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OF THE
FEDERAL RESERVE SYSTEM
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TO: Federal Open Market Committee

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Enclosed for your information is a "fact sheet" on the President's program to control inflation, prepared at the Treasury Department.

Enclosure

Department of the **TREASURY**

NEWS

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FACT SHEET

A PROGRAM TO CONTROL INFLATION IN A HEALTHY AND GROWING ECONOMY

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A PROGRAM TO CONTROL INFLATION
IN A HEALTHY AND GROWING ECONOMY

Although our economic system remains sound and strong, with its basic vitality intact, the economy is experiencing severe difficulties. Inflation is far too high. Too many people are having trouble finding employment. The financial markets are out of kilter. Interest rates are exorbitant. Housing is suffering badly. The productive capacity of the economy is expanding too slowly.

The origins of these problems are complex. Part of the problem grew out of several international shocks:

- The disastrous world-wide drop in crop production in 1972, which sent food prices soaring.
- Two international devaluations of the dollar, which made the United States a more attractive source for other countries to buy scarce materials.
- The tripling of crude oil prices, which exerted a powerful and pervasive effect on our entire price structure.

Here at home, a long period of excessively stimulative policies created inflationary pressures that gradually and inexorably mounted in intensity. With that condition prevailing, the economy could not absorb the outside shocks; rather, those have now been built into the system, deepening and extending our problem.

Twice within the past decade, in 1967 and in 1971-72, we let an opportunity to regain price stability slip through our grasp. Thus inflation has gathered momentum and has become the chronic concern of producers and consumers alike. Indeed, today inflation is the primary cause of our recession fears.

- Consumer confidence has been shaken, causing most families to hold back on spending, as clearly indicated by the lack of growth in the physical volume of retail sales for the past year and a half.

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-- An "inflation premium" has been added to "true" interest rates, so that we now have mortgages at 9-10 percent and corporate bonds at 10-12 percent. This has warped our financial markets, including the stock market, which were structured for an economy with a relatively stable price level.

Another development that has created a serious economic imbalance is the fact that our civilian labor force has been expanding rapidly. For the size of our labor force, therefore, we are short on capital equipment. During this same period, the effectiveness of price controls in certain sectors -- e.g., steel, paper and other basic materials -- created specific bottlenecks that limited the production capacity of the entire economy. As a result, unemployment was higher than it otherwise would have been. Also, the dampening impact of price controls on profits held back new capital expansion programs in some of these vital industries.

Thus, because our problems are complex, it is clear that our program to deal with them must be comprehensive. It is also clear that the solution cannot be achieved quickly. There are no simple, instantaneous cures for our difficulties. Discipline and patience are the watchwords.

We must, therefore, have a strong policy of budgetary and monetary restraint to work down the rate of inflation. At the same time, we must provide the means for a healthy long-run growth in the capacity of the economy, correct the imbalances that have developed in recent years, and see to it that the burdens of this effort are shared on an equitable basis. Some further rise in unemployment appears probable, and we will take steps to deal with it. However, we can and will achieve our goals without a large increase in unemployment. There will be no economic depression in the United States.

AMENDING THE EMPLOYMENT ACT OF 1946

The Employment Act of 1946 makes it the policy of the Federal Government to "promote maximum employment, production and purchasing power." Although the words "purchasing power" have sometimes been interpreted as meaning price-level stability, it would nevertheless be helpful to clarify the term and make explicit in the Employment Act the goal of

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stability in the general price level. The American people have a right to receive from their government stronger assurance that policies will be followed to safeguard the purchasing power of their money in addition to policies that will provide abundant job opportunities and a rising level of living.

We, therefore, suggest that the section of the Act referred to above be amended to read as follows: ". . . for all those able, willing, and seeking to work, to promote maximum employment, maximum production, and stability of the general price level."

INTERNATIONAL COOPERATION

There is much that we and other nations can do to restore the health of the international economy. The economic problems of one nation, as well as its policies for dealing with them, affect other nations. Governments thus have the responsibility not only to maintain healthy economies but also to formulate policies in a way that complements, rather than disrupts, the constructive efforts of others.

This is particularly true for major economic powers such as the United States. Our policies to reduce inflation and restore satisfactory growth are intended to contribute to the strengthening of the international economy. We intend, further, to work with others so that:

- We can ensure secure and reasonably priced goods, particularly food and fuel, for all nations.
- We can minimize national policy conflicts or distortions that direct resources away from their most productive uses.
- We can provide early warning of potential shifts in supply and demand so that nations can avoid potential disruptions.
- We can try to harmonize national efforts in such areas as conservation, investment and balance of payments management.

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A small delegation led by Ambassador Eberle departed today for Canada, Europe and Japan to discuss the policies described herein and to explore how we can better address and resolve common problems in a mutually supportive fashion.

A cornerstone of our international efforts is the multilateral trade negotiation scheduled to begin this fall. Passage of the Trade Reform Act will provide the United States with an opportunity to help improve the international trading order and to ensure that United States interests are well served therein. Without this bill, the United States will be regarded abroad as lacking the tools or the interest to build multilateral solutions to pressing economic problems. With it, the United States can play a leadership role in negotiating guidelines to reduce distortions of trade and investment that force workers or farmers in one nation to pay for the economic policies of another nation. We can also work toward a multilateral system of safeguards that provide for temporary -- but only temporary -- limits on imports when there is a need for certain industries to adjust smoothly to economic shifts.

FOOD AND FIBER

Food prices are of major concern in our fight against inflation. Because of weather problems and heavy demands from around the world, food prices are anticipated to increase at an annual rate of 10 percent or more over the next 18 months. Only by expanding farm production, improving productivity, and containing foreign demand can we hope to reduce the rate of increase.

Increased production offers our brightest hope for combating inflation, and we are committed to a program of all-out food production. There are presently no government restrictions on planting of wheat, feed grains, soybeans and cotton (excluding extra-long-staple cotton). To remove restrictions on rice production, we support pending legislation, but with a noninflationary target price. In addition, new legislation, which we support, has just been introduced to remove restrictions on the production of peanuts and extra-long-staple cotton.

Farmers must be assured of adequate supplies of fertilizers and fuel. The Secretary of Agriculture has been directed to work with the interagency Fertilizer Task Force to establish a reporting system. Fuel will be allocated if necessary. Authority

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will be sought to allocate fertilizer, if that is needed. We will work with fertilizer companies to initiate voluntary efforts to reduce nonessential uses of fertilizer.

Over the past weekend the Federal Government initiated a voluntary program to monitor grain exports. We can and shall have adequate supplies at home, and through cooperation meet the needs of our trading partners abroad. A committee of the Economic Policy Board will be responsible for determining policy under this program. In addition, in order to better allocate our supplies for export, the President has asked that a provision be added to Public Law 480, under which we ship food to needy countries, to waive certain of the restrictions on shipments under that Act on national interest or humanitarian grounds.

The U. S. Department of Agriculture and the National Commission on Productivity have been directed to help reduce the cost of food by improving efficiency in the agricultural sector. The Department and the Council on Wage and Price Stability will review marketing orders to insure that they do not reduce food supplies. Government regulations will be examined to eliminate those that interfere with productivity in the food processing and distribution industries.

Upward pressure on U. S. food prices will be reduced by helping developing nations to become more self-sufficient. We will share our advanced agricultural technology and aid in the construction of new fertilizer plants. We will support food reserve and emergency food aid programs. We are also taking steps to assure that the burden of the current tight feed grain situation is equitably distributed.

