Energy and Education. Both secretaries are wholly in accord with this. Some of the activities in both of these departments will, of course, be continued either independently or in other areas of government. There's only one way to shrink the size and cost of big government and that is by eliminating agencies that are not needed and are getting in the way of a solution. Now, we don't need an Energy Department to solve our basic energy problem. As long as we let the forces of the marketplace work without undue interference, the ingenuity of consumers, business, producers and inventors will do that for us.

Similarly, education is the principle responsibility of local school systems, teachers, parents, citizen boards and state governments. By eliminating the Department of Education less than two years after it was created, we cannot only reduce the budget, but ensure that local needs and preferences rather than the wishes of Washington determine the education of our children. We also plan the elimination of a few smaller agencies and a number of boards and commissions, some of which have fallen into disuse or which are now being duplicated.

Fourth, we intend to make reductions of some \$20 billion in federal loan guarantees. These guarantees are not funds that the government spends directly. They're funds that are loaned in the private market and insured by government at subsidized rates. Federal loan guarantees have become a form of back door, uncontrolled borrowing that prevent many small businesses that aren't subsidized from obtaining financing of their own. They are also a major factor in driving up interest rates. It's time we brought this practice under control.

Fifth, I intend to forward to Congress this fall a new package of entitlement and welfare reform measures, outside Social Security, to save nearly \$27 billion over the next three years. In the past two decades we've created hundreds of new programs to provide personal assistance. Many of these programs may have come from a good heart but not all have come from a clear head. And the costs have been staggering.

In 1955 these programs cost \$8 billion. By 1965 the cost was \$79 billion. Next year it will be \$188 billion. Let there be no confusion on this score. Benefits for the needy will be protected, but the black market in food stamps must be stopped, the abuse and fraud by beneficiaries and providers alike cannot be tolerated, provision of school loans and meal subsidies to the affluent can no longer be afforded.

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In California when I was Governor and embarked upon welfare reform, there were screams from those who claimed that we intended to victimize the needy. But in a little over three years we saved the taxpayer some \$2 billion at the same time we were able to increase the grants for the deserving and truly needy by an average of more than 40 percent. It was the first cost of living increase they'd received in 13 years. I believe progress can also be made at the national level.

We can be compassionate about human needs without being complacent about budget extravagance.

Sixth, I will soon urge Congress to enact new proposals to eliminate abuses and obsolete incentives in the tax code. The Treasury Department believes that the deficit can be reduced by \$3.0 billion next year and \$22 billion over the next three years with prompt enactment of these measures.

Now that we've provided the greatest incentives for saving, investment, work and productivity ever proposed, we must also ensure that taxes due the government are collected and that a fair share of the burden is borne by all.

Finally, I am renewing my plea to Congress to approve my proposals for user fees -- proposals first suggested last spring, but which have been neglected since.

When the federal government provides a service directly to a particular industry or to a group of citizens, I believe that those who receive benefits should bear the cost. For example, this next year the federal government will spend \$525 million to maintain river harbors, channels, locks, and dams for the barge and maritime industries. Yacht owners, commercial vessels and the airlines will receive services worth \$2.8 billion from Uncle Sam.

My spring budget proposals included legislation that would authorize the federal government to recover a total of \$980 million from the users of these services through fees. Now, that's only a third of the \$3.3 billion it will cost the government to provide those same services.

None of these steps will be easy. We're going through a period of difficult and painful readjustment. I know that we're asking for sacrifices from virtually all of you. But there is no alternative. Some of those who oppose this plan have participated over the years in the extravagance that has brought us inflation, unemployment, high interest rates and an intolerable debt. I grant they were well intentioned but their costly reforms didn't eliminate poverty or raise welfare recipients from dependence to self-sufficiency, independence and dignity. Yet in their objections to what we've proposed they offer only what we know has been tried before and failed.

I believe we've chosen a path that leads to an America at work, to fiscal sanity, to lower taxes and less inflation. I believe our plan for recovery is sound and it will work.

Tonight I'm asking all of you who joined in this crusade to save our economy to help again. To let your representatives know that you'll support them in making the hard decisions to further reduce the cost and size of government.

Now, if you'll permit me, I'd like to turn to another subject which I know has many of you very concerned and even frightened. This is an issue apart from the economic reform package that we've just been discussing, but I feel I must clear the air. There has been a great deal of misinformation and for that matter pure demagoguery on the subject of Social Security.

During the campaign I called attention to the fact that Social Security had both a short and a long range fiscal problem. I pledged my best to restore it to fiscal responsibility without in any way reducing or eliminating existing benefits for those now dependent on it.

To all of you listening and particularly those of you now receiving Social Security, I ask you to listen very carefully: First to what threatens the integrity of Social Security and then to a possible solution.

Some thirty years ago, there were 16 people working and paying the Social Security payroll tax for every one retiree. Today that ratio has changed to only 3.2 workers paying in for each beneficiary.

For many years we've known that an actuarial imbalance existed and that the program faced an unfunded liability of several trillion dollars.

Now, the short range problem is much closer than that. The Social Security retirement fund has been paying out billions of dollars more each year than it takes in and it could run out of money before the end of 1982 unless something is done.

Some of our critics claim new figures reveal a cushion of several billions of dollars which will carry the program beyond 1982. I'm sure it's only a coincidence that 1982 is an election year.

The cushion they speak of is borrowing from the Medicare fund and the disability fund. Of course doing this would only postpone the day of reckoning. Alice Rivlin of the Congressional Budget Office told a congressional committee the day before yesterday that such borrowing might carry us to 1990, but then we'd face the same problem. And as she put it, we'd have to cut benefits or raise the payroll tax. Well, we're not going to cut benefits and the payroll tax is already being raised.

In 1977, Congress passed the largest tax increase in our history. It called for a payroll tax increase in January of 1982, another in 1985, and again in 1986 and in 1990.

When that law was passed we were told it made Social Security safe until the year 2030. But we're running out of money 48 years short of 2030.

For the nation's work force, the Social Security tax is already the biggest tax they pay. In 1935 we were told the tax would never be greater than 2% of the first \$3,000 of earnings. It is presently 13.3% of the first \$29,700 and the scheduled increases will take it to 15.3% of the first \$60,600. And that's when Mrs. Rivlin says we would need an additional increase.

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Some have suggested reducing benefits. Others propose an income tax on benefits, or that the retirement age should be moved back to age 68 and there are some who would simply fund Social Security out of general tax funds as welfare is funded. I believe there are better solutions. I am asking the Congress to restore the minimum benefit for current beneficiaries with low incomes. It was never our intention to take this support away from those who truly need it.

There is, however, a sizeable percentage of recipients who are adequately provided for by pensions or other income and should not be added to the financial burden of Social Security.

The same situation prevails with regard to disability payments. No one will deny our obligation to those with legitimate claims. But there's widespread abuse of the system which should not be allowed to continue.

Since 1962, early retirement has been allowed at age 62 with 80 percent of full benefits. In our proposal we ask that early retirees in the future receive 55 percent of the total benefit, but, and this is most important, those early retirees would only have to work an additional 20 months to be eligible for the 80 percent payment. I don't believe very many of you were aware of that part of our proposal.

The only change we proposed for those already receiving Social Security had to do with the annual cost of living adjustment. Now, those adjustments are made on July 1st each year, a hangover from the days when the fiscal year began in July. We proposed a one-time delay in making that adjustment, postponing it for three months until October 1st. From then on it would continue to be made every 12 months. That one time delay would not lower your existing benefits but would, on the average, reduce your increase by about \$36 one time next year.

By making these few changes, we would have solved the short and long range problems of Social Security funding once and for all. In addition, we could have cancelled the increases in the payroll tax by 1985. To a young person just starting in the work force, the savings from cancelling those increases would, on the average, amount to \$33,000 by the time he or she reach retirement, and compound interest, add that, and it makes a tiny nest egg to add to the Social Security benefits.

However, let me point out, our feet were never imbedded in concrete on this proposal. We hoped it could be a starting point for a bipartisan solution to the problem. We were ready to listen to alternatives and other ideas which might improve on or replace our proposals. But, the majority leadership in the House of Representatives has refused to join in any such cooperative effort.

MORE

I therefore am asking, as I said, for restoration of the minimum benefit and for interfund borrowing as a temporary measure to give us time to seek a permanent solution. To remove Social Security once and for all from politics I am also asking Speaker Tip O'Neill of the House of Representatives and Majority Leader in the Senate Howard Baker to each appoint five members and I will appoint five to a task force which will review all the options and come up with a plan that assures the fiscal integrity of Social Security and that Social Security recipients will continue to receive their full benefits.

I cannot and will not stand by and see financial hardship imposed on the more than 36 million senior citizens who have worked and served this nation throughout their lives. They deserve better from us.

Well now, in conclusion, let me return to the principal purpose of this message, the budget and the imperative need for all of us to ask less of government, to help to return to spending no more than we take in, to end the deficits and bring down interest rates that otherwise can destroy what we've been building here for two centuries.

I know that we're asking for economies in many areas and programs that were started with the best of intentions and the dedication to a worthwhile cause or purpose, but I know also that some of those programs have not succeeded in their purpose. Others have proven too costly, benefiting those who administer them rather than those who were the intended beneficiaries. This doesn't mean we should discontinue trying to help where help is needed. Government must continue to do its share. But I ask all of you, as private citizens, to join this effort too. As a people we have a proud tradition of generosity.

More than a century ago a Frenchman came to America and later wrote a book for his countrymen telling them what he had seen here. He told them that in America when a citizen saw a problem that needed solving he would cross the street and talk to a neighbor about it and the first thing you know a committee would be formed and before long the problem would be solved. And then he added, "You may not believe this, but not a single bureaucrat would ever have been involved."

Some years ago, when we were a young nation and our people began visiting the lands of their forefathers, these Americans tourists then were rather brash, unsophisticated by European standards, but blessed with a spirit of independence and pride. One such tourist, an elderly, small-town gentleman, and his wife, were there in Europe listening to a tour guide go on about the wonders of the volcano, Mt. Aetna. He spoke of the great heat that it generated, the power, the boiling lava, et cetera.

Finally, the old boy had had enough of it, turned to his wife, and he said, "We've got a volunteer fire department at home that'd put that thing out in 15 minutes." Well, he was typical of those Americans who helped build a neighbor's barn when it burned down. They built the West without an area redevelopment plan, and cities across the land without federal planning. I believe the spirit of voluntarism still lives in America. We see examples of it on every hand, the community charity drive, support of hospitals and all manner of non-profit institutions, the rallying around whenever disaster or tragedy strikes.

The truth is we've let government take away many things we once considered were really ours to do voluntarily out of the goodness of our hearts and a sense of community pride and neighborliness. I believe many of you want to do those things again, want to be involved if only someone will ask you or offer the opportunity. Well, we intend to make that offer.

We're launching a nationwide effort to encourage our citizens to join with us in finding where need exists and then to organize volunteer programs to meet that need. We've already set the wheels of such a volunteer effort in motion.

As Tom Paine said 200 years ago, "We have it within our power to begin the world over again."

What are we waiting for?

God bless you, and good night.

END

9:26 P.M. EDT

HIGHLIGHTS OF SENATE BUDGET PACKAGE

file
Economic
Program

- o Reduces projected deficits by \$416 billion over FY 83-85 -- or by two-thirds of projected deficit baseline without new savings.
- o Results in rapidly declining deficit path over three years -- with the deficit shrinking to less than one percent of GNP by 1985.

<u>1983</u>	<u>1984</u>	<u>1985</u>
-106	-69	-39

- o Based on "freeze" concept and equal burden sharing. Freezes Federal pay, discretionary spending and COLA's except for Social Security.
- o Direct spending restraint and interest savings total \$281 billion or 68% of total three year package. Outlay savings are approximately three-times greater than revenue increases.
- o Provides balanced package of deficit reduction measures including \$95 billion in additional revenues, \$22 billion in defense program savings and \$18 billion in DOD pay savings. These measures compromise 33 percent of total three year package.
- o Assures full July Social Security COLA of 7.4% and mandates action by December to balance the Social Security fund and guarantee minimum solvency levels needed to maintain regular monthly payments to all recipients.
- o Assures no change in third year of tax cut and preserves the preponderant share of the 1981 tax reduction. The President's February budget provided \$358 billion in tax reduction over FY 83-85. The Domenici package provides \$313 billion or 87 percent of the President's budget.
- o Achieves \$72 billion in discretionary and targeted entitlements savings over three years -- 72% of the President's February recommendation.
- o Combination of spending cuts and revenue increases will dramatically slow the growth of the national debt and ease pressure on financial markets so that interest rates can come down and economic recovery can move forward. Resulting interest savings will total \$106 billion over three years.

I. SENATE BUDGET PACKAGE

	<u>1983</u>	<u>1984</u>	<u>1985</u>
1) Baseline Deficit.....	182	216	233
<u>Deficit Reduction Measures:</u>			
2) Management.....	9	12	12
3) User Fees.....	2	2	2
4) Federal Pay Freeze* **.....	6	9	13
5) COLA Freeze (Excluding Social Security)*	3	5	7
6) Non-Defense Discretionary.....	6	13	20
7) Targeted Entitlements.....	7	11	15
8) Social Security Commission Solvency Recommendations...	6	17	17
9) Defense (excluding pay/retirement).....	5	7	10
10) Revenue.....	20	35	40
11) Interest (market effect).....	8	19	28
12) Debt Service.....	5	17	29
13) Total Deficit Reduction.....	76	147	193
14) Remaining Deficit.....	106	69	39

* Assumes 4% increase in out-years.

**Provides \$1.3 billion readiness-related and incentive pay' increases for military (FY83)

THE ALTERNATIVE CORPORATE MINIMUM TAX: A PENALTY TAX ON JOBS AND INVESTMENT

In response to a media-created perception that corporations no longer pay any income taxes, the Administration has proposed an alternative corporate minimum tax. The media is wrong.

The Price of a Minimum Tax is Unemployment and Less Investment

Tax increases crimp expansion, discourage employment, and reduce the supply of lendable funds, driving up interest rates, while doing little or nothing to bring down the deficit. In order to stimulate private employment, businesses must have access to funds and the incentive to invest. The minimum tax proposal undermines the Accelerated Cost Recovery System which was designed to stimulate economic recovery by enhancing cash flow and encouraging investment in plant and equipment. In short the minimum tax is a step backward, away from greater employment and economic growth.

Corporations Do Pay Tax

Corporations continue to pay substantial monies to the Treasury. According to the 1983 Budget figures, corporate tax receipts are projected to rise from \$47 billion in 1982 to \$65 billion in 1983 and \$84 billion in 1984. This reflects a growth in the corporate share of total tax receipts from 7.5 to 11.6 percent between 1982 and 1984, while every other revenue source remains virtually steady or declines as a share of total receipts.

However, although corporate tax receipts are increasing, in reality corporations do not pay taxes -- people do. The corporation acts only as tax collector for the government. If the corporate income tax is increased, companies will pass on the burden to customers by raising prices; to workers by laying off staff, shortening hours, or reducing wage and benefit increases; and to shareholders by realizing lower profits.

The Minimum Tax is not a Loophole Closer

The corporate minimum tax is counterproductive. It distorts investment flows and will add more complexity to an already complex tax code. The alternative minimum tax subjects to taxation certain business deductions properly taken from income as a result of Congressional desire to create incentives for certain types of economic behavior. For example, disallowing the application of the investment tax credit to the alternative minimum tax accounts for 45 percent of the revenue to be gained by enacting this proposal. The alternative minimum tax will not ensure that corporations with too many "tax preferences" will pay some tax, but rather it will repeal the basic incentives for capital investment which were enacted last summer.

If such incentives are no longer needed, they should be repealed or modified directly. Repeal of these incentives has not been requested because they are necessary in order to make the economic recovery program work properly. Both Congress and the Administration realized this necessity when they enacted the Economic Recovery Tax Act of 1981.