

CUOMO/GANNETT TALK

- No one proposes to use Federal policy, tax or otherwise, to penalize States that try to innovate in dealing with social problems, whether it be welfare or industrial development. But certainly it is fair for the Federal government to take a neutral stance in this record--which is what we would do, for example, if State and local taxes were not deductible.

- Obviously, higher-tax States will be the most concerned about the impact of ending deductibility on their own efforts to raise revenue. But the argument can be made that voters in each State have a right to know what they are paying for and why, without a cushion from the Federal tax code.

- In any event, Federal tax policy shows only one side of the relationship between States and the Federal government. Federal aid of all kinds, including benefit programs, subsidies, and grants-in-aid, represent the other side. For example, the Tax Foundation found that in 1982 New York paid only 79 cents in Federal taxes for every dollar in Federal aid the State received. We ought to consider whether our tax and spending policies, taken together, ought to give a net subsidy to States like New York.

TAX REFORM

DECEMBER 11, 1984

Fairness

CAPITAL HILTON

- The Treasury proposal is an attempt to improve the fairness of the tax laws rather than just simplifying preparation of tax returns.
- By "fairness" I mean that Treasury has tried to make the tax code more neutral--not trying either to encourage or discourage certain behavior and by treating similar taxpayers more alike. Fairness is more important than return simplification, both as public policy and as a method of increasing compliance by increasing public perception that the code is fair.
- That is not to say that the Treasury plan is perfect or that it should not be significantly changed if it becomes the basis for legislation. However, it certainly points out that the tax code today is neither neutral nor consistent in what public policies should be encouraged.

Individual v. Corporate Taxes

- As everybody knows, inflation and bracket creep, combined with additional payroll taxes, have kept individuals' tax liability relatively high. In 1983, individual income tax comprised 56 percent of Federal revenues, compared with 53 percent in 1975. In 1983, in contrast, corporate income taxes comprised less than 10 percent of Federal revenues. In 1975, the corporate income tax accounted for almost 16 percent of Federal revenues.
- Maybe it's true that shareholders and customers actually pay the corporate tax, but the trend away from corporate income taxes is very noticeable.

Incentives v. Revenue Collection

- One of the problems we have in the tax code is that we have so many incentives that say "if you do what the Government wants you to do with your money, you will pay less tax." Taxpayers who don't follow the Government's "advice" on how to spend their money pay taxes at a higher rate.
- There probably isn't anything wrong with providing incentives through the tax code, but the current set of incentives do not present a coherent tax, economic or social policy. We have incentives for consumption like the deduction for consumer interest paid and the exclusion of employer-paid medical coverage and we have incentives for savings like the IRA deduction and the tax benefits for qualified pension plans. Some of these special incentives are itemized

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deductions, others are credits, and still others are complete exclusions from income.

- Maybe we should review the impact of these provisions to see if taxpayers would be better off with fewer special provisions and lower rates.

Treasury Proposal

- The Treasury proposal is "revenue neutral." However, it shifts the tax burden away from individuals and onto profitable corporations who have been paying their fair share.
- Some people have implied that the Treasury proposal would be unfair to cover and middle income taxpayers. That is simply wrong. Under the proposal, individuals would have an average tax cut of 8-1/2 percent (and a rate cut of 20 percent). Seventy-eight percent of individuals would have a tax cut or no change in tax liability. Twenty-two percent would have a tax increase. The higher a taxpayer's income, the greater the chance that his tax liability would increase.
- The proposal does not significantly change the tax burden by income class, retaining the progressive system advocated by Governor Cuomo and others. In fact, if there is any bias in the proposal, it is toward relieving the tax burden on lower income taxpayers a little more than the burden on wealthier taxpayers. Under the proposal, no one under the poverty line will pay any income tax, unlike under present law.
- Corporations would pay for the individual tax reductions with a tax increase of between \$25 and \$37 billion per year.
- Among corporations, the Treasury proposal would even out the tax burden among profitable corporations so that the service and high technology industries won't pay more than they should.
- On the individual side, don't forget that over 65 percent of Americans don't itemize. They will not be affected by reduction or elimination of itemized deductions such as the State and local tax deduction which governors of high tax States have opposed. However, those States that "piggyback" their individual income tax on the Federal return will have increased State revenues from a broadened tax base.
- As for tax-free fringe benefits, the reduction in individual tax rates should more than offset any increase in taxable income for most taxpayers by making compensation like group health and life insurance taxable.

- I know that some governors are also concerned about the impact of lower tax rates on tax-exempt bonds. However, we reduced the maximum tax rate from 70 percent to 50 percent in 1981 and issuance of tax-exempt bonds has still increased dramatically (despite further efforts to limit IDB's in 1982 and 1984).
- If the President decides to endorse a proposal like this, he should have a lot of support from the majority of individual taxpayers who will benefit from the changes. He also will have great opposition from many special interests who benefit from particular provisions.