While increased food supplies are the only effective weapon against higher food prices in the long run, it takes time to grow those supplies. We cannot expect to see immediate benefits from the initiatives outlined here. We can, however, be confident that policies to maximize food and fiber production and to restrain food price increases are being pursued vigorously.

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ENERGY

I. General Statement

Expensive petroleum from insecure foreign sources jeopardizes national security, increases worldwide inflation and places strains on the international financial system. Therefore, in order to reduce United States dependence upon foreign supplies of energy, the President has decided upon the following program to meet the current energy challenge.

The immediate objective is to reduce oil consumption one million barrels per day by the end of 1975 below what it would have otherwise been without affecting industrial output. This energy program calls for both mandatory and voluntary action.

If immediate reductions are not achieved through the energy program presented today, the President will seek more stringent means to insure that United States dependence is reduced.

II. Develop a new conservation policy

During the embargo last winter, Americans responded to energy conservation voluntarily. Now, though the crisis is less obvious, Americans must continue to apply voluntary restraint in the use of energy. As part of our continuing effort to conserve energy, the individual American and the American Industry and Government must think and act conservation, of not only energy but also resources and commodities that are used in our day to day life.

III. Specific Program

A. Submit Legislation to Require Use of Coal and Nuclear for New Electric Power Generation and Conversion for Existing Plants

The Administration's policy is to eliminate oil and natural gas fired plants from the Nation's mainland baseloaded electric capacity where it is feasible to convert to coal or nuclear without endangering public health. A meeting of representatives from the utilities, the coal and nuclear industries, state regulatory

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commissions and the relevant Federal agencies will be called by FEA to establish within 90 days a schedule for phasing out enough oil-fired plants to save 1.0 million barrels per day and to provide a list of actions required to ensure that the schedule is met. Any legislation necessary to accomplish this goal will be submitted afterwards.

Relevant considerations inherent in such a program are as follows:

-- Potential for Conversion

Existing oil and gas plants that are convertible	.75 MM b/d
Future plants (before 1980) scheduled for oil or gas (30,000 MW)	1.0 MM b/d
Total	<u>1.75</u> MM b/d
Goal (allowing for cases where conversions will not be attempted)	1.0 MM b/d

-- Costs

- A. Because future plants are in varying stages of planning and development, total cost of one million barrels per day conversion is not known.
- B. However, report from utilities included in "existing plants" category above indicates that 750 thousand b/d conversion costs total \$106 million. It should be noted that these costs are considerably lower than what it would cost to continue burning oil at current world prices.

-- Illustrative Comparison of Cost of Using Coal vs. Oil
(based on 1 million barrels/day)

- 1 Cost of coal = \$ 6 million (at \$25 ton)
- 2 Cost of residual = \$12.0 million/day (at \$12.00 barrel)
- 3 Savings = \$6.3 million/day or \$2.2 billion/year

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- There are approximately 500 coal fired units that will not meet state regulations as of June of next year. However, most of these could meet the primary air quality standards (i.e. standards to protect human health).

These plants use 185 million tons (1/3 of the nation's total coal consumption) of coal per year. This program would allow these plants to continue to burn coal, thus easing additional pressure on oil supplies.

B. Defense Production Act

The Defense Production Act will be used selectively to ensure sufficient supplies of scarce materials needed for energy development projects. This Act was recently invoked to give priority to the delivery of supplies to expedite construction of the Trans-Alaskan pipeline terminal facilities.

C. Automobile Industry must Develop Program for Gasoline Savings

During the past two sessions of Congress, legislation to require fuel saving on new automobiles has been considered. Pursuant to the Energy Supply and Environmental Coordination Act of 1974 a specific study of one aspect of this question is now underway. Unfortunately, the sum total of legislative requirements on automobile manufacturers has often caused confusion, additional cost to the consumer and unworkable deadlines. Therefore, the President is requesting the major automobile manufacturers to submit a five-year schedule of their plans to produce more efficient automobiles. Goals on efficiency for industry to meet will then be established. If necessary, the President will present legislation to the Congress for consideration.

D. Industry must Conduct Energy Audit and Develop Savings Programs

During the last six months, it has been demonstrated time and again that individual companies can cut energy usage dramatically. Nationwide, the potential savings for all industries under a strict conservation program can be significant. The President has requested the Secretary of Commerce to develop energy use guidelines which will suggest ways for industry to use energy more efficiently. The Secretary will also report on energy savings in specific industries, and

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communicate that information to businessmen across the nation. In addition, the Commerce Department will monitor to determine areas of energy misuse within industry, and suggest alternatives to stop such waste.

E. More rigid compliance with the maximum speed limit of 55 miles per hour; suggest new traffic control measures

The 55 mile speed limit set by Congress earlier this year has saved at least 250,000 b/d of petroleum. The Administration will emphasize the importance of rigid enforcement of this limit by State and local law enforcement agencies. In addition, the President is directing the Secretary of Transportation to work with State officials to suggest additional traffic control measures for conserving gasoline.

F. Further Conservation within Government

The effects of energy conservation efforts within government has been dramatic. Most agencies have far exceeded their goals. However, governmental conservation programs will be made stricter, and enforced more vigorously. As a top priority, a review will be made of all governmentally imposed impediments to energy conservation, in so far as they adversely affect the day-to-day programs of both the government and the private industry operations..

Specific actions mandated and underway, or to be taken :

- Thermostats lowered to 68 degrees in the winter and raised to 78 degrees in the summer.
- Lighting reduced in public buildings.
- Speed limits on government vehicles reduced.
- Cut backs ordered in the number of trips taken, including miles driven and miles flown.
- Car pooling locators to be set up within metropolitan government bases.
- Parking spaces to be allocated on a priority basis to car poolers.
- Smaller automobiles to be purchased to replace larger cars

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- Decorative lighting to be reduced.
- Outside lighting to be reduced.
- Voluntary Conservation Actions:

G. Reduce energy consumption in commercial buildings

The commercial sector of the economy accounts for almost 15% of our total energy use. Studies have shown that commercial energy requirements can be significantly reduced by improved efficiency measures, and by taking positive steps to reduce lighting, heating and air conditioning. A 10% reduction in this sector can save the equivalent of approximately 500,000 barrels of oil per day.

H. Reduce energy consumption in residences

Residential consumption of energy accounts for approximately 20% of total energy use. Prudent use of heating and air conditioning, reduced usage of hot water, lighting and appliances, and improved home insulation has the potential for saving the equivalent of well over one million barrels of oil per day. These steps would also, of course significantly reduce energy costs for the consumer.

I. Reduce gasoline consumption

About one third of all automobile travel consists of commuting to and from work. If the average number of passengers per commuter auto were to increase by one, a reduction in gasoline usage of well over 500,000 barrels per day could be achieved. The resulting lower consumption would also reduce the commuters out-of-pocket costs for high priced gasoline.

Regarding specific voluntary actions relating to (a), (b) and (c), the Administration will:

- Encourage everyone to lower thermostats in the home in the winter and raise them in the summer.
- Ask architects to design buildings with energy conservation in mind.
- Ask motorists to keep cars tuned and maintain proper tire pressure.
- Ask everyone to reduce temperature settings on hot water heaters.

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- Ask everyone to turn off pilot lights on furnaces in the summer.
- Encourage everyone to use cold water for laundry.
- Encourage the use of public transportation.
- Urge an increase in the use of car pools.
- Urge reduction in use of nonessential home appliances.
- Urge reduced use of stoves, refrigerators, televisions, electric lights, washing machines.
- Encourage home owners to insulate and install storm windows.
- Urge turning off outside gas lights.
- Urge measures to increase the load factor on airline flights.

J. Request state and federal regulatory authorities to eliminate rate schedules which encourage excessive energy consumption

The utility industry, under both state and federal regulations, have often developed rate structures that encourage increased energy consumption. Regulatory authorities should seek to design rate structures that encourage maximum energy conservation, promote use of generation capacity in off-peak periods, and only charge individual categories of users the cost of the power they actually consume.

K. Natural Gas Supply Act

Natural gas is an invaluable source of clean, environmentally sound energy. For fifteen years, the Federal Power Commission has controlled and kept low its wellhead price, and thus reduced incentives to the development of new domestic supplies. In 1957, new discoveries of natural gas totalled approximately 22 trillion cubic feet. By 1972 this had fallen to less than three trillion cubic feet. In 1955 the U. S. had a 22.5 year supply of gas reserves, and in 1972 only 10.7 years.

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The nation is now importing foreign liquefied gas (LNG) at prices three times controlled domestic price. The nation faces continued and increasing rates of curtailment of gas being supplied to current users, including gas for agricultural production.

The only real solution to the supply problem lies in deregulation of new gas, so as to stimulate production.

Legislation to achieve this result has long been stalled in the Congress. This logjam must be broken, so that domestic gas reserves may be identified and brought into production as quickly as possible.

- L. Naval Petroleum Reserves - permit maximum production from reserve #1 (Elk Hills) and implement full scale exploration and development of production capability of reserve #4 (Alaska)

At the present time, two Naval Petroleum Reserves, Elk Hills, California (NPR #1), and NPR #4 in Alaska, could, if fully developed, provide significant production capability. Elk Hills is about 50% developed but needs further development to place it in a state of readiness. It is estimated that production capability of 160,000 barrels per day could be achieved within two months, with the long term maximum efficient rate of production at about 267,000 barrels per day. The estimated potential of NPR #1 runs as high as 1.7 billion barrels. The vast tract in Alaska, NPR #4, is largely unexplored but offers a significant potential for development. Recoverable reserves are estimated to be as much as 30 billion barrels.

The statutory authority for the naval petroleum reserves, and oil shale is included in Chapter 641, Title 10, U.S. Code. Key provisions in the authority provide that the reserves shall be used and operated for:

- (1) The protection, conservation, maintenance and testing of the reserves.

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- (2) The production of petroleum, gas, oil shale or products thereof, whenever and to the extent the Secretary of the Navy, with the approval of the President, finds that it is needed for national defense and production is authorized by a joint resolution of Congress.

The President is directing the Secretaries of Defense, Navy and Interior, within the next 90 days, to develop proposals (including any needed legislation) directed toward the exploration and development of NPR #4 as rapidly as possible.

M. Clean Air Act

The Clean Air Act Amendments of 1970 represent a landmark in our progress toward environmental protection, and definite progress is being made in cleaning up the Nation's air.

The Act describes very stringent guidelines for compliance by mobile and stationary sources. Many of these goals are achievable as drafted. In some cases, however, more flexibility is needed to achieve the objectives of the Act and to allow use of coal, the nation's most abundant domestic energy source. The amendments that have been transmitted to the Congress by the Administration would provide this needed flexibility to effectively respond to the nation's energy problems without jeopardizing the Act's health related requirements. Passage of all of these amendments will not diminish continuing efforts for a cleaner environment.

N. Surface Mining

Coal is the nation's most abundant and available energy resource. The Administration has proposed and long supported surface mining legislation that would allow continued and accelerated development of domestic coal reserves with appropriate protection of environment values.

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Severe problems still remain with some of the provisions of the legislation which has passed both houses of the Congress. Its enactment as now drafted could involve not only serious production losses but inflationary cost impacts throughout the entire economy.

Secretary Morton and his staff have been working closely with the committee to resolve the most important of these problems, including surface owner protection provisions, funding absolute prohibitions of mining in certain areas, unnecessarily broad statements of purposes, and provisions for multiple litigation that could delay or halt ongoing production efforts.

O. Nuclear Plant Licensing Bill

The 9-10 years now required to bring nuclear power plants on line must be reduced. Towards this end, Congress should pass the Nuclear Plant Licensing Bill which will expedite licensing and construction power costs, and accelerate U.S. energy self-sufficiency.

P. Windfall Profits Tax

Since 1973, the prices that may be charged for domestic crude oil production have been strictly controlled by the Cost of Living Council and the Federal Energy Administration (formerly the Federal Energy Office).

Various measures are available to stimulate production from our existing fields by adjusting these controls. Such adjustments are needed on a priority basis, but they could generate sudden profit increases for companies producing oil.

The Administration has proposed a windfall profits tax that would cushion this shock and reduce such profits, and this requires prompt action by the Congress. Expeditious enactment of this tax measure is necessary to maximize production without undue enrichment of the industry.

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Q. Deepwater Port Facilities Act

Pending legislation would authorize the Federal Government to grant permits for the construction and operation of offshore oil terminal facilities. Such facilities would allow imported oil to be transported more safely and economically on very large crude carriers, and reduce tanker traffic in the nation's already overcrowded harbors. It would encourage the construction of domestic refineries and thus lessen U.S. dependence on imported products from foreign refineries. An extensive environmental impact statement already prepared indicates that the amount of oil spilled in the nation's harbors and coastal regions will be reduced by these facilities.

R. Energy Research and Development Administration, ERDA

The President is urging to complete consideration of legislation to create ERDA before the recess. ERDA's mission will be to develop technologies for efficiently using fossil, nuclear and advanced energy sources to meet growing needs and in a manner consistent with sound environmental and safety practices. The agency will have responsibility for policy formulation, strategy development, planning, management, conduct of the energy R&D and for working with industry to assure that promising new technologies can be developed and applied.

S. Accelerate Oil Leasing of Federal Lands on the Outer Continental Shelf

Prospects for large, new discoveries of onshore oil and gas deposits in the lower 48 states are small. For this reason, leasing of the Federal OCS must be greatly accelerated with a target of ten million acres annually in 1975. This is an amount 5-times larger than the 2 million acres expected to be leased during 1974; and 1974 in turn is twice the acreage leased during 1973. To sustain this schedule it will be necessary to lease frontier areas off Alaska, California and the Atlantic coast. The accelerated leasing program will comply with all provisions of the National Environmental Policy Act, and every step will be taken to insure that development will be carried out under environmentally sound conditions. The President has directed the Secretary of Interior to meet with coastal state officials to establish the program needed to rapidly develop Outer Continental Shelf resources.

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T. Incentives to Secondary and Tertiary Production

Under current technology, 65 billion barrels of oil would be left in the ground in known reservoirs. Some existing price controls have a tendency to discourage increased production from existing oil fields, especially declining fields. The President has directed the adjustment of these controls so as to maximize incentives to use secondary and tertiary production methods in such cases.

U. Coal Leasing of Federal Lands

The government intends to complete steps to resume leasing of federal lands in 1975 to develop the vast coal resources underlying these lands. Increased world oil prices have forced the nation to look to alternative supplies of energy. The nation's most plentiful resource is coal, with over 1.5 trillion tons beneath the surface of America; public lands alone contain 200 billion tons. The President has directed Secretary of the Interior Rogers C.B. Morton to complete the requisite environmental impact statements and move to establish a program for leasing coal on Federal lands in 1975 that will insure the availability of this resource when needed for immediate production.

V. Leasing Public Lands for Oil Shale and Geothermal Development

Early this year, the government leased 18 tracts in known geothermal areas. Ten of these tracts, located in the Geysers Field of Northern California, can supplement efforts on private lands that have already proven to be of commercial value. The remaining tracts, in the Imperial Valley of California, offer a testing opportunity--tapping hot, mineralized water for commercial use as an energy source.

Early this year, four oil shale tracts were leased in Colorado and Utah which are expected to be of commercial value. Developmental work, already underway, will assess the economic and environmental feasibility of exploiting this vast oil shale resource--estimated as containing 400 billion barrels of oil in the western United States.

The Administration will immediately re-evaluate the government's oil shale and geothermal leasing programs with a view toward encouraging more rapid development of these resources.

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W. Completion of Plans to Bring Alaskan Gas to Market

Exploration and development of natural gas in Alaska is moving very rapidly. By next year, the basic information will be available to determine whether Alaskan gas should be brought to the U. S. via a pipeline across Alaska or a pipeline across Alaska and through Canada. In response to a congressional mandate, environmental and economic analysis for each alternative is under way, and should be completed early next year. With the completion of these studies and plans, the President will determine whether and what legislation is needed to expedite access to this large source of environmentally clean energy.

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INCREASING THE PRODUCTIVE CAPACITY
OF THE ECONOMY

In the long run, the answer to inflation is an economy with sufficient productive capacity to meet the demands of its people. This growth can be accomplished in three inter-related ways: First, through a better-trained, better-motivated and healthier work force. Second, through a larger and more productive stock of plant and equipment. Third, through an increase in the operational efficiency of workers and their equipment -- in short, by working smarter.

Increasing Investment. To accelerate the growth of capital investment, the President is calling for an increase in and a restructuring of the investment tax credit. The credit will be increased from 7 to 10 percent; for utilities the increase is from 4 to 10 percent. The restructuring of the credit will eliminate existing restrictions that now limit the incentive value of the credit and that discriminate unfairly between types of taxpayers and investments that qualify for the credit. (See Tax Proposals.)

Strengthening the Capital Markets. The financial markets are the centerpiece of our economic system. Healthy and freely functioning markets to bring together savers and investors are crucial to the expansion of the nation's plant and equipment, which in turn is essential to the creation of new jobs and also to the growth of productivity that permits a rise in our standard of living. Every American has a vital stake in the vitality of our financial markets.

The most important thing that we can do to restore the glow of health to our capital markets is to get control of inflation. A rapidly rising price level is the bitter enemy of savings and investment.

As part of this anti-inflation effort, we will take a step that will also have, of itself, a direct beneficial impact on our financial markets. That step is to move toward a balanced budget, and to end the drain that past deficits have made on our capital markets. This would mean that more of the savings generated by our private economy could be used for new productive investment.

And in this context, we must also take account of the demands of the off-budget agencies of the Federal Government, and Federal credit guarantees (for housing, student loans, etc.)

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as well.

We must create a better environment in the financial markets for equity capital. In recent years, corporations have been unable to raise adequate new equity capital. They have been adding heavily to their debt, however, and as a result the capital structure of business has been getting out of balance, with too much debt and too little equity. This is especially true for our electric utilities.

As a contribution toward the solution to this problem and also to improve the health of our financial markets and to encourage investment, the President has proposed tax legislation to provide that dividends paid on qualified preferred stock be allowed as a deduction to the paying corporation.

The Administration also supports strongly the Financial Institutions Act of 1973 (see Thrift Institutions), and the securities reform legislation pending in Congress that would authorize the Securities and Exchange Commission to establish a national market system for securities transactions. We are also working with the Congress to revise the treatment of capital gains and losses in such a way as to increase efficiency in the flow of capital.

In addition, we support pending legislation to eliminate the withholding tax on interest and dividend income accruing to foreign holders of U.S. securities. Elimination of this would stimulate a larger flow of funds to capital markets in the United States.

CREDIT ALLOCATION

An issue that has been widely debated in recent years is whether or not the Federal Government should intervene directly into the financial markets to require banks and other credit institutions to make more loans for socially desirable purposes and less for "unproductive" purposes. In our view, allocation of credit by the Federal Government would be highly undesirable. There is no basis for believing that the Government could in fact allocate credit in a way that was acceptable to the American people.

However, the Federal Advisory Council, a statutory body that advises the Federal Reserve Board, has suggested constructive guidelines for credit extension by the banks on a

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voluntary basis. The Federal Reserve Board has endorsed these guidelines, and expects compliance by the banks.

ANTITRUST

The elimination of outmoded government regulation must of course be accompanied by dedicated and vigorous enforcement of the antitrust laws. Violation of these laws is a serious crime. Only through maintenance of vigorous competition can we realize the benefits of less regulation. Our efforts must be strengthened. We will focus particularly on more effective enforcement of the laws against price fixing and bid rigging. These types of activities which increase prices substantially cannot be permitted.

Illegal fee schedules in the professions and in real estate closings must also be eliminated. Such conduct will be prosecuted to the full extent of the law.

To support this intensified enforcement effort, the President has asked for legislative enactments in two areas. First, we must increase the penalties associated with anti-trust violations -- for corporations the maximum fine should be increased from \$50,000 to \$1 million while for individuals it should be increased from \$50,000 to \$100,000. Second, we must strengthen the investigation powers of the Antitrust Division of the Department of Justice. This can be accomplished by speedy passage of the Administration's legislation now pending before the Congress that would amend the Antitrust Civil Process Act, and to provide laws which would give enforcement agencies greater capability to detect bid rigging.

GOVERNMENT REGULATION

The Federal Government imposes many hidden and inflationary costs on our economy. Laws and regulations have been put into effect with little concern for the underlying costs. These billions of dollars of increased costs are passed on to American consumers in the form of higher prices. A broad program will be undertaken to attack this problem and to identify opportunities for change. These proposals could save billions of dollars, which could then be devoted to more productive investments. They would also reduce the visibility and impact of government on the American people.

The Council on Wage and Price Stability will act as a continuing watchdog on the inflationary actions of the Executive

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Departments and agencies to uncover laws and regulations that raise costs and stifle economic flexibility and initiative. We need to eliminate or alter many restrictive practices of the Federal Government in areas such as transportation, labor and agriculture -- practices that unnecessarily increase the overall costs of goods and services. Both the Conference on Inflation and the Joint Economic Committee recommendations support this approach. The Council will devote a very substantial part of its effort to this function.

National Commission on Regulatory Reform. The independent regulatory commissions, through their broad policy determinations and individual case decisions, create a body of regulatory policy separate and apart from that of the rest of the Executive Branch. The President will submit legislation to create a National Commission on Regulatory Reform to examine the policies, practices and procedures of these Agencies and develop appropriate legislative and administrative recommendations. Its membership should include Executive Branch, Congressional, and private sector representation.

Inflation and Job Impact Statement. The President will require all executive agencies to develop Inflation Impact Statements to assess the inflationary consequences of major legislation or regulations prior to the agency taking action. Such an impact statement would sensitize government decision-makers to the broader consequences of government activities, and to the tradeoff of costs versus benefits in government programs.

The President recommends that the Congress set a similar requirement for itself. The proposed Commission on Regulatory Reform should examine the feasibility of legislation requiring independent regulatory agencies to do a similar preanalysis of their actions.

Speedier Adjudication and Proceedings. New approaches are required to eliminate the interminable delays often created before regulatory matters are resolved. The courts and the independent regulatory agencies are urged to develop new approaches to assure prompt resolution of pending matters. The Executive Branch will undertake a similar effort.

States and Local Governments. Other governmental units are urged to undertake a similar broad program to bring under control the inflationary influence of government at all levels.

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Enactment of Pending Legislation. There are several important pieces of legislation now pending before Congress, whose enactment would help to reduce the burdens now imposed on the economy by government activities. These include the Surface Transportation Act, the Financial Institutions Act, Trade Reform, and the creation of a Paper Work Commission to review the administrative "bookkeeping" requirements levied by government on the private sector. Congress is urged to move swiftly to enact these measures.

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COUNCIL ON WAGE AND PRICE STABILITY

The Council on Wage and Price Stability will devote primary emphasis to two functions: First, it will act as a watchdog on the actions of the Executive Departments and Agencies of the Government that raise costs and impede competition. It will recommend needed changes in administrative procedures, and changes in legislation where necessary, to correct these practices.

Second, it will monitor wage and price movements in the private sector. In general, the Council will carry out this function by seeking the full, voluntary cooperation of labor, industry, and the public to solve problems of mutual concern. The Council will cooperate fully with the President's new Labor-Management Committee. In addition, the Council has the power to conduct public hearings and intends to use it to explore the justification for price and wage increases, as appropriate.

Among other duties the Council on Wage and Price Stability will work with the Cabinet Committee on Food and the Inter-agency Fertilizer Task Force. Also, in dealing with specific sectors in which price pressures are particularly virulent, efforts will have to be concentrated on food, energy, construction, medical care and primary industrial capacity.

The Council, however, will not be a wage and price control agency. Controls do not stop inflation; they did not do so the last time around nor even in World War II when prices increased despite severe rationing.

Indeed, controls can make inflation worse. They often create shortages, hamper increased production, stifle growth and cause unemployment. Ultimately, they can cause the fixer and black marketeer to flourish while decent citizens confront empty shelves and long waiting lines.

NATIONAL COMMISSION ON PRODUCTIVITY

Increased productivity -- working smarter to increase the total economic output of our work force and equipment -- is a vital component of the drive to increase production. This long-term goal will be pursued by a revitalized National

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Commission on Productivity. The Commission will also extend and deepen the drive to increase productivity in government -- Federal, state and local. It is important that government set a good example of leadership in this effort, and we may be sure that there is no shortage of opportunity for productivity in the operations of government. The rest of its effort will be in the private sector, with primary emphasis on meaningful programs at the plant level. Special attention will be devoted to food, transportation, construction and health-services.

EMPLOYMENT ASSISTANCE

Increases in unemployment have raised the Nation's unemployment rate to 5.8 percent in September. During this period of high inflation and unemployment, there is a need for Federal standby authority with minimal inflationary impact, which will help alleviate the impact of unemployment should unemployment rates rise. Such action is necessary to help alleviate unemployment problems in areas most affected and to assure that the impact of inflation does not unduly burden those workers least able to bear the costs.

The National Employment Assistance Act of 1974 would respond to these needs by authorizing, during the next 12-month period two programs which would begin to operate should the national unemployment rate average 6 percent or more for 3 months:

(1) A temporary program of income replacement known as the Special Unemployment Assistance Program for experienced unemployed workers in areas of high unemployment who have exhausted all other unemployment compensation or who are not eligible for such compensation; and

(2) A program of employment projects for these same areas, known as the Community Improvement Program.

While the primary purpose of the two programs is to alleviate the hardships of unemployment upon individuals, it will also alleviate the adverse impact on those local economies hardest hit by unemployment.

The unemployment assistance benefits serve to cushion the effects of protracted unemployment by providing additional income replacement to workers who have either

exhausted their regular unemployment compensation benefits or to individuals with a demonstrated labor force attachment not otherwise eligible for unemployment insurance benefits. Not only does this replace lost income, but it provides workers with the time and opportunity to look for work consistent with their skills and experience.

The table below shows funds and services now available under Unemployment Compensation laws and the Comprehensive Employment and Training Act (CETA). It also indicates how much would become available over a twelve month period for current unemployment programs, and for the two new proposed programs, at average national unemployment levels of 6 percent and 6.5 percent. Title II of the National Employment Assistance Act would make a further \$1 billion available if national unemployment exceeded 7 percent on average for three months or more.

	<u>5.8%</u>	<u>6%</u>	<u>6.5%</u>
CETA Public Service Jobs			
Funds:.....	\$1,015 mil.	\$1,015 mil.	\$1,015 mil.
Jobs:.....	170,000	170,000	170,000
CETA Other Training and Employment			
Funds:.....	\$1,700 mil.	\$1,700 mil.	\$1,700 mil.
Man Years:.....	380,000	380,000	380,000
Unemployment Benefits (current law)			
Payments:.....	\$7,775 mil.	\$8,145 mil.	\$9,065 mil.
Beneficiaries:.....	7.9 mil.	8.2 mil.	9.2 mil.
		(annual rate)	
National Employment Assistance Act			
Special Unemployment Benefits			
Payments.....	----	\$2,120 mil.	\$2,550 mil.
Beneficiaries.....	----	2.73 mil.	3.31 mil.
UI Exhaustees.....	----	(.83 mil.)	(1.05 mil.)
Previously Ineligible.....	----	(1.9 mil.)	(2.26 mil.)
Community Improvement Projects			
Funds.....	----	\$500 mil.	\$1,250 mil.
Man Years of Employment.....	----	83,000	208,000

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The initiation of temporary projects by State and local governments is perhaps the least inflationary way of providing jobs for unemployed workers. Jobs provided by these projects help to cushion the loss of income due to unemployment, while enabling State and local governments to provide their citizens with a socially useful product.

Because projects under this program will be generated in and geared to areas with high unemployment in which there exists a substantial amount of available manpower, there should be little or no adverse impact on the regular labor market. There is a limit of \$7,000 a year for jobs authorized by this program and therefore the average wages will be considerably less than those earned in the private sector. Most workers will obtain private jobs as the economy grows.

The added cost of Community Improvement Projects may be offset somewhat by reduced demand for food stamps and welfare payments, and by some increase in tax receipts from employees in these projects.

Basic funding provisions of the National Employment Assistance Act. Funds for both the Special Unemployment Assistance Program and the Community Improvement Program become available when the national unemployment rate reaches 6.0 percent on average for three consecutive months. For the Special Unemployment Assistance Program, such funds as are necessary are authorized if unemployment is above this level. For Community Improvement Program, successive increments of funds are authorized if the national unemployment level reaches, for three consecutive months an average of:

- 6.0 percent -- \$500 million dollars authorized;
- 6.5 percent -- another \$750 million dollars authorized; and
- 7.0 percent -- an additional one billion dollars authorized.

When the national unemployment rate recedes below these respective levels for three consecutive months on average, Federal funds for new projects will cease.

Eighty percent of the available funds for Community Improvement Projects will be distributed by formula among

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eligible applicants based on (1) the relative number of unemployed residing in areas of substantial unemployment within their jurisdictions, and (2) the severity of unemployment; 20 percent would be expended at the discretion of the Secretary, principally to finance projects in areas which become eligible after the formula distribution is made.

The local labor market area--and balance of State--unemployment rates determine the communities in which both programs will be operating. Both programs are directed to those areas in which unemployment is highest. Both programs come into effect in a labor market area, with a population of 250,000 or more, when it has an unemployment rate equal to or in excess of 6.5 percent for three months on average. The balance of each State not included in such areas will constitute a single area in which the programs will become effective, subject to the same unemployment rate criterion. When the local unemployment level recedes below 6.5 percent on average for three consecutive months no new individuals become eligible and no new projects may be started.

Special Unemployment Assistance Program. This new temporary unemployment assistance program will be separate from but supplemental to the existing Federal-State Unemployment Insurance (UI) System, and is designed to extend coverage to experienced persons in the labor force who have exhausted their UI benefits or are otherwise ineligible for such benefits. The program would be operated through agreements with the States. All experienced members of the workforce will be eligible for benefits as follows:

- They must have last worked in a labor market area (or balance of State area) with substantial unemployment.
- Benefits will be governed by benefit provisions of each State UI law.
- Individuals who had exhausted their benefits under State UI programs will be eligible for a maximum of 13 weeks benefits.
- Individuals who were not previously eligible for State UI benefits will be eligible for a maximum of 26 weeks provided that they have attachment to labor force as required by the relevant State UI law.

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- Benefits for UI ineligibles will generally be the amount that would be payable as computed under State law if all work was performed for covered employers.
- No new beneficiaries would be eligible after December 31, 1975.

Community Improvement Program.

- New program is structured so that as the national employment rate rises, more money is available for community improvement projects.
- Projects are limited to areas eligible for the Special Unemployment Assistance Program.
- Eligible applicants are prime sponsors under the Comprehensive Employment and Training Act, in areas that qualify.
- Projects may be with State or local government agencies.
- Each Community Improvement project is limited to 6 months duration.
- Not more than 10 percent of a sponsor's funds may be used for administrative costs, supplies, material, and equipment.
- Individuals eligible for employment on these projects are those who have exhausted their benefits under the Special Unemployment Assistance Program.
- Wages paid project employees must be at least the minimum wage under the Fair Labor Standards Act, or the State or local minimum wage, whichever is higher; however, in no case may the wage exceed an annual rate of \$7,000. State or local governments may not supplement wages with their own funds.
- Prohibitions against political activities and discrimination apply to the program.

The Community Improvement Program will provide funding for projects such as conservation, maintenance or restoration of natural resources, community beautification, anti-pollution and environmental quality efforts, economic development and the improvement and expansion of health, education, and recreation services and such other services which contribute to the community.

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INTERIM HOUSING AID

President Ford proposed extending, on a temporary basis, the advantages offered by the Government National Mortgage Association (GNMA or Ginnie Mae) to mortgages which are not Federal Housing Administration (FHA) insured or Veterans Administration (VA) guaranteed -- so called "conventional" mortgages. Three billion dollars -- an amount sufficient to finance about 100,000 new homes -- would be available. The proposed program will be in addition to the over \$19 billion of Federal funds that have been made available over the past year for the purchase of mortgages to supplement the buying power of hard-pressed thrift Institutions.

GNMA currently aids in creating a supply of credit for mortgages on new homes insured by FHA or guaranteed by VA -- about 20% of the total mortgages -- at reasonable interest rates by

- assuring, through commitments in advance, purchase of mortgages at a pre-determined price.
- subsidizing market interest rates to lower levels in the event interest rates do not fall after commitments are made.
- guaranteeing, on a "full faith and credit basis," obligations secured by such mortgages.

Housing Industry Situation Critical. Over the past 22 months

- housing starts have dropped from 2.51 million units to 1.13 million units.
- unemployment in the construction industry is 12.4 percent and climbing, with almost a half million construction workers now unemployed.
- many homebuilders are in financial difficulty.

President Ford's Proposal for Interim Housing Aid

By making conventional mortgages on new homes eligible for purchase by GNMA, builders and homebuyers will be assisted where home mortgage credit is scarce or non-existent.

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1. Level of Commitments. Aggregate amount of commitments and mortgages which GNMA could hold at any time, i.e. have purchased and not resold, could not exceed \$7.75 billion. A program of \$3 billion of mortgage commitments, or enough to finance about 100,000 new homes, is contemplated. The precise amount would be determined on the basis of market conditions at the time the new authority becomes law, and additional programs would be activated as circumstances require.

2. Mortgage Amounts, Discounts, Interest Rates, and Downpayment Requirements. Subject to Congressional approval the program would provide for a maximum mortgage amount of \$45,000. The effective interest rate would be determined on the basis of market conditions at the time the program went into effect and would be somewhat above the rate offered on GNMA tandem programs for FHA/VA mortgages -- presently 8 3/4%. Twenty percent downpayments would be required with an exception for down to 5% downpayments if the additional mortgage amount is covered by a qualified private mortgage insurance contract so as to minimize cost of mortgagor defaults.

3. GNMA Disposition of Conventional Mortgages. Following the precedent of existing law, GNMA could, depending upon market or other factors, sell mortgages to the Federal National Mortgage Association (FNMA) or the Federal Home Loan Mortgage Corporation (FHLMC), sell mortgages or commitments with a provision for pooling by FNMA or FHLMC or other approved issuers and sale by such issuers of GNMA-guaranteed "pass through" securities or bond type securities on the market or to the Federal Financing Bank or sell guaranteed "pass through" securities to the Federal Financing Bank.

4. Cost and Budget Implications. Any subsidy would be paid out of corporate funds and ultimately from Treasury borrowing. Dollar amount of mortgages purchased would not be excluded from budget authority, but would appear as outlays in any fiscal year only to the extent they are not offset by sales that year. Assuming (i) all mortgages purchased in a given fiscal year were sold in that year, (ii) a face interest rate of 9 1/4%, (iii) no discount points on GNMA purchase and (iv) an average market rate at time of GNMA sale of 10%, the budget outlays per each billion dollars of mortgages would be about \$50 million.

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PUBLIC UTILITIES

The problems of our public utilities are extremely serious. More than anything, they are suffering from the effects of inflation -- in particular the explosion in oil prices but also from high interest rates. Their inability to raise all the capital they need is forcing them to reduce construction plans, which causes unemployment today and the real threat of brown-outs tomorrow.

The most fundamental part of the solution to these problems is for increases in the cost of electricity, reflecting high prices for fuel, to be paid by the consumers. This means higher rates, as painful as they are.

In the past, the utilities industry has developed rate structures that encourage excessive energy consumption. These promotional rates are often at lower levels than the cost of the energy provided, and thus give a perverse incentive at a time when conservation is our goal. Regulatory authorities should eliminate such rate schedules promptly.

While the Federal Government will not pre-empt the regulatory functions of the States, the States must meet their responsibilities fully.

In addition, the restructuring of the investment tax credit and its increase from 4 percent to 10 percent for the utilities (the same as for businesses generally) will assist these companies in overcoming their financial problems. The new proposal that dividends paid on qualified preferred stock also be allowed as a deduction to the paying corporation will also help the utilities improve their capital structure, and energy conservation measures, mandatory and voluntary, will hold down future financing requirements of utilities.

THRIFT INSTITUTIONS

Our savings institutions are another victim of the twin scourges of high inflation and high interest rates. To correct this situation, we must bring inflation down. However, we must also provide the means for the thrift industry to restructure itself -- to give these institutions the ability to compete on an equal basis in the financial markets and to operate effectively under all interest-rate conditions. To this end, we urge prompt passage of the Financial Institutions Act of 1973.

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The Act will reduce the structural differences between commercial banks and thrift institutions, primarily by permitting the thrift institutions to engage in additional deposit and credit activities. Passage of this Act would provide a broader range of financial services for consumers and a higher rate of return for savers. It would improve income and liquidity in the thrift institutions. The Act also contains provisions that will improve and support the mortgage market.

In addition, we support the proposals now under consideration in both the House and Senate to increase Federal insurance on private deposits. We recommend an increase from \$20,000 to \$50,000. Such an increase will reinforce public confidence in our financial system.

THE BUDGET

Control of the Federal Budget is a vital component of our anti-inflation efforts. Reducing the fiscal 1975 budget is the first step in reducing the powerful momentum of our rapidly climbing Federal budget and thereby gaining the spending control so necessary for 1976 and beyond. And this extended budget control will substantially reduce inflation over the longer term.

This should not suggest that budget control has no short-run benefits. Quite the contrary. A reduction in the deficit for fiscal 1975 would reduce pressures in the financial markets, lower interest rates and provide more credit for housing and other new capital investment. It would mean that monetary policy would not have to bear the full burden of economic policy restraint. And it would reduce inflationary expectations by demonstrating convincingly that the Federal government is putting its own financial house in order.

Our program for fiscal discipline has elements on both sides of the budget. On the revenue side we have proposed a tax surcharge on high-income taxpayers and corporations. The increased revenues from the surcharge will pay for the additional unemployment insurance, the Community Improvement Program, the increased and restructured investment tax credit and the revised tax status of preferred stock dividends.

On the expenditure side, the President has reaffirmed his intention to hold budget outlays for fiscal 1975 to below \$300 billion. Cutbacks of over \$5 billion will be needed to reach the goal. We are

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already in the fourth month of the fiscal year; thus reductions of the amount required will be difficult to obtain. There is need for rapid action, and the Congress and Executive together will need to work together quickly and effectively to put expenditures on a long-term track that is consistent with the productive capacity of the American economy and with what the American people are willing to pay for.

The President has asked the Congress to enact a bill setting a spending target for fiscal year 1975 of less than \$300 billion. In establishing that target, the bill outlines a plan for developing a set of actions that would result in the necessary spending reductions of FY 1975. These actions would be transmitted to Congress for its consideration when it returns in November. The actions to hold down spending will concentrate on those programs that serve special interests, create inequities, or are less essential at this time when fiscal discipline is so important. Concurrence of the Congress in these proposals before the beginning of calendar year 1975 is essential if the \$300 billion target is to be achieved.

The Administration together with the Congress have already begun to take action on this outlay control program in national defense activities. The Congress has passed, and the President has signed, a defense appropriation bill that will reduce defense outlays in FY 1975 by about \$2 billion. This is the largest single cut we will be making and is a good start toward the \$300 billion goal.

The remainder of the necessary outlay control plan will be carried out in the fullest spirit of cooperation with the Congress. Rapid consideration by the Congress of legislative proposals and budget rescissions and deferrals under the Congressional Budget and Impoundment Control Act of 1974 will be essential if we are to meet our goal. Only through the most careful consultation with the Congress can we succeed. We must achieve a mutual understanding of the best ways to hold down the budget.

We also have to improve the content of the budget. As now stated, the budget -- because it does not adequately show the impact of the Government's credit program -- does not present to the American people a complete picture of Federal activities and their effect on the economy. The Federally sponsored credit agencies and the many guarantee programs must be brought into the budget more directly.

The table below shows the estimated impact on budget expenditures and receipts of the proposals in this message.

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BUDGET IMPACT

	<u>FY 1975</u>	<u>FY 1976</u>
	(\$ billions)	
<u>New Proposals</u>		
<u>Additional Revenues:</u>		
Tax surcharge:		
Corporations	+0.6	+1.5
High-income individuals	+1.0	+1.6
<u>Revenue Losses:</u>		
Employment assistance*	-0.1	-1.3
Housing program	-0.1	-0.1
Investment tax credit:		
Individuals	-0.1	-0.5
Corporations	-0.7	-2.0
Preferred stock dividends	---	-0.1
Net Impact	<u>+0.6</u>	<u>-0.9</u>
<u>Pending Tax Reform Bill</u>		
Pending tax reform:		
Increased oil taxes	+1.3	+2.2
Closing loopholes**	+0.1	+0.8
Simplification	---	-0.4
Other tax reform	-1.0	-0.2
Low-income relief	-0.9	-1.6
-- recommended addition	---	-0.4
Net Impact	<u>-0.5</u>	<u>+0.4</u>
<u>Budget Impact of New and Pending Proposals</u>		
	+0.1	-0.5

Note: In addition to the above items, new expenditure deferrals and recissions will be proposed to hold fiscal 1975 expenditures below \$300 billion.

* For fiscal 1975, this assumes that a 6 percent unemployment rate triggers the program into effect on Mar. 1, 1975. Note, however, that the total expenditures for this program in fiscal 1975 will be \$0.9 billion; \$0.8 billion is already included in earlier budget estimates. For fiscal 1976, this assumes that the unemployment rate falls below 6 percent and thus triggers an end to payments as of December 31, 1975.
 **Minimum tax on income and limitation on accounting losses.

TAX PROPOSALS

Surcharge

1. Corporations

A 5 percent corporate tax surcharge will be imposed effective January 1, 1975, and continuing through December 1975. The surcharge will be computed by multiplying the corporate tax (before credits against tax, but including the additional tax for tax preferences) by 5 percent. For corporations with taxable years ending in 1975 or beginning in 1975 and ending after 1975, the surcharge will be computed on a pro rata basis according to the number of days of the taxable year in 1975.

2. Individuals

A 5 percent individual tax surcharge will also be imposed for 1975 on income tax liabilities attributable to income above an upper income threshold.

In general, the proposal is designed to exclude from surcharge families with adjusted gross incomes below \$15,000 and single persons with adjusted gross incomes below \$7,500. However, because income tax liabilities are based on "taxable income" rather than "adjusted gross income," it is necessary to translate, on some average basis, the \$15,000 and \$7,500 into comparable "taxable income" figures. That was done as follows:

	<u>Families</u>	<u>Single persons</u>
Adjusted gross income	\$15,000	\$7,500
Standard deduction	-2,000	-1,300
Exemptions (assuming 4 for families 1 for single person)	-3,000	- 750
	<u>\$10,000</u>	<u>\$5,450</u>

Thus, the surcharge will be expressed technically as a surcharge on tax liabilities attributable to that portion of the taxpayer's "taxable income" in excess of the \$10,000 or \$5,450, as the case may be. Not all taxpayers have the same deductions and exemptions as those assumed above. For

example, there will be married taxpayers with more exemptions and deductions than those assumed, who will pay no surcharge even though their adjusted gross incomes are somewhat greater than \$15,000. Conversely, some with fewer exemptions may pay surtax even though their adjusted gross incomes are somewhat less than \$15,000.

The computation is straightforward. The taxpayer (1) computes his regular tax, (2) subtracts from that the amount of tax applicable to either his \$10,000 or his \$5,450 exemption, and (3) then multiplies the balance by 5 percent. For example, a family of four filing a joint return and having \$20,000 of taxable income would calculate a regular tax of \$4,380 and subtract from that \$1,820 (the tax on the first \$10,000) to arrive at \$2,560 which is subject to the 5 percent surcharge of \$128. A single person with \$10,000 of taxable income would calculate a regular tax of \$2,090 and subtract from that \$994.50 (the tax on the first \$5,450) to arrive at \$1,095.50, which is subject to the 5 percent surcharge of \$54.78.

Investment Tax Credit

The proposal to change the investment tax credit has three principal parts: (1) the elimination of existing limitations and restrictions on the credit which tend to discriminate unfairly between the types of taxpayers and investments which qualify for the credit, (2) an increase in the rate of the present credit from 7 percent to 10 percent, and (3) making the credit a reduction in basis for depreciation purposes.

1. Present law

An amount equal to 7 percent of the cost of qualifying property (generally, tangible personal property used in a trade or business) may be offset directly against income tax liability, with the following limitations based on the expected useful life of the property:

<u>Useful Life</u>	<u>Percent of cost of property qualifying for credit</u>
0-3 years	0
3-5 years	33-1/3
5-7 years	66-2/3
7 years and over	100

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Public utility property qualifies for only a 4 percent credit (The Ways and Means Committee has tentatively decided to remove this limitation).

The maximum credit which may be claimed in a taxable year is limited to \$25,000 plus one-half of the excess of tax liability over \$25,000.

Excess credits (limited by the above provision) may generally be carried back three taxable years and forward seven taxable years, after which they expire if still unused.

2. Proposed changes

Increase the rate from 7 percent to 10 percent. This will increase cash flow for all companies in the immediate future. It will be offset in future years by lesser depreciation deductions.

Eliminate the limitations based on useful life so that all property with a life in excess of three years will qualify for the full credit.

Eliminate the discrimination against public utility property so that it will qualify for the full rate and otherwise be treated the same as other qualifying property.

Replace the present limit on the maximum credit which may be claimed with eventual full refundability for the excess of credits over tax liability. Credits in excess of the present limitations may be carried back three years and then to the succeeding three years to offset tax liability, after which time any remaining excess credits will be refunded directly to the taxpayers. This will

- Help growing companies which have present investments which are large in comparison with their current incomes.
- Help companies in financial difficulties, which get no benefit from credit because they have little or no income tax liability against which to apply it.

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-- Help small businesses, which under present law are more severely affected by the restrictions and limitations.

The three-year rule postpones adverse budget impact until revenues from basis adjustment are sufficient to offset revenue loss from this refundable feature.

Require the taxpayer to reduce the cost of qualifying property for depreciation purposes by the amount of the investment tax credit. This makes the credit neutral with respect to long-lived and short-lived assets and removes the present discrimination against long-lived assets.

Retain the present \$50,000 per year limitation on qualifying used property.

Deduction for Dividends Paid on Certain Preferred Stock

To encourage expansion of corporate equity capital and increase the effectiveness of capital markets, it is proposed that dividends paid on qualified preferred stock be allowed as a deduction to the payor corporation. The provisions of the Internal Revenue Code providing for exclusions for dividends received by corporations would not be applicable to these dividends.

The deduction would only be available for cash dividends paid on preferred stock issued after December 31, 1974, for cash or pre-existing bona fide debt of the issuing corporation. For these purposes, preferred stock would be required to be non-voting, limited and preferred as to dividends and entitled to a liquidating preference. The intention to qualify preferred stock under this new provision of the Internal Revenue Code would be required to be clearly indicated at the time the stock was issued.

The Tax Reform Bill

1. Low-income taxpayer relief

We support the Tax Reform bill now pending in the Ways and Means Committee. It provides about \$1.4 billion of tax

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relief for individuals with incomes of less than \$15,000. In addition, the Tax Reform bill would produce a long-term revenue gain of about \$500 to \$600 million per year beginning in FY 1976 and we support using those revenues when received also to provide further income tax reductions for lower income families.

The principal individual tax reductions provided in the bill are increases in the minimum standard deduction, the standard deduction and the retirement income credit and a new simplification deduction which for most taxpayers will be larger than the miscellaneous, hard-to-compute deductions which it would replace.

The tax reductions in the bill are made possible primarily by revenues gained from tax reform measures and by increased taxes on oil producers. The tax reform proposals are based on Treasury proposals advanced a year and a half ago. The two main features are: (1) a minimum tax, designed to ensure that all taxpayers pay some reasonable amount of tax on their economic income, and (2) a provision (known as "LAL, i.e., limitation on artificial accounting losses) designed to eliminate tax shelter devices under which tax is avoided through the deduction of artificial losses which are not real losses.

In December 1973, the Treasury proposed a windfall profits tax on oil, which is now incorporated in the Tax Reform bill in modified form. The Committee has also provided for the phase-out over three years of percentage depletion on oil and gas.

The Committee bill raises less revenue from tax reform and oil taxes for calendar years 1974 and 1975 than the Treasury proposed. The Treasury hopes that Congress will restore some of the reform which the Treasury proposed. However, it is most important that tax reform and tax reduction legislation be enacted as promptly as possible and the Administration will support the bill in its present form.

2. Savings and investment proposals

Greater productivity in the next several years will be critical in winding down the wage-price spiral. That will require major new investments.

The Tax Reform bill now pending makes an important contribution by (i) bringing the investment credit for utilities up to the credit generally applicable for other industries,

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(ii) liberalizing the treatment of capital gains and losses, and (iii) eliminating U.S. withholding tax on foreign portfolio investments, thus encouraging investment by foreigners in the United States.

Tax Exemption for Interest
on Savings Accounts

Various proposals have been made to exempt interest on savings accounts. We do not support any such proposal for reasons which include the following:

(1) It would initially decrease the aggregate amount of saving. A \$750 exemption for interest on time and savings deposits would cost about \$2 billion, which the government would have to borrow in the private market to make up. That borrowing reduces the amount of savings available for private investment.

(2) It would not be effective. It would not substantially increase savings deposits because the tax exemption would not be a major benefit to most taxpayers. For a taxpayer in the 25 percent bracket, exemption would make a 5.25 percent account equivalent to a 7 percent taxable account, which is still considerably below the rates available elsewhere. Only high-bracket taxpayers would get major benefits.

(3) Passbook savings may increase some, but total savings will not increase. The principal effect would be some switching. It doesn't operate as an incentive for new savings because it doesn't reward the increase in savings.

(4) It would create new distortions in the credit and investment markets.

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CITIZENS' ACTION COMMITTEE TO FIGHT INFLATION

The following Citizens have already agreed to help organize and support a voluntary private sector effort to mobilize all Americans in the fight against inflation:

MAYOR JOSEPH ALIOTO of San Francisco	Chairman, U. S. Conference of Mayors
ARCH BOOTH	President, Chamber of Commerce of the United States
RUSSELL W. FREEBURG	White House Coordinator
DAVID L. HALE	President, United States Jaycees
MRS. LILLIE HERNDON	President, National Congress of Parents and Teachers
ROBERT P. KEIM	President, The Advertising Council
MRS. CARROLL E. MILLER	President, General Federation of Women's Clubs
WILLIAM J. MEYER	President, Central Sprinkler Co. Landsdale, Pennsylvania
GEORGE MYERS	President, Consumer Federation of America
RALPH NADER	Private Citizen
LEO PERLIS	Director of Community Service, AFL-CIO
SYLVIA PORTER	National Syndicated Columnist
GOVERNOR CALVIN RAMPTON of Utah	Chairman, National Governors Conference
STANFORD SMITH	President, American Newspaper Publishers Association
FRANK STANTON	Chairman, American National Red Cross
ROGER FELLOWS	4-H, University of Minnesota

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VINCENT T. WASILEWSKI

President, National Association
of Broadcasters

ROY WILKINS

Executive Director, National
Association for the
Advancement of Colored People

DOUGLAS WOODRUFF

Executive Director, American
Association of Retired
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