NCPA

National Center for Policy Analysis

POLICY BACKGROUNDER No. 113
*For people with limited time
and a need to know.*

For Immediate Release
February 28, 1992

FEDERAL BUDGET ISSUE

Reviving the Economy: Bush vs. The House Democrats

President Bush and the Democrats in the House of Representatives have submitted proposals to move the economy more quickly out of the current recession and to achieve a higher rate of economic growth. Would these proposals achieve their objectives?

The Two Bush Proposals

"When the Republicans refused to introduce Bush's original plan, Democratic leader Dick Gephardt introduced it."

In his State of the Union message, President Bush outlined a new economic plan, the details of which were made public about a week later. Republicans in the House of Representatives responded favorably to the President's speech. When they saw the fine print, however, they refused to endorse it. Instead, they devised their own plan — which the President then adopted as his "fast track" proposal.

When no Republican would introduce the President's original proposal, Democratic leader Dick Gephardt (R-MO) introduced the plan. And in an obvious attempt to embarrass the Republicans, the Democrat-dominated House Ways and Means Committee reported the President's original plan to the floor of the House — forcing the full chamber to vote on it. After the plan failed by a vote of 427 to 1, two replacements were allowed — a House Republican plan and a House Democratic plan. The Democrats' proposal eventually passed.

- more -

First Interstate Plaza 12655 N. Central Expy., Suite 720 Dallas, TX 75243-1739 (214) 386-NCPA FAX 386-0924

"The President promised to cut the capital gains tax rate in half, but two-thirds of the tax cut was taken back in the fine print."

Bush I. As outlined in the President's State of the Union message, the key elements of the Bush proposal are (1) a lowering of the maximum capital gains tax rate from 28 percent to 15.4 percent;[1] (2) new incentives for investment in equipment;[2] (3) restoration of the right to make deposits to IRA accounts, including the right to make aftertax deposits and tax-free withdrawals;[3] (4) a $500 increase in the personal exemption for dependent children; and (5) other provisions, including a tax credit for first-time home buyers,[4] the removal of certain passive loss restrictions in real estate[5] and the repeal of the luxury tax[6] on boats and planes.[7] When the details of this proposal were made public, the House Republicans balked [See attached *Washington Post* article] and for good reasons.

- Whereas the President had promised a 15.4 percent capital gains tax, application of the alternative minimum tax would make the rate for people with a large capital gain at least 24 percent and possibly as high as 30 percent.[8]

- Whereas the President had promised to restore the opportunity to make deposits to IRA accounts, this right would be limited by income — denying the opportunity to those most likely to take advantage of it.[9]

- Whereas the President had promised new incentives for investments in equipment, the actual tax cut was about one-tenth of what others had proposed and was also temporary — lasting for only 17 months.[10]

- Whereas the President had promised special relief for the real estate industry, "recapture rules" in the fine print took away much of the value of the capital gains tax cut for sales of real property.[11]

- The President's plan also would have eliminated the tax-free buildup in life insurance and the tax advantages of annuities — provisions which would have threatened the financial health of an already weakened insurance industry.

House Republicans were especially upset over the provisions on capital gains. Orally the President had promised to cut the tax rate almost in half. In the fine print, two-thirds of the tax cut was taken back through the application of the alternative minimum tax.

Bush II. In the past few weeks, House Republicans faced a daunting political task. They had to rewrite the President's proposal to make it genuinely "pro-growth." At the same time, their new plan had to have enough in common with Bush I that the President could claim that the House Republican plan was actually a fast-track version of his own plan. Among other changes, the House Republicans:

- Made the 15.4 percent capital gains tax rate real, rather than illusory, and made it fully applicable to the sale of real estate and closely held businesses.[12]

- Dropped the provisions allowing expanded IRA deposits and dropped the repeal of the luxury tax on boats and airplanes.

- Dropped the $500 increase in the personal exemption (for which the President paid a heavy price in the New Hampshire primary).

"The most difficult task for the House Republicans was to find all of the ways in which the Treasury staff additions had subverted the President's goals."

Note that the $500 increase in the personal exemption simply would have transferred income from government to taxpayers. While perhaps a good idea in its own right, it also would increase the deficit and have no effect on incentives to work or invest. It is not clear why the House Republicans dropped the President's IRA proposal — which has been endorsed by many Republicans without the income limits. Repeal of the luxury tax was probably dropped for political reasons, although this tax has proved to be especially harmful. By one estimate, the luxury tax destroys one job for every $1,073 of revenue collected.[13]

The most difficult task faced by the Republicans was to search through the fine print in the President's budget to find the many provisions added by the U.S. Department of Treasury staff that subverted the President's goals. At one point the Republicans even added statutory language to the effect that investors could not be made worse off as a result of the package.

Key Elements of Bush II (The House Republicans' Plan)

The final version of the House Republicans' plan is analyzed below. Table I summarizes the major differences between this plan and the original Bush proposal.

Capital Gains. Because of indexing, wage earners cannot be pushed into a higher tax bracket by the effects of inflation alone. Savers do not have similar protection, however. People who sell assets are forced to pay taxes on inflation-created profits even if the real profit is zero or negative.

TABLE I

A Comparison of the Bush Plans

	BUSH I	BUSH II
Capital Gains	15.4% rate modified by AMT (to 24%) and recapture rules[1]	15.4% rate; retains some recapture rules[2]
IRAs	$2,500 contribution to flexible IRAs, tax exempt for higher-income families	
Equipment Investment	15% increase in first-year depreciation	same
Personal Exemption	$500 increase for each child	
Luxury Tax	Repeal for boats and airplanes	
Real Estate:		
First-time Home Purchase	$5,000 income tax credit	same
Home Purchase	Tax-free IRA withdrawals	same
Passive Loss Rules	Partially repealed	same
Pension Funds	Relaxation of investment rules	same
Home Sales	Deduction of loss in excess of 10% of AGI	
Low-income Housing	Extends current tax benefits for investors	
Student loans	Interest deductible	
Mass Transit	Higher employer subsidies allowed	
Worker Training	Extends employer tax benefits for hiring low-income workers	
Research and Development	Makes 20% tax credit permanent	
Alternative Minimum Tax	Reduction for depreciable assets	same

[1]The 15.4 percent rate is achieved by allowing people to exclude 45 percent of the gain on assets held for three years. The alternative minimum tax applies to the excluded income, however. For depreciable assets, the right to exclude applies only to the nondepreciated portion of the asset.

[2]Drops recapture rules for real estate and closely held businesses.

For example, an asset purchased in 1978 for $1,000 would be worth $2,000 today if its value increased with the rate of inflation. Yet an owner who sold the asset for $2,000 would be taxed on a gain of $1,000 even though the value of the asset had not changed in real terms. Current law, then, discourages people from investing — especially in assets with lengthy productive lives. A capital gains tax cut is designed to partially correct this distortion and encourage future investment.

An unfortunate element of the President's original plan was retained by the House Republicans — the capital gains tax rate is staggered, declining with the length of time an asset is held. The rate would be 23.8 percent for an asset held for one year, 19.6 percent for an asset held two years and 15.4 percent for an asset held three years. This has the effect of lowering the average marginal tax rate to about 19 percent rather than 15.4 percent.

"Once people make an investment in a long-lived asset, we have no economic reason to care how long they hold it."

The idea of staggering the rate is common to many capital gains reform proposals. The argument is that people should be encouraged to invest in long-lived assets. But this argument confuses two separate issues: (1) the life of an asset and (2) the length of time an owner holds the asset. The tax law does discriminate against long-lived assets and this discrimination should be removed. However, once people invest in such assets, there is no economic reason for us to care how long a particular owner holds the asset before selling it.

Investment in Equipment. The tax code also fails to index the depreciation of productive assets so that the write-offs keep up with inflation. In a period of no inflation, the tax law is reasonably fair. But if inflation averages 5 percent a year, a company must spend 50 percent more to replace a machine after 8 years. This means the company must earn additional income and pay additional taxes equal to about one-fourth of the replacement cost.

The House Republican plan partially deals with this problem by adopting the President's proposal to speed up the deduction allowed for tax depreciation. This solution is still modest, however. Other proposals, such as neutral cost recovery[14] or a 10 percent investment tax credit, would be ten times more effective.

Provisions for Real Estate. From the President's original plan, the House Republican proposal retains four measures designed to stimulate real estate. These measures are: (1) a tax credit for first-time home buyers, (2) the right to make tax-free withdrawals from an IRA for the purchase of a home, (3) the removal of passive loss restrictions for real estate investors and (4) provisions that would make it easier to invest pension funds in real estate.

"The House Republican plan will pay for itself, even without the accounting gimmicks the Republicans use to 'finance' the plan."

Paying for the Republican Plan. The plan proposes to: (a) increase minimum private pension plan funding requirements to limit exposure of the federal insurance program that guarantees the retiree benefits of failed plans;[15] (b) extend the statute of limitation for collecting on defaulted student loans; and (c) eliminate the lump-sum retirement distribution option available to participants in the federal civil service retirement program. The majority of these changes — $20 billion over 1992 through 1997 — come from the private pension plan reforms. These reforms reduce the accrual of future government pension liabilities but do not reduce current outlays. Because this practice departs from prior government accounting procedures, we have ignored it in our deficit calculations.

The House Democrats' Plan

The Democratic leadership in the House of Representatives has devised an alternative economic plan. It combines some pro-growth elements with others that are anti-growth.

Capital Gains. Like the Republicans, the congressional Democrats have acknowledged the need for capital gains tax reform. Their proposal goes right to the heart of the most fundamental problem: gains produced by inflation. The Democratic proposal would solve this problem by indexing capital gains — thus eliminating the taxation of inflationary gains. Because this proposal affects only future gains, the short-term impact would be less than the Republican rate cut. However, over the long-term, inflation indexing may have more of an impact than the rate cut.

Investment in Equipment. In recognition of the need to create new incentives, the Democrats have adopted the Bush proposal to accelerate first-year depreciation for investment in equipment.

Middle-Class Tax Reduction. In an effort to create middle-class tax benefits, the Democrats propose a tax credit against 20 percent of the employee's share of Social Security (FICA) taxes up to a maximum of $400. Since workers would reach the maximum credit at an income level of about $13,000, only 13 percent of wages would face a lower marginal tax rate. Like the President's proposal to increase the personal exemption, this proposal does little to alter the marginal tax rate on wage or investment income. It transfers income from government to taxpayers but does not create new incentives to work, save or invest.

Higher Tax Bracket for Higher Incomes. To "pay" for their other proposals, the House Democrats propose to increase the marginal tax rate by

4 percentage points (from 31 percent to 35 percent) for annual taxable incomes above $85,000 for individuals and $145,000 for couples. Unlike the tax credit against Social Security taxes, this proposal does affect marginal tax rates. Moreover, since investment income tends to be a higher proportion of total income for higher-income taxpayers, this proposal penalizes investors and discourages investment. For example, 60 percent of total adjusted gross income over $200,000 in 1989 came from sources other than wages and salaries.[16]

The Millionaire Surtax. Perhaps the worst provision of the Democrats' plan is a proposal to place an additional 10 percent surtax on income in excess of $1 million. When combined with a higher tax bracket, this means that incomes over $1 million would be taxed at a rate of 38.5 percent. The proposal is misguided for two reasons.

First, the tax would fall almost totally on investment income, thus discouraging what is most needed — more investment in the American economy. About 75 percent of the income of millionaires is investment income,[17] and income in excess of $1 million is almost all investment income.

"The Democrats would raise the income tax rate on high-income investors to 38.5 percent — a measure likely to raise no new revenue and cause a great deal of economic harm."

Second, history shows that increases in tax rates on the highest income earners almost always result in less — not more — revenue for government. One reason is that wealthy people have enormous discretion over how they realize their income.[18] For example, instead of investing in real assets, they can buy tax-exempt bonds and pay little or no taxes. Thus, the surtax creates the wrong incentives if the objective is more investment and higher economic growth.

Comparing the Republican and Democratic Plans

The Bush proposal, even when modified by the House Republicans, is relatively modest — especially when compared to alternatives that might be politically acceptable.[19] Nonetheless, the House Republican plan is definitely pro-growth. It is also self-financing. The new investment it would encourage would increase output, national income and, therefore, tax revenues — more than enough to offset the static losses from the tax cuts.

The Democrats' proposal moves in the right direction by lowering the tax on capital gains and creating temporary incentives for increased investment in equipment. These pro-growth proposals are offset, however, by higher taxes on investment income realized by high-income taxpayers. Thus, the net effect of the Democrats' plan would be fewer jobs, less output and less revenue for government. The capital gains cuts build very slowly while the tax increases are immediate. The result is a net loss in economic growth and tax revenue until end of the decade. The tax credit for middle-income families would further increase the federal deficit.

Jobs. As Table II and Figure I show, the Republican plan leads to job creation while the Democrats' plan leads to job losses. Specifically:

- The House Republican plan would lead to 593,000 new jobs by 1997 and 612,000 new jobs by the end of the decade.

- By contrast, the Democrats' plan would lead to a net loss of jobs — reaching a peak of 103,000 lost jobs in 1997.

"The Democrats' plan would have an immediate negative impact on the economy."

Note that the Democrats' plan has an immediate negative impact on the economy — which becomes cumulatively worse through 1997. In the final three years of the decade, the Democrats' jobs loss total begins to reverse, however, as the positive effects of capital gains indexing begin to offset the negative effects of higher income tax rates for higher income investors.

Investment. The biggest difference in the two plans is the effect on investment spending. For the first five to six years, the Republicans reward investors while the Democrats punish them. Specifically:

- The Republican plan would increase investment spending by about $200 billion a year through 1997.

- By contrast, the Democrats' higher taxes on high-income investors would more than offset the stimulus provided by capital gains indexing and would decrease investment spending by about $40 billion a year through 1995.

- Cumulatively, the Republican plan would create $1.1 trillion in new investment in the U.S. economy through 1996, while the Democrats' plan would lead to a $150 billion decrease in investment spending over the same time period. [See Figure II.]

Output. Because of increased investment under the Republican plan, the nation's annual output of goods and services would grow. By contrast, reduced investment under the Democrats' plan would cause contraction. Specifically:

- The Republican plan would increase domestic output by $476 billion through 1997 and by $1.013 trillion by the end of the decade. [See Figure III.]

- more -

TABLE II

A Comparison of the Two Plans[1]

(Financial totals are in nominal dollars)

	Jobs (thousands)		Gross Domestic Product ($ billions)		Federal Deficit ($ billions)	
	House Republican	House Democrat	House Republican	House Democrat	House Republican	House Democrat
1992	+ 24	- 21	+$ 12.9	- $ 3.0	+$ 6.6	+ $ 9.8
1993	+ 84	- 62	+ 38.0	- 8.5	+ 9.6	+ 38.0
1994	+ 220	- 71	+ 67.0	- 14.8	+ 10.1	+ 47.2
1995	+ 353	- 81	+ 93.7	- 19.3	+ 8.4	+ 50.2
1996	+ 479	- 80	+ 120.8	- 16.9	+ 4.9	+ 53.9
1997	+ 593	-103	+ 143.2	- 6.3	+ 0.7	+ 58.2
1998	+ 609	- 98	+ 161.3	+ 12.1	- 1.7	+ 62.7
1999	+ 612	- 65	+ 179.2	+ 38.1	- 2.7	+ 64.0
2000	+ 617	- 24	+ 197.0	+ 67.8	- 3.5	+ 61.6

[1]Job totals are the net increase or reduction in jobs as of the year indicated. GDP numbers are annual changes. Federal deficit totals are cumulative as of the date indicated. Republican deficit reduction is the result of dynamic economic growth — changes in pension liabilities were ignored.

- The Democrats' plan would reduce GDP by $69 billion through 1997 and would result in a $49 billion gain by the end of the decade.

- Thus the difference in the two plans is worth almost $4,000 to every man, woman and child in the country.

"The difference in the two plans is worth almost $4,000 for every man, woman and child in the country."

Federal Deficit. By 1997, the additional revenues caused by greater output would offset the revenue loss from the Republican tax cuts. Thus in the long run the Republican plan is self-financing — even without the accounting gimmicks the Republicans adopted to "pay for" it.

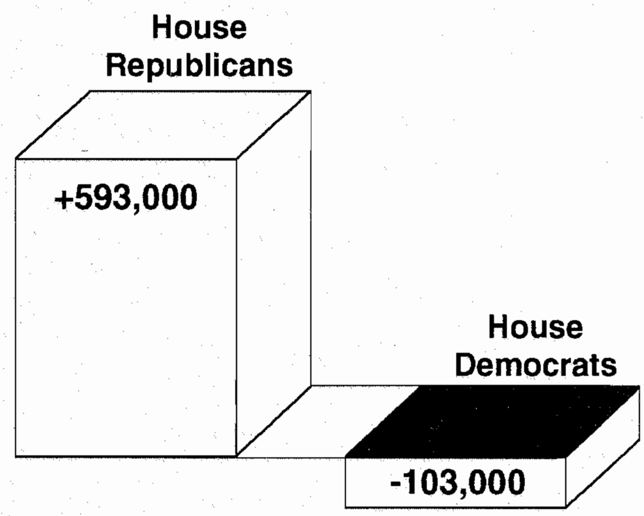
The Democrats' plan, by contrast, would result in a net loss of revenue, adding $58 billion to the federal deficit by 1997 and $62 billion by the end of the decade. [See Figure IV.]

"Through 1997, the Republicans would create almost 600,000 new jobs, while the Democrats would lose more than 100,000 jobs."

FIGURE I

Effects on Jobs

(by 1997)

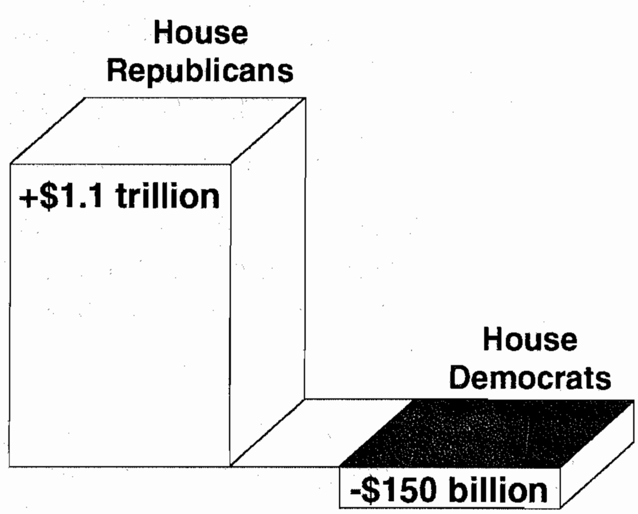


"Through 1996, the Republican plan would add $1.1 trillion in new investment, while the Democratic plan would decrease investment by $150 billion."

FIGURE II

Effects on Investment

(through 1996)

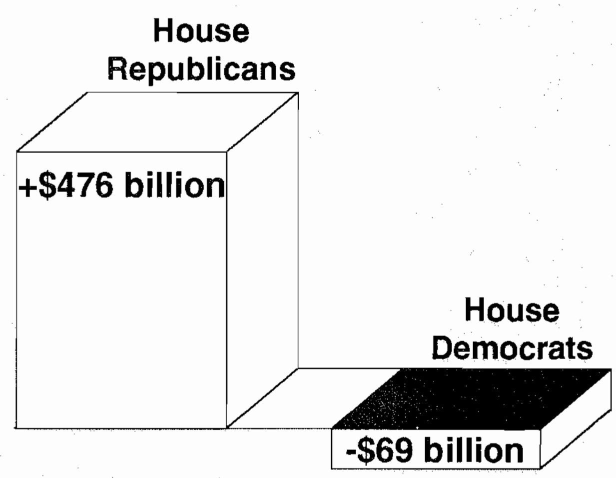


"Through 1997, domestic output would increase by $476 billion under the Republican plan and decrease by $69 billion under the Democrats' plan."

FIGURE III

Effects on Gross Domestic Product

(1992 - 1997)

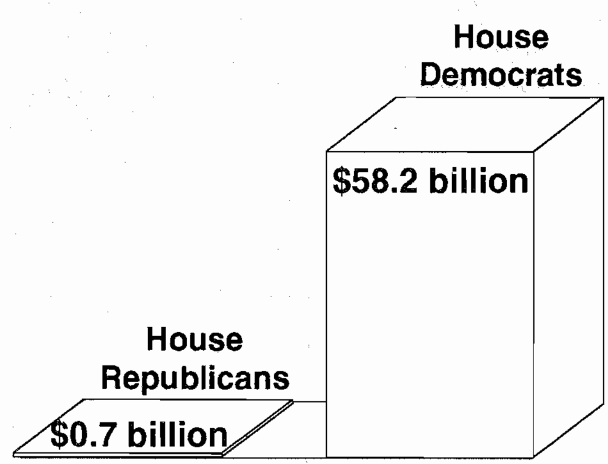


"Whereas the Republican plan is self-financing the Democrats' plan would add $58 billion to the federal deficit by 1997."

FIGURE IV

Increase in the Federal Deficit

(1992 - 1997)



The Fairness Debate

We calculate that the Republican plan will add $5.7 billion to the aftertax income of investors over the next five years. [See Table III.] By contrast, the Democrats' plan would lower the aftertax income of investors by $1.5 billion. Since investors tend to have above-average incomes, does this mean the Republican plan favors the rich?

Almost all arguments about "tax fairness" make the implicit assumption that a tax cut for investors creates no benefit for anyone else. The converse of that assumption is that government could confiscate all of the income of investors with no cost to anyone else. The experience of the U.S. economy says otherwise.

"For every additional dollar investors get under the Republican plan, national income will grow by $43."

TABLE III

Total Gains and Losses

1992 - 1996

(Amounts in billions of nominal dollars)

	House Republicans	House Democrats
Labor Income Net of Tax	**+$140.1**	**- $26.3**
Government Revenue	**+ 99.0**	**- 46.5**
Capital Income Net of Tax	**+ 5.7**	**- 1.5**
Gross Domestic[1] Income	**+$244.8**	**- $74.3**

[1]Gross domestic product less depreciation.

Republican Fairness. Because the Republican plan allows investors to receive an additional $5.7 billion in aftertax income, investors will invest about $1.1 trillion in the economy. (For the most part, investors do not gain unless they make new investments.) This investment will expand the national income by $245 billion, creating $140 billion in new wages for workers and almost $100 billion in new tax revenue for government at all levels. As a result:

"For every additional dollar investors lose under the Democrats' plan, the national income will shrink by $50."

- For every $1 in additional income received by investors, workers will receive $25 in additional aftertax wages. [See Figure V.]

- For every $1 in additional income received by investors, government will receive about $17 in new revenue.

Democrat Fairness. Because the Democrats' plan reduces the aftertax income of investors by $1.5 billion, the economy pays a heavy price. Total investment would be reduced by $150 billion, leading to a $74 billion contraction in national output. Moreover:

- For every $1 reduction in the income of investors, workers would suffer from $18 in lost wages. [See Figure VI.]

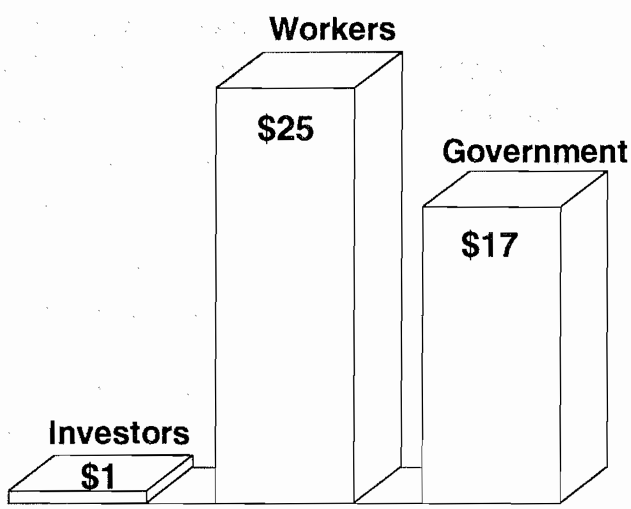
- For every $1 reduction in the income of investors, government at all levels would lose about $31 in revenue.

Under the Republican plan, investors would receive 2.3 percent of the increase in national income. Under the Democrats' plan, investors would lose 2.0 percent of the decrease in national income. What is most astonishing about the "fairness" debate is that it focuses on these almost trivial changes in the fortunes of a few and ignores the huge impact of the two plans on everyone else.

"Under the Republican plan, workers get $25 in additional aftertax wages for every $1 of additional aftertax income for investors."

FIGURE V

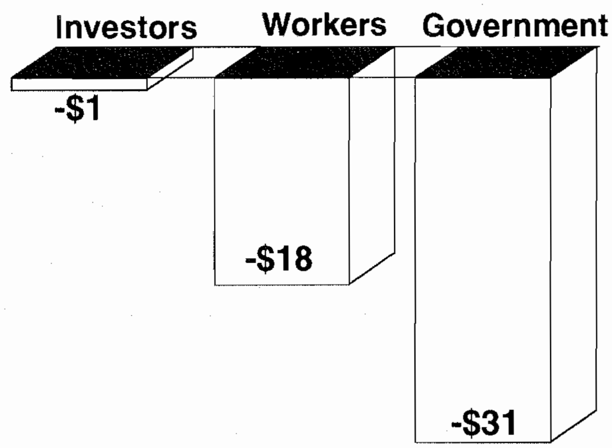
Relative Gains Under The House Republican Plan



"Under the Democrats' plan, workers will lose $18 in take-home pay for every $1 reduction in aftertax income for investors."

FIGURE VI

Relative Losses Under The House Democrats' Plan



Why Economic Forecasts Differ

The economic forecasts produced here will undoubtedly differ from the forecasts of the Joint Committee on Taxation (JCT), the Congressional Budget Office (CBO) and even the Administration's Office of Management and Budget (OMB) and the Treasury Deparment. What accounts for these differences?

Static Forecasts of Government Agencies. Among members of Congress, there is almost unanimous agreement that a higher economic growth rate is desirable and that incentives for new investment are required in order to achieve this higher rate. The economists who staff the government forecasting agencies are of a different view. In general:

- The government economists assume that tax cuts on investment spending have no effect on investment.
- Because they assume that lower tax rates on investment income have no effect on investment, these economists assume that tax cuts have no beneficial effect on the economy.
- Thus they also assume that pro-growth tax cuts do not lead to an increase in jobs or a higher rate of economic growth.

- more -

These are not the conclusions of economic studies; they are the assumptions the federal forecasters begin with before they conduct their studies.

"Government forecasting agencies begin their studies with the assumption that taxes on investment income have no effect on the amount of investment."

NCPA Dynamic Forecasts. The assumptions used by the federal forecasters are not based in reality. In fact, they are contradicted by U.S. economic experience over the past 37 years.[20] NCPA forecasts, by contrast, are based on the observation that the world financial community is willing to provide almost any amount of investment to the U.S. economy as long as investors receive an aftertax, real rate of return of more than 3.3 percent on investments in real capital.

Experience shows that reductions in tax rates on investment income always result in an infusion of capital and that this infusion will continue until the historical average rate of return of 3.3 percent is reestablished. This fact forms the basis for all NCPA forecasts.

Conclusion

Even though the House Republican plan is less stimulative than many had hoped for, all of its provisions move us in the right direction. The plan would lead to more investment, more jobs and a higher output of goods and services.

The Democrats' plan combines measures that would stimulate investment with an attempt to redistribute income from high-income to lower-income taxpayers. But since high-income taxpayers derive most of their income from investments, the higher taxes for investors would discourage savings and investment. The net result would be to prolong the current recession and reduce jobs for the foreseeable future.

In general, those left-of-center parties around the world which have won the right to lead their countries have abandoned the politics of redistribution in favor of the economics of growth. They have learned that economic growth is the most effective antipoverty program ever discovered. It is doubtful that the Democratic Party in the United States can regain the presidency unless it too learns this lesson.

Aldona Robbins
Gary Robbins
John Goodman

Footnotes

[1] Forty-five percent of capital gains income would be excluded from taxation. Thus, given a maximum tax rate of 28 percent, the actual tax would be 15.4 percent (65% x 28%). This rate applies only to assets held for three years, however. The rate would be 19.6 percent for assets held for two years and 23.8 percent for assets held for one year.

[2] By accelerating first-year depreciation, taxable income would be reduced by an additional 15 percent of investment, but the revenue loss would be made up with lower deductions in later years.

[3] Individuals would have the option either to deposit up to $2,500 per year into a conventional IRA and take a tax deduction or to make the deposit with aftertax dollars to a "flexible IRA" and withdraw the funds tax free after seven years.

[4] A 10 percent tax credit, up to a maximum of $5,000 would be allowed for a home purchased by anyone who has not owned a home in the past three years. This temporary provision would expire on June 30, 1993.

[5]"Passive loss" is the tax term applied to business losses claimed by shareholders who do not actively manage an investment. The Tax Reform Act of 1986 deems all owners of real estate as passive regardless of their involvement in the project. This provision limits the ability of taxpayers to deduct losses against current income from other sources. Losses must be deferred (without adjustment for inflation or the time value of money) until the project generates income sufficient to cover the losses. Real estate projects typically experience initial losses. The passive loss provision has dramatically affected the structure of real estate projects, making them less profitable and lowering their value. The Bush provision would apply to real estate the same passive loss rules applied to other investments. This would allow investors with a direct management role to deduct losses as they are incurred.

[6] A 10 percent luxury tax currently applies to that portion of the sales price of boats above $100,000 and planes above $250,000. This controversial tax, imposed as part of the 1990 budget summit agreement, is alleged to have cost jobs and raised little revenue. See "The Cost of Tax-Related Job Loss versus Projected Revenue Gain from Luxury Taxes in Fiscal 1991," July 1991, and update February 12, 1992, both prepared for Representative Olympia Snow and Senator Connie Mack by Joint Economic Committee Republican Staff.

[7]Other provisions would restore the tax deduction for interest on student loans, make permanent the 20 percent tax credit for investment in research and development, increase from $21 to $60 per month the amount of employer-provided mass-transit benefits a worker can exclude from taxation, allow people who sell their home at a loss to deduct that portion of the loss that exceeds 10 percent of adjusted gross income, and temporarily extend special tax benefits for people who invest in low-income housing or buy bonds to help finance low-income housing and tax benefits that encourage the hiring of young, low-income workers.

[8] The alternative minimum tax would be applied to that portion of capital gains excluded from the capital gains tax. See "Treasury's Capital Gains," *Wall Street Journal*, February 6, 1992.

[9] The ability to make deposits would be limited to individuals with incomes up to $60,000 and couples with incomes up to $120,000.

[10] To qualify, the investment must be ordered after February 1, 1992 and before January 1, 1993. It must be put in service before July 1, 1993. Even for investments within this period, the net effect of this provision is a reduction in taxes equal to 0.8 percent of the value of investment in equipment.

[11]On the sale of real estate, the lower capital gains tax rate would apply only to the portion of the asset that had not been depreciated.

[12]The House Republicans dropped the application of the alternative minimum tax (AMT) to the excluded portion of capital gains income for real estate and corporate stocks. Other assets are still subject to the AMT provision.

[13]See "The Cost of A Tax-Related Job Loss."

[14]See Gary Robbins and Aldona Robbins, "Strategy for Growth," National Center for Policy Analysis and the U.S. Chamber of Commerce, NCPA Policy Report No. 170, January 1992.

[15]It also clarifies the status of Pension Benefit Guarantee Corporation claims and the treatment of pension plans in bankruptcy proceedings.

[16]Internal Revenue Service, *SOI Bulletin*, Spring 1991, p. 17.

[17]*SOI Bulletin*, p. 17.

[18]See Lawrence Lindsey, *The Growth Experiment* (New York: Basic Books, 1990).

[19]See Gary Robbins and Aldona Robbins, "Strategy for Growth."

[20]See Gary Robbins and Aldona Robbins, "Taxes, Capital and Growth," National Center for Policy Analysis, NCPA Policy Report No. 169, January 1992.

Economic Experts

1. Gary Robbins (NCPA Senior Fellow)
   (President) Fiscal Associates 703-979-1371

2. Aldona Robbins (NCPA Senior Fellow)
   (Vice President) Fiscal Associates 703-979-1371

3. John Goodman (President)
   National Center for Policy Analysis 214-386-6272

4. Lawrence Hunter (Deputy Chief Economist)
   U.S. Chamber of Commerce 202-463-5620

5. Lawrence Kudlow (Chief Economist)
   Bear Stearns and Co., Inc. 212-272-2000

GOP Conservatives Seek Brady Ouster

Legislators Maintain Bush Is Ill-Served by Treasury Secretary

FEBRUARY 26, 1992

By Ann Devroy and Steven Mufson
Washington Post Staff Writers

Some conservative congressional Republicans, apparently emboldened by the strong showing of conservative challenger Patrick J. Buchanan in last week's New Hampshire primary, have launched a coordinated assault on Treasury Secretary Nicholas F. Brady.

They accuse him of giving President Bush bad economic advice and allowing his department to sabotage administration economic initiatives.

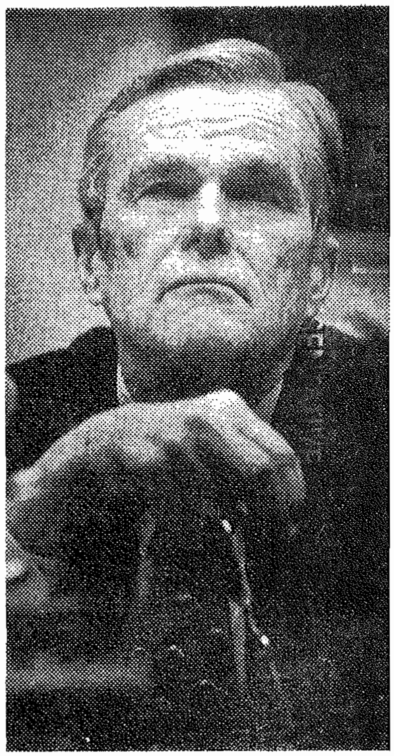
Sen. Connie Mack, a Republican conservative who co-chairs Bush's Florida campaign, called for Brady's resignation on the Senate floor yesterday, a day after a group of House Republicans complained in an Oval Office meeting with Bush that he is being ill-served by Brady.

House Minority Whip Newt Gingrich (R-Ga.) pointedly announced yesterday that Treasury staff members would no longer be allowed to attend House Republican leadership meetings.

Conservatives have long been unhappy with Brady, viewing him as the scion of what one called "Wall Street establishment rich Republican economic policy." But not since the 1990 budget agreement with Congress, when Brady and Budget Director Richard G. Darman were under virtual conservative siege, has Brady come under such direct public attack. In 1990 Gingrich vowed to force Darman's resignation.

The White House dismissed this week's assault. "The president has full confidence in Secretary Brady and believes he is doing a fine job," spokeswoman Judy Smith said. One official, in some exasperation, said the "Gingrich-Mack wing" of the GOP is "never going to be happy. They're always going to find something to complain about." Virtually no one in the administration thinks Bush is prepared to move Brady out of his job to assuage conservative Republicans, whose support he needs for reelection.

According to a Republican source familiar with the effort to oust Brady and one of the president's closest friends, "The formulation is this: President Bush's word was his bond with Republican voters in 1988 and then he broke his word in 1990. Now, when he says in another election year he won't raise taxes, his word is not believed. He needs collateral and that collateral is a treasury secretary who is one of us, who has demonstrated a belief in conservative economic positions. Nicholas Brady is not that man."



NICHOLAS F. BRADY
. . . White House dismisses criticism

The current complaint against Brady by conservatives is the proposal that Treasury sent to Congress implementing Bush's State of the Union address. These officials charge that Bush's call for a cut to 15.4 percent in the capital gains tax rate was sabotaged at Treasury and turned into a much higher effective rate. They also accuse "Treasury bureacrats" of writing into Bush's proposal a collection of revenue-raisers with no support among Republicans and widespread opposition among GOP special interest groups.

In his letter to Bush, Mack said the "message from New Hampshire" was that Americans "want fundamental change and they want it now." The "time has come to ask for Secretary Brady's resignation," Mack stated in the letter, noting he had received the same message while in Florida. Bush, he said, needs to "signal to the country" that he has gotten the message that change is needed by putting in place a new team.

Rep. Robert S. Walker (R-Pa.), one of the House members who met with Bush Monday, said Treasury had "dropped poison pills" into the president's budget proposal and added, "We are not convinced that Treasury is on our team." Conservatives had believed that Bush would put forth a budget proposal that satisfied all their concerns.

Neither Walker nor other House Republicans called for Brady's resignation Monday, but Walker said, "I don't think Brady has sat hard enough on his people. I have to hold responsible the people who are in charge." Rep. Tom DeLay (R-Tex.) said those at the White House meeting Monday complained about the capital gains tax proposal.

Gingrich, who is playing a campaign role in touting Bush's conservative credentials against Buchanan in the March 3 Georgia primary, was circumspect in his complaints. In an interview, Gingrich said, "I am not singling out any individual and I am not getting into personalities. But the Treasury Department is not serving the interests of the president."

Conservative Republicans complain that the new Bush budget proposal includes $41 billion of tax increases over the next five years, increases that were not mentioned in the president's State of the Union address. The budget package does include some tax increases, mostly for particular groups, such as certain federal, state and local government employees who were not paying the same level of Social Security or Medicare payments. But Bush administration officials assert that spending cuts are twice as big in its proposal as tax increases.

Conservative evangelical groups were angered by a Treasury proposal to require church groups to report the names of all who contribute more than $500. The Treasury believes billions of dollars in taxes have been avoided by people who overstate contributions.

Among business objections to the plan was one from the life insurance industry that complains about a measure that would end tax exemptions for income on annuity policies. Annuities have been fast-growing and have provided an alternative to tax-free Individual Retirement Accounts.