Law Quadrangle Notes

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Gift

briefs

A Report On The U-M Law Alumni Reunion And Law Forum

By Professor Roy F. Proffitt

On May 29, 30, and 31, the Lawyers Club sponsored its first "U-M Law Alumni Reunion and Law Forum." It went well—very well—and the second U-M LARLF is on the drawing board.

Perhaps, for those of you who did not attend, we should tell you what you missed. Our goals were to provide an exciting and outstanding intellectual challenge, and, at the same time, have a pleasant and rewarding social occasion. We think we succeeded.

On Thursday afternoon and evening there was an informal open house in the main lounge of the Lawyers Club where those who arrived early could register, visit with others who were there, enjoy some refreshments (as a courtesy of the Michigan Alumni Association), and make their plans for dinner or for the next day. Seminars were scheduled for both Friday and Saturday, and a luncheon was held for everyone on each day, as well.

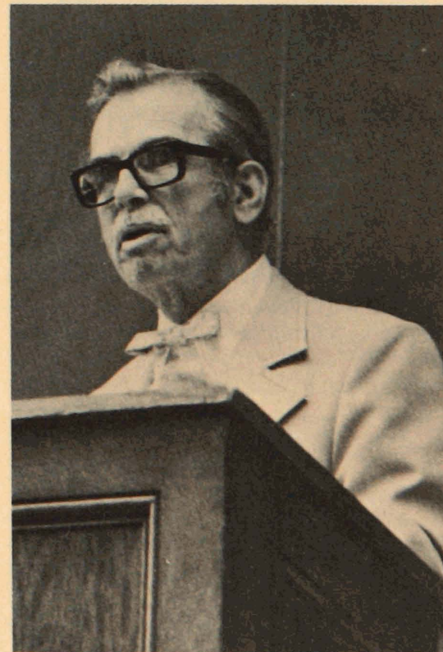
Past . . . and Prologue.
U-M LARLF—you cannot pronounce it, but you can learn to love it.

Although these seminars certainly dealt with law and lawyers, they were not the usual ICLE "how-to-do-it" sessions. The participants spoke on subjects of current interest and dealt with some of the major policy issues confronting lawmakers, lawyers, judges, and the public in the application of those laws in our daily lives. Many of the non-lawyer spouses who accompanied the lawyer member of their families attended and enjoyed these sessions, too. In each seminar, there was an opportunity for audience participation.

[Professor L. Hart Wright's predictions about some "Coming

Robben W. Fleming, former U-M president and law professor, was U-M LARLF luncheon speaker.

Seminar audience at the U-M Law Alumni Reunion and Law Forum.



Professor L. Hart Wright predicting changes in our federal tax system.

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Crowd at reunion luncheon.

Seminar leaders Professors Rosemary Sarri and Francis Allen.

Judge Avern Cohn chats with Ina Sandalow, wife of Dean Terrance Sandalow.

Revolutionary Changes in Our Federal Tax System" are reproduced elsewhere in this issue.]

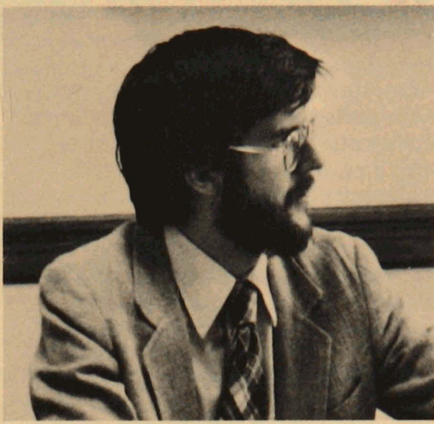
In a seminar entitled "Divorce: When Parents Fight Over Custody and Child Support" Professor David Chambers and a dozen alumni and alumni spouses shared ideas about the appropriate resolution of child custody disputes. The group discussed an actual case involving a dispute over an eight-year-old daughter between an ambitious working mother who had recently remarried and a father who had returned to living with his parents. The intensely differing and lively reactions to this case by the dozen people sitting around the table (a group that included three judges) led to a discussion whether, in most child custody disputes today, there is any way for judges to make sensible choices between competing parents and whether they would do just as well flipping coins.

The principal theme of the panel conducting the seminar entitled "Rehabilitating Rehabilitation: Modern Problems of Penal Policy" related to the recent significant changes in thought about the administration of criminal justice, especially in the decline of the notion of rehabilitation and the rise of competing theories such as "just desserts." Professor Francis Allen's discussion of these ideas was supplemented by a description of the dilemmas and frustrations associated with the exercise of sentencing powers in criminal cases by Judge Avern Cohn (U.S. District Court, Eastern District of Michigan) and a consideration by Professor Rosemary Sarri (U-M School of Social Work) of the large discrepancies in theory and practice revealed by the criminal justice system.

Professor John Jackson spoke on "Problems of International Trade Policy and the United States Law." Setting United States law relating to imports and exports in the context of the U.S. Constitution, with its perennial struggle for power between the branches of government (the Presidency and the Congress), he noted that U.S. law had a great influence on the formation of the international institutions relating to international trade, particularly the GATT (General Agreement on Tariffs and Trade). Likewise, such institutions have had considerable influence on U.S. law. After the failure of an international trade organization to materialize in 1946-48, the GATT was forced to fill the gap and become the principal international organization governing trade. Since that time, there have been a number of major trade negotiating rounds, culminating in the most recent "Tokyo Round," often called the "MTN" (Multilateral Trade Negotiation). The trade negotiation was mostly completed in 1979, and was implemented by United States legislation known as the "Trade Agreements Act of 1979." Professor Jackson outlined the various techniques under United States law (in relation to international law and treaties under the GATT) for regulating trade, particularly imports. In this connection he discussed briefly problems of tariffs, quotas, anti-dumping duties, countervailing duties, orderly marketing agreements, etc. He also discussed some of the major trade policy instruments of the United States government, including the escape clause and the "Section 301" procedure for retaliation against foreign government activities deemed to be unfair.

The final seminar on Saturday morning featured a three-person panel dealing with the changing obligations of a lawyer under the proposed rules of professional conduct. The panelists were Professor Richard Lempert; Judge Horace Gilmore of Detroit, then a Wayne County Circuit Judge and now a U.S. judge for the Eastern District of Michigan; and John C. Elam of Columbus, Ohio, President of the American College of Trial Lawyers. The discussion involved a searching commentary on and criticism of the ABA's draft of "Model Rules of Professional Conduct." Judge Gilmore, who has taught a popular course on professional responsibility in the Law School for several years, pointed to a number of inconsistencies in or difficulties with the proposed rules, and was particularly troubled by places where they did not, in his opinion, go far enough. John Elam, focusing on different sections, issued a scathing denunciation of what he considers serious infringements of the lawyer-client relationship. Professor Lempert, who observed several working sessions of the so-called "Kutak Commission," gave the audience some insight into the considerations that led to certain controversial provisions of the proposed rules. As might be expected, audience participation during this seminar was wide-ranging and substantial, not to say emotional.

As exciting and challenging as these seminars were, the pièce de resistance for many was the Reunion Luncheon on Friday noon, and the talk that followed. Former U-M President Robben Fleming spoke on "Public Policy Problems in Public Broadcasting." He was able, of course, to draw on situations he has experienced in his present position as president of the Corporation for Public Broadcasting in Washington, D.C. One subject of great interest was


Seminar on parental custody was conducted by Professor David L. Chambers.

International trade is the specialty of Professor John Jackson.

Forum speakers from left, John C. Elam, Professor Richard Lempert, Judge Horace Gilmore.

the then recent decision to permit the showing of the controversial TV documentary "Death of a Princess."

The reunion closed with a buffet luncheon on Saturday.

Although this may read like a busy schedule, there was plenty of free time for those who attended to be with friends, play some golf and tennis, take a walk through the Arb, shop a bit, visit some of the University museums, etc. Two Law School classes—'35 Law and '40 Law—used the free time for class reunion activities.

Some of these opinions are, of course, my own, but they were voiced by many who were the charter members of LARLF. Since this was our first experience with this type of program we asked each person for his or her comments. No one had any serious complaints, and we did receive some constructive suggestions that planning committees can consider in subsequent U-M LARLF's. A brief sampling of these comments include:

. . . The law forum sessions which I attended were extremely good and, personally, I appreciated the relatively intimate atmosphere in which they were conducted . . . I would like to attend the second annual [LARLF] next year, and I have already encouraged others to seriously consider attendance . . .

. . . I perhaps most enjoyed the luncheon presentation by Dr. Fleming. It was the first time I had had the chance to hear him, and he certainly has an insight to humor and a class to what he says . . . I think it might be well to have a panel on the broad social impact of law and what our legal system can do with the social problems we have . . .

. . . It is difficult to select a program that will appeal to all, but I feel the one in 1980 was more oriented to big firm practice and corporate practice. Perhaps something of interest to others would spark more attendance . . .

. . . Your choice of subject matters and speakers was especially attractive to me. The time was well spent. The opportunity to socialize before and during the Friday luncheon is appreciated and was enjoyed . . .

It was a great day for me. Many Thanks.

. . . I hope that more classes will hold their reunions concurrently with this event . . . I would suggest, however, that an evening dinner and some sort of entertainment be planned for those who are not having a class reunion . . .

. . . You ought to have the meeting in the fall, coincident with a football game . . .

. . . We believe the general time of year for holding the Alumni Reunion and Law Forum was just right . . . Specifically I would urge you to avoid tying in such a general "Homecoming" with an athletic event . . .

So it goes, and there were many more. We hope that if you were not here in 1980, you will come in 1981 to discover for yourself why so many had such a pleasant and rewarding experience.

And what are the plans for 1981? The second annual U-M Law Alumni Reunion and Law Forum is scheduled for **May 21-23, 1981.**

We hope you will mark those dates on your calendar now. Although we cannot tell you today the precise program, your committee is hard at work planning the details. The format and content for number two will be similar, but not identical, to number one.

A few comments about the timing. We are aware that in recent years a substantial number of individual class reunions have been in the fall so that those who attend can see a Michigan football game. But for what we have in mind, spring seems better. The pressure on hotels and motels in the fall, particularly football weekends in Ann Arbor, is horrendous, and getting adequate space reserved each year would be most difficult. This pressure applies to banquet space and party space as well as rooms. Reserving a suitable block of football tickets is also a real problem. The converse of these problems makes a spring meeting a more realistic and attractive prospect. In addition Ann Arbor is a beautiful place in the springtime, and those who wish will have the opportunity to play golf, tennis, picnic in the countryside, etc.

Our date selection process has to deal with several additional factors. Since we make use of several classrooms in the Law School for our meetings we have to wait until classes and final examinations have ended and "senior day" is past. Moreover, we have to take into account the annual Advocacy Institute and the spring meeting of the Presidents Club because both attract a number of Law School alumni and put pressure on the hotel room situation. Finally, of course, Ann Arbor is a popular location for many other groups and meetings, and we have to find a weekend when space is not being sought by many others.

May 21-23, 1981, should work well. It is, as you may recognize, the Memorial Day weekend, which means that Monday, May 25, will be a national holiday. Thus, those who attend will have an extra day to get home, to have a family gathering, or just to rest up before going back to the office on Tuesday.

At the time of this writing it appears that four Law School classes whose graduation year ends with "1" or "6" will have their individual class reunions in conjunction with the second U-M LARLF. The class of 1941 has made definite plans to do so, and 1931, 1956, and 1966 are giving these dates "serious consideration." We have yet to hear from some of the other "1" and "6" class leaders. We hope they, too, will find U-M LARLF an ideal occasion to plan a mini-reunion.

Alumni Association Covers All Europe

U-M Law School alumni in Europe have formed an all-European alumni organization.

"The University of Michigan Law School Association of Europe" was established during an all-European alumni meeting Sept. 20-21 at the seaside resort Sofitel La Réserve at Knokke, Belgium. While European law alumni of various nations have gathered in the past, this was the first meeting of alumni from throughout Europe.

Giorgio V. Bernini (LLM 1954, SJD 1959) of Bologna, Italy, was elected president of the new group. Jean-Michel Detry (MCL 1976) of Brussels, Belgium, is the secretary; and Walter Konig (MCL 1969) of Zurich, Switzerland, is treasurer.

Other members of the association's board of governors: Jurgen O. A. Gliss (MCL 1962) of Germany; John K. Toulmin (LLM 1965) of England; Jean Marie Pascal Gilbert (1952-53) of France; Frans D. Fischer (MCL 1977) of the Netherlands; and Thierry Renard (MCL 1978) of Belgium.

"While the Law School has given encouragement for this type of activity, the all-Europe alumni association was initiated and organized by the European alumni themselves," said U-M law Prof. John H. Jackson, who will serve as the Law School's liaison with the new group in his capacity as chairman of the Law School's new Committee on International and Comparative Legal Programs.

People from the Law School who attended the meeting at Knokke, at the invitation of the European alumni, were Profs. Jackson and Joseph Vining, and Dean Terrance Sandalow.

Highlights of the meeting included a discussion of the implications for the U.S. and Europe of the Tokyo round of international trade negotiations. The featured speakers were Claus-Dieter Ehlermann (U-M Law School 1955-56), head of the legal service of the European Economic Community Commission; Jacques Bourgeois, U-M law 1959-60), a member of Ehlermann's staff; and Prof. Jackson, a specialist in international trade law.

Attending were some 50 alumni from Belgium, France, Germany, Italy, the Netherlands, Switzerland, United Kingdom, and other countries. The meeting was organized by Jean-Michel Detry and Thierry Renard, both of Brussels.

The newly combined European alumni association and a similar Japanese group are the two largest overseas U-M law alumni organizations. Last May, law Profs. Whitmore Gray, John Jackson, Jerold H. Israel, and former U-M law faculty member B. J. George met with the Japanese group in Tokyo. The Japanese alumni organized a reception for the U-M law faculty members, who were each in Tokyo for separate research or business reasons.

Of U-M law graduates, more than 900 presently live in 72 foreign countries. The figure increases to 1,100 when one includes former U-M research scholars and visiting professors who now live abroad. Highest representation is in West Germany with some 140 U-M affiliated persons, followed by Japan with 135.

MEPA Documents Are Placed In Bentley Library

A comprehensive collection of legislative history and documentation on the enactment of the Michigan Environmental Protection Act of 1970 (MEPA) has been assembled for public use at the Michigan Historical Collections, Bentley Historical Library at the U-M.

MEPA was originally drafted by Prof. Joseph L. Sax of the U-M Law School. It was also one of the first projects undertaken by the Environmental Law Society, a student organization now in its 10th year at the Law School.

Assembling and cataloguing the MEPA materials were carried out by Joseph DiMento, a 1974 U-M law graduate who now teaches urban planning at University of California, Irvine. DiMento worked on the project while serving as a visiting professor of urban planning at U-M last year; he was assisted in the project by U-M law student Don Patterson. The project was funded by a grant from the University and partially subsidized by the Law School Fund.

"There now exists at the Bentley Library on the North Campus a single source of primary information about the statute," said DiMento. "Materials in the collection trace the history of the act from the first correspondence between the West Michigan Environmental Action Council and Prof. Sax requesting that he draft a model law for them, through passage of the law by the Michigan legislature and its signing by Gov. William Milliken on July 27, 1970.

"The collection also contains post-enactment materials—including attempts to amend the bill—covering a period through April, 1976. Plans are under way to add to the collection all relevant legislative materials relating to the law, its interpretation and amendment."

Among materials which are found in the collection are: correspondence concerning MEPA from the files of Prof. Sax, state Rep. Thomas Anderson of Southgate (who sponsored the bill), Mrs. Joan Wolfe of Grand Rapids (who was director of the West Michigan Environmental Action Council), and other persons who were instrumental in passage of the act; all the various versions and drafts of the bill; analyses of the bill by the governor's office and state agencies; testimony delivered at public hearings on the bill; extensive newspaper coverage of the movement of the bill through the legislature; and popular and scholarly commentary on the bill and its impact. Also in the collection is the tape of the state Senate debate on the bill.

The materials include those collected by Prof. Sax during the past 10 years, contributions by Mrs. Wolfe (who is currently a member of the state Natural Resources Commission), and relevant material from the Michigan State Archives. Materials have also been requested of the governor and attorney general who played important parts in the passage of the Michigan act, according to Sax and DiMento.

The project involved assembling these materials, cataloguing them in ways they would be useful to historians, attorneys and legal scholars, and briefly describing the history of the act and the primary materials that are in the collection.

"The project was motivated in part by requests made of Prof. Sax and others by lawyers, historians, and legislators in the United States and abroad about the background of the Michigan act. Prof. Sax feared that the documents that he had collected, many of which are unique and irreplaceable, might begin to be scattered or deteriorate," according to DiMento.

"Students of the environmental movement will find a rich source of information on the early activities of the movement in Michigan and the philosophies behind various approaches to environmental control," said Sax and DiMento.

"Lawyers interested in the legislative history of the MEPA will find an extensive collection of documents tracing the bill's movement through a number of committees and through the House and Senate. Arguments about many of the issues which continue to be raised in MEPA litigation are presented in full detail in several of the policy analyses, bill analyses, and summaries of testimony found in these files. Students of government

and political science may also find the documentation useful in studies of interest group politics and the legislative process."

Dollar Signs Direct Career Traffic

Economic pressures could rob law schools of some of their top faculty prospects, as more young graduates turn to higher paying jobs as practicing lawyers, warns a U-M law professor.

"A remarkable number of the brightest and ablest young people in

Theodore J. St. Antoine

the country are still headed for law school to become lawyers, but all too few of them are now staying around or returning to become teachers," says Prof. Theodore J. St. Antoine, who served as U-M law dean from 1971 to 1978.

While salaries for lawyers and law faculty members in the early stages of their careers were roughly comparable 15 years ago, today there is a growing pay differential, St. Antoine said.

Law graduates who choose to teach rather than enter legal practice "will probably have had to take a $10-20,000 annual pay cut for the privilege of mounting the podium," said St. Antoine.

He discussed economic problems facing legal education at the American Bar Association's annual meeting in Hawaii this summer.

Pointing to a successful capital campaign at U-M Law School, where contributions from alumni and other private sources are financing a new library addition, endowed professorships, and other school needs, St. Antoine said law schools will likely be "forced back upon ourselves" to raise money in difficult economic times.

While tuition increases are another potential source of revenue, St. Antoine warned of the social consequences of placing too heavy a financial burden on students.

"Every increase in tuition decreases the likelihood that tomorrow's law schools will be populated by minorities and other disadvantaged groups," he said.

"Thus, any school contemplating tuition increases as the means of ameliorating its financial problems must also ponder both the depth of its commitment to minority advancement and the depth of its financial aid resources available to meet that commitment."

St. Antoine said difficulties attracting top faculty are most likely to be seen in such areas as corporate and commercial law, tax and antitrust, and estate and business planning, where there are strong economic incentives for young lawyers to enter corporate and private law practice.

In 1980, said St. Antoine, "our top graduates are starting on Wall Street or the equivalent of $35,000 a year, and in another three years or so they will be making $50,000 in current dollars." By contrast, "the new assistant professor who bids the seniors farewell will be lucky to be getting $30,000 a year.

"If we continue down our present path, we shall wind up with a very different sort of law faculty from the potent mix of high-caliber theoretician and practitioner that we have known and prized."

Another "hard choice" to save money may be to have fewer teachers handling more students, St. Antoine noted. "If a choice must be made, however, I would prefer to have one truly outstanding teacher holding forth before 100-150 students rather than two mediocrities evoking yawns among separate groups of 50 or 75 each."

U-M Project Focuses On Child Abuse Cases

Victims of child abuse often face difficult times even after being removed from abusive families, says a University of Michigan group that is helping Michigan communities and agencies become better equipped to handle legal and other problems in such cases.

In addition to the "trauma" of foster home placement, abused and neglected children—as well as their natural families—must cope with a tangle of social and legal agencies whose actions often appear to lack clear purpose and direction, say lawyer Donald Duquette and social worker Kathleen Coulborn Faller of the U-M's Interdisciplinary Project on Child Abuse and Neglect (IPCAN). The project involves students and faculty from the U-M law, social work and medical schools.

The traditional way of handling of child abuse cases by available community agencies—including schools, police, substance abuse and mental health centers, juvenile courts, and hospitals—may create "duplication or gaps in service, and sometimes a situation where different agencies work in opposition to one another," says Faller.

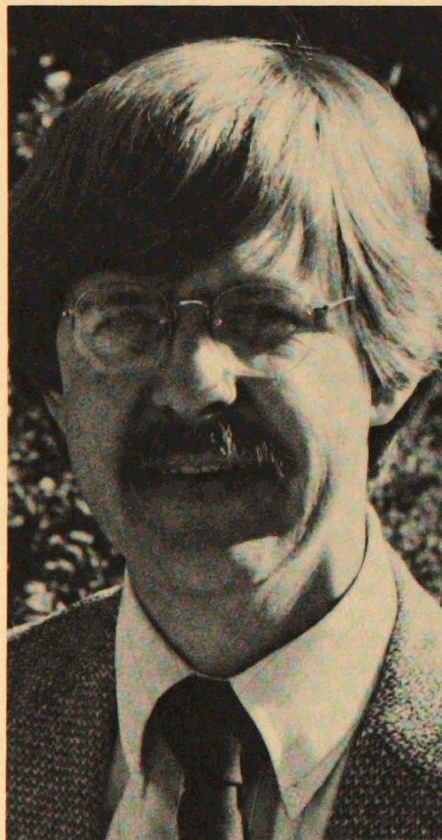
"Usually there is no feedback to the initial referral agency, and very little communication among different professionals working on a case."

To help achieve greater coordination in these cases, the U-M child abuse specialists have trained "multidisciplinary teams" of professionals—including physicians, lawyers, social workers, police officers, nurses, and judges—from 10 Michigan communities over the past year. Some 97 professionals have been trained at the U-M, and "these 97 will in turn train about 1,000 professionals in the 10 communities," say IPCAN staff.

"Michigan's Child Protection Law of 1975 requires the state Department of Social Services to establish multidisciplinary teams throughout the state and to train agency and court personnel. The community teams trained by the U-M's interdisciplinary project will help organize and coordinate services for children in each county, assist the Department of Social Services on specific cases of child abuse and neglect, and provide training to other community professionals," according to Faller and Duquette.

In Michigan, more than 32,000 child abuse cases—including actual physical harm, sexual maltreatment, emotional abuse or neglect, and educational and medical neglect—are

Kathleen Coulborn Faller


Donald Duquette

handled by Child Protective Services each year, "but these cases represent only the tip of an iceberg when one considers the many unreported cases," according to Duquette.

One national study estimated that some 14 percent of all children aged 3 to 17 are abused each year, including some 6.5 million reported cases, says Duquette, noting that the figures are increasing each year.

Citing some of the difficulties of dealing with child abuse cases without interagency cooperation, Duquette and Faller note the "job burnout" rate of Child Protective Services caseworkers is high because of the stresses of the job.

Without the availability of advice from professional social workers, lawyers, and physicians, the caseworkers are more likely to "intervene" by removing the child from his natural home rather than seeking resolution to the problems within the existing family unit, according to the U-M specialists.

"But such a move should not be made hastily," warns Faller. "The decision to place a child in a foster care facility will mean a traumatic adjustment for the child, with lifelong repercussions."

In some cities, removal of the child from his natural home is often followed by cumbersome legal procedures and court adjournments which cause some parents to give up their quest to have their child returned, says Duquette.

At Wayne County Juvenile Court—where the interdisciplinary U-M team has been attempting to apply their expertise in child abuse cases—previous court decisions have leaned heavily in favor of removing the child from the natural home, according to Duquette. Such removal is ordered in some 50 percent of suspected child abuse cases in Wayne County, compared to a national average of 10 percent, he says.

As part of the U-M training programs, Faller, Duquette, and Leslie Hoover, a nursing instructor from the Department of Pediatrics and Human Development at Michigan State University, made initial visits to selected areas of the state to determine community needs in child abuse cases.

Counties included in the training projects were Marquette, Ogemaw, Monroe, Genesee, Oakland, Kalamazoo, Ottawa, Muskegon, Jackson, and the Traverse area cluster of Grand Traverse, Benzie, Antrim, Kalkaska, and Leelanau counties.

The U-M program, including training in specific disciplines as well as instruction in interdisciplinary management of child abuse cases, strives for cost efficiency: "The IPCAN multi-disciplinary team training encourages a model of community organization which does not rely on a large infusion of new dollars to improve services. Instead, various public and private organizations—hospitals, social and public health agencies, and the Department of Social Services—contribute staff time and other resources for multi-disciplinary team activity," according to Duquette and Faller.

One major obstacle to an interdisciplinary approach in child abuse cases has been confidentiality requirements of professionals. But Duquette stresses that under the state's 1975 Child Protection Law, such confidentiality is waived for treatment personnel dealing with child abuse cases.

Generally, says Duquette, consultation among different professionals is permitted in suspected child abuse cases "for purposes of providing service to a child or family and if each professional is bound by the same requirements of confidentiality."

The U-M training projects, financed by Title XX training funds from the U.S. Department of Health, Education and Welfare, and administered by the State Department of Social Services, are free to participating communities. The University's interdisciplinary program in child abuse and neglect was initiated in 1976 with a grant from the Harry A. and Margaret D. Towsley Foundation of Ann Arbor. It provides training for U-M students from the School of Social Work, Medical School, and Law School, and also includes a clinical law program in which law students represent clients in child abuse cases.

In conjunction with the program to train community professionals, the U-M has developed written materials for lawyers, physicians, nurses, social workers, and mental health professionals. Films, videotapes, and slides were also made available to the trainees.

Further information on the program is available from: The University of Michigan Interdisciplinary Program on Child Abuse and Neglect, Social Work Center Building, 1015 E. Huron, Ann Arbor, MI 48109.

Among other aspects of the program:

—U-M training faculty members are providing multi-disciplinary team services to the Protective Services staff at the Taylor office of the Wayne County Department of Social Services, as part of a "demonstration" project. U-M social work graduate students also receive training as part of this program.

—Faculty from the U-M's IPCAN have provided consultation in the development and implementation of

Michigan's Child Protection Law.

—During 1978 some 400 Child Protective Service workers received legal training from U-M faculty members, and in 1979 some 300 Department of Social Services foster care workers and some private agency workers received training in legal aspects of foster care and adoption.

—Law students in the Child Advocacy Law Clinic have been serving as attorneys for the child protection agencies in Wayne and Washtenaw counties, while they have represented the children and parents in Genesee and Jackson counties. Similar clinical programs are in operation for social work and medical students at U-M.

—At U-M Hospital, members of IPCAN staff serