MEETING WITH
ECONOMIC ADVISERS ON TAX STRATEGY

Monday, December 8, 1975

2:00 P.M.

THE PRESIDENT HAS SEEN....

THE WHITE HOUSE

WASHINGTON

December 8, 1975

MEMORANDUM FOR THE PRESIDENT

FROM: L. WILLIAM SEIDMAN LWS

SUBJECT: Meeting on Tax Strategy

A memorandum on "Economic and Policy Assumptions for the 1977 Budget: Tax Policy Decisions" which was reviewed by the EPB Executive Committee this morning is attached for your information. It will provide some useful background for the discussion on tax strategy at 2:00 today.

DRAFT
December 6, 1975

MEMORANDUM FOR THE ECONOMIC POLICY BOARD
EXECUTIVE COMMITTEE

SUBJECT: Economic and Policy Assumptions for the 1977 Budget: Tax Policy Decisions

The 1977 Budget will be published on January 19. Unless Congress acts in a surprising manner, the President's proposal for a $28 billion tax cut will not have been enacted by that date. A new effective date and possibly a new structure will have to be specified for the proposed tax cut and this date must be decided by December 12 for the purposes of the outlay, receipts, and economic assumptions that will appear in the 1977 Budget.

As of January 1, a number of scenarios are possible:

(1) A return to 1974 tax law because of a successful Presidential veto of congressional tax action that does not include a spending ceiling.

(2) A temporary extension of 1975 tax law.

(3) Something like the House's proposed tax cut enacted over the President's veto.

Regardless of the scenario that emerges, it is assumed that the Budget will propose a further tax cut to become effective sometime in 1976 and that for Budget purposes the President will adhere to his goal of a tax cut of $28 billion from 1974 levels accompanied by a $395 billion spending limit for FY 1977.

Any tax cut that become effective during 1976 will have to be made retroactive to January 1. Otherwise taxpayers would face the extremely difficult task of determining whether 1976 income and deductions occurred before or after the effective date of the new tax law.

However, this leads to a problem which can be illustrated by the following example. Let us suppose that the Congress has enacted an extension of 1975 withholding rates. This would lead to a $12 billion personal tax reduction compared to 1974 law. The President's original proposal was for an additional $8 billion in personal income tax cuts (total $20 billion) effective January 1, 1976. If the effective date of his proposal is delayed to, say, July 1, 1976 with the additional $8 billion cut retroactive to January 1, it would be necessary to make a decision regarding withholding rates.

If the cut in withholding rates is sufficient to provide taxpayers with the entire $8 billion during the six months remaining in 1976, either withholding rates will have to be raised in January 1977 or a further tax reduction will be required to keep rates constant.

Clearly, there will be strong pressures for the latter. This problem is very much more serious if 1974 tax law goes into effect January 1, 1976.

There are two ways out of this difficulty. First, withholding rates would be set at the levels which would prevail in 1977 and afterwards. If 1975 tax law is extended into 1976, or if the House bill is enacted, this would result in about $4 billion of overwithholding in 1976 which would be refunded in the spring of 1977. If 1974 tax law goes into effect on January 1, 1976, overwithholding would be about $10 billion which may make this approach less acceptable.

Secondly, the President's proposed tax cut could be phased in. For example, if the effective date for new withholding rates were July 1, and if the Congress had already provided a $12 billion reduction from 1974 levels effective January 1, an additional $4 billion in liability reductions could be proposed for 1976 to be followed by a further $4 billion reduction in 1977. Thus, the total reduction in 1976 tax liabilities would be $16 billion from 1974 levels and the total reduction in 1977 tax liabilities would be $20 billion from 1974 levels. In this way, withholding rates would be immediately lowered to their eventual 1977 levels on July 1, 1976. There would be no overwithholding in 1976. Moreover, the fiscal 1977 deficit would be reduced. However, there could be some technical problems. A special set of tax rates and exemptions would have to be designed for 1976, and some equity problems would be encountered in distributing the first phase of the eventual $28 billion tax cut. The business tax reductions could be phased in in a similar manner. The exact nature of the phase in of both personal and business cuts will depend on the choice of an effective date.

Needless to say, the choice of a strategy has important implications for the computation of budget totals and for the economic forecast.

The options regarding the basic strategy are summarized below. A discussion of different effective dates follows.

Options

Option 1: Implement the President's original proposal for a $28 billion reduction in tax liabilities from 1974 levels retroactive to January 1, 1976.

If this option is selected there are two options regarding withholding rates:

Option 1A: Lower rates sufficiently to provide the entire $28 billion cut during whatever remains of 1976.

This implies that withholding rates will rise in January 1977 unless the tax law is changed.

Option 1B: Lower withholding rates only to their eventual 1977 levels.

This implies overwithholding in 1976.

Option 2: Phase in the President's proposed tax cut.

The amount provided in 1976 will depend on the effective date of the withholding change and will be calculated so as to keep withholding rates constant between 1976 and 1977.

Decision

Option 1 ________ Implement the President's original proposal retroactive to January 1, 1976.

Option 1A ________ Implement magnified withholding rates.

Option 1B ________ Implement rates which will apply to permanent levels in 1977 and afterwards.

Option 2 ________ Phase in the President's proposed tax cut.

Regardless of the decision, the budget estimates and economic forecast will be dependent on an assumption regarding what tax law will be in effect on January 1, 1976. Hopefully, the events of the next week will clarify this problem.

THE PRESIDENT HAS SEEN....

THE WHITE HOUSE

WASHINGTON

December 6, 1975

MEETING WITH ECONOMIC ADVISERS ON TAX STRATEGY
December 8, 1975
2:00 p.m.
Cabinet Room

From: L. William Seidman LWS

I. PURPOSE

To review recent congressional action on your proposed tax reduction and spending restraint program and to consider alternative legislative strategies.

II. BACKGROUND, PARTICIPANTS AND PRESS PLAN

A. Background: The House has passed a tax bill providing approximately $17 billion in permanent tax reductions comprised of approximately $13 billion in personal income tax cuts and $4 billion in tax reductions for business. Repeated attempts by Republicans in the House to couple the tax reduction bill with a spending ceiling for FY 1977 were unsuccessful.

The tax bill will be taken up by the Senate Finance Committee on Tuesday. Senator Long has advised Secretary Simon that he supports separating the tax reduction from tax reform and passing a temporary (6 month) tax reduction at the level of current withholding rates coupled with some form of Expanded Stock Ownership Program and the earned income credit. Furthermore, Senator Long is convinced that the Senate will not pass a spending limitation on FY 1977 expenditures at this time.

A memorandum outlining the range of possible tax bills that may emerge from the Congress and alternative strategies is attached at Tab A. The Economic Policy Board Report is attached at Tab B.

B. Participants: William E. Simon, L. William Seidman, John T. Dunlop, Rogers C. B. Morton, James T. Lynn, Alan Greenspan, Arthur F. Burns, Richard B. Cheney, John O. Marsh, Max Friedersdorf, Robert T. Hartman.

C. Press Plan: David Hume Kennerley photograph. Meeting to be announced.

III. AGENDA

A. Tax Reduction/Spending Limitation Strategy

Secretary Simon will review the recent and anticipated congressional action on a tax bill and alternative Administration strategies.

A

December 6, 1975

MEMORANDUM FOR THE PRESIDENT

FROM: L. WILLIAM SEIDMAN LWS

SUBJECT: Tax Reduction/Spending Limitation Strategy

The House has passed a tax bill providing approximately $17 billion in tax cuts ($13 billion personal and $4 billion business). Repeated attempts by the Minority to add your proposed FY 1977 spending ceiling of $395 billion failed. With each attempt, however, the margin of defeat narrowed culminating in a 220 to 202 defeat of a motion to recommit to add a $395 billion ceiling for FY 1977.

Our next initiative will be an attempt to have the Senate add your $395 billion spending ceiling to their tax bill. Secretary Simon spoke with Senator Long who advises that he will attempt to separate the tax cut from tax reform and pass a simple six-month tax reduction at the level of current withholding rates coupled with some form of Expanded Stock Ownership Program and the earned income credit. Long believes it is not possible to pass a spending ceiling in the Senate at this time.

Depending on Senate action, we anticipate that the tax bill presented to you after a House/Senate Conference will be one of the following:

(1) A permanent $17 billion tax reduction/No spending ceiling. (House Bill)

(2) A permanent $17 billion tax reduction with a spending ceiling. (Coupled Ceiling)

(3) A temporary (six months) extention of the 1975 reductions adjusted to retain current withholding rates. (Six-month extension)

(4) A temporary (60-90 day) extension of current withholding rates to permit time to agree on a permanent tax reduction effective retroactively to January 1, 1976. (Withholding freeze)

In general, your advisors feel that alternative (2) A tax reduction coupled with a spending ceiling would be acceptable even though the tax reduction is below your proposed $28 billion and that alternative (1) A tax reduction only would not be acceptable. In their view your position on alternative (3) Six month extension and alternative (4) Withholding freeze need not be decided at this time.

It is our best estimate that Congress will pass either alternative (1) Tax reduction only or alternative (3) A six month extension. Your possible options include:

Option A: During the 10 days following enrollment of a tax reduction bill signal a veto unless the Congress passes a concurrent resolution of a spending ceiling.

Option B: Veto the bill and indicate that you will sign their $17 billion tax reduction if it is coupled with your $395 billion spending ceiling.

Our best estimate is that a $17 billion tax reduction coupled with a $395 spending ceiling (an $11 billion smaller tax reduction than originally included in our forecasts) would entail a reduction in our real GNP growth estimate of less than one half of one percent.

Option C: Veto the bill and request a 60-day freeze in the present withholding rates.

Option D: Veto the bill. In this case withholding rates will legally return to 1974 levels on January 1 but actual changes in payroll withholding will not occur until at least February 1.

Secretary Simon is scheduled as the sole witness before the Senate Finance Committee when they take up the tax bill on Tuesday. You are scheduled to meet with the EPB on Monday, December 8 at 2:00 p.m. to review tax strategy. Senator Long has expressed a desire to be cooperative and an interest in meeting with you. You may want to talk with him following the EPB meeting.

A summary of the effects of the individual income tax reductions in the House bill is attached.

MEMORANDUM

THE WHITE HOUSE

WASHINGTON

Distribution of Tax Cuts by Income

Special to The New York Times

WASHINGTON, Dec. 4—The following table, based on data fro mthe Congressional Joit Committee on Internal Revenue Taxation, shows how the tax reductions in the House bill would be distributed among the different income groups:

ADJ. GROSS INCOME Class	RETURNS WITH TAX DECREASE (Thousands)	AMOUNT OF TAX DECREASE ($Millions)	RETURNS WITH TAX INCREASE (Thousands)	AMOUNT OF TAX INCREASE ($Millions)	NET TAX CHANGE ($Millions)
No A.G.T.	*...	*...	94	14	+ 14
0-5,000	2,585	— 28	2,681	704	+ 676
5-10	12,578	— 691	3,456	467	— 224
10-15	12,989	—1,240	...	...	—1,240
15-20	9,792	—1,283	...	...	—1,283
20-30	7,650	—1,049	...	...	—1,049
30-50	2,357	— 324	...	...	— 324
50-100	668	— 90	...	...	— 90
100+	143	— 20	...	...	— 20
TOTAL	48,763	—4,726	6,231	1,186	—3,540

*Persons reporting no adjusted gross income—despite high real economic incomes—through declarations of large deductions.

Effect of Proposed Cuts On Families' Tax Bills

Special to The New York Times

WASHINGTON, Dec. 4—The following tables, based on data from the Congressional Joint Committee on Internal Revenue Taxation, show the Federal income tax that will be paid by families of different size with typical deduction under present law and under the bill passed by the House of Representatives:

SINGLE PERSON

Adjusted Gross Income	Present Law	House Bill
$3,000	$63	$63
5,000	404	381
6,000	594	551
8,000	1,007	924
10,000	1,452	1.331
15,000	2,519	2,315
20,000	3,754	3,544
25,000	5,200	3,990
40,000	10,485	10,275

MARRIED COUPLE
NO DEPENDANTS

Adjusted Gross Income	Present Law	House Bill
$3,000	$0	$0
5,000	170	170
6,000	326	326
8,000	674	642
10,000	1,054	982
15,000	1,969	1,810
17,500	2,456	2,276
20,000	2,975	2,795
25,000	4,110	3,930
40,000	8,483	8,303

MARRIED COUPLE
TWO DEPENDENTS

Adjusted Gross	Present Law	House Bill
$3,000	+300	0
5,000	+300	0
6,000	+265	35
8,000	347	347
10,000	709	709
15,000	1,579	1,510
20,000	2,540	2,420
25,000	3,630	3.510
40,000	7,838	7,718

(Plus sign [+] means a cash payment from the Government will be made to the taxpayer.)

B

December 6, 1975

ECONOMIC POLICY BOARD REPORT

Issues Considered by the EPB During the Month of November

1. Council of Economic Advisers Annual Report

   Reviewed and provided comments on the outline of the CEA Annual Report.

2. EPB/NSC Task Force on Commodities

   Approved reestablishment of an EPB/NSC Task Force on Commodities, jointly chaired by the Departments of the Treasury and State, to serve as the focal point for monitoring and regularly reporting on commodity issues to the EPB/NSC.

3. New York City

   Intensive monitoring of New York City financial situation and development of Administration position on bankruptcy legislation and seasonal financing assistance.

4. Broadening Stock Ownership

   Reviewed alternative plans for broadening stock ownership, including an assessment of their revenue impact.

5. Social Security Reform

   Reviewed economic aspects of Social Security reform, including decoupling issue and short-term financing problem.

6. International Economic Summit

   Reviewed briefing materials prepared for International Summit Conference.

7. Review of Government's Employment and Unemployment Statistics

   Approved memorandum proposing a review of the Government's employment and unemployment statistics for submission to the President.

8. Withholding Rates Strategy

   Reviewed options memorandum on alternatives with respect to withholding rates and approved memorandum for submission to the President.

9. Future of OPEC

Reviewed a memorandum on the future of OPEC, focusing on the validity of a number of commonly held beliefs about OPEC, the economic tools available to bring pressure to bear on the cartel, and the balance of payments problems of developing countries resulting from the significant increase in oil prices.

10. Economic Effects of Marketing Orders for Agricultural Products

Reviewed memorandum on economic effects of marketing orders for agricultural products, focusing on price effects, shifts in the allocation of resources, and the economic value of such orders in providing such services as grading, inspection and research.

11. Capital Goods Outlook in 1976-77

Reviewed capital goods outlook in 1976-77. Secretary Dunlop will prepare a memorandum on the policy implications of the outlook for Executive Committee consideration.

12. Railroad Legislation

Unanimously reaffirmed the original Administration position outlined by the President in April regarding railroad legislation.

13. Economic Assumptions for the 1977 Budget

Reviewed options paper on economic assumptions for the 1977 budget.

14. U.S. Grain Export Policy Statement

Reviewed a proposed statement on U.S. grain export policy.

15. Regulations on Tax Exempt Financing for Regional Municipal Power Systems

Approved the proposed regulations and the Treasury recommendation that they be noticed in the Federal Register following compliance with OMB Circular A-85 pertaining to consultation with heads of state and local governments.

16. Public Debt Limits

Approved Treasury preparing appropriate legislation to amend the debt limit provisions of the Second Liberty Bond Act to place effective responsibility for establishment of the public debt limit on the Budget Committees.

17. Prospective UK Import Controls

Discussed prospective UK import controls and reaffirmed U.S. position that we do not consider that existing conditions constitute "acute or emergency circumstances" and that therefore British protectionist measures at this time are inappropriate and could be detrimental to efforts for liberalization of trade.

Task Force Status Reports

Food Deputies Report

- o November Crop Report estimated feed grain production up 1.6 million tons and soybean production up 1.3 million tons.
- o USDA reports a 12 percent increase in cattle on feed.
- o Feed grain and livestock supply increases have resulted in a substantial decline in prices.

Commodities: Coffee Agreement

- o Tentative agreement reached on new coffee agreement which would commence October 1, 1976, without quotas in effect.
- o U.S. secured in negotiations a quota suspension provision, a change in the definition of shortfalls and an obligation to declare shortfalls, and a 3+3-year agreement (a 6-year agreement with provision for reaffirmation by participating countries at the end of the first 3 years) rather than a 5-year agreement.
- o The U.S. has made no commitment to sign the agreement.
- o Task Force will prepare an analysis of the agreement after the final text of the agreement is completed.

THE PRESIDENT HAS SEEN....

THE WHITE HOUSE

WASHINGTON

December 8, 1975

MEMORANDUM FOR THE PRESIDENT

FROM: L. WILLIAM SEIDMAN LWS

SUBJECT: Provisions in House Tax Bill

As background for the discussion on tax strategy it is useful to clarify that the tax bill which has passed the House contains both temporary and permanent provisions.

Temporary Provision

The bill provides for a temporary (1 year) tax credit of either $30 times the number of exemptions or 2 percent of taxable income up to $12,000 of taxable income (maximum of $240.00) which ever is greater. The credit is 2 percent of taxable income up to $6,000 for married taxpayers filing separately.

This provision is estimated to result in $10.5 billion in lost revenue.

Permanent Provisions

The bill provides for a permanent increase in the minimum standard deduction from $1,300 to $1,600 for single returns and from $1,300 to $1,900 for joint returns. It raises the percentage standard deduction from 15 percent with a maximum of $2,000 to 16 percent with a maximum of $2,300 for single returns and $2,600 for joint returns.

The provisions are estimated to result in $2.9 billion in lost revenue.

Jim

Note we have now received the decision memo from this meeting ---

I will keep here for the time being.

Trudy

THE WHITE HOUSE

WASHINGTON

December 9, 1975

MEETING WITH ECONOMIC ADVISERS ON TAX STRATEGY
December 8, 1975
2:00 p.m.

MEMORANDUM OF DECISIONS

FROM: L. WILLIAM SEIDMAN LWS

Decision 1: Reaffirmation of Linked Tax Reduction and Spending Limitation Program

The President reaffirmed that his tax reduction proposal of $28 billion must be coupled with a $395 billion limitation on Federal spending in FY 1977.

Implementation: Secretary Simon will reaffirm this in his December 9 testimony before the Senate Finance Committee.

Decision 2: Procedures for Calling Congress Back Into Session

The President requested that Max Friedersdorf contact the Parliamentarians of the House and the Senate to clarify procedures for either extending the current session of Congress or calling the Congress back into session after a congressional recess has begun.

Implementation: Max Friedersdorf will contact the Parliamentarians of the House and Senate and report to the President by December 9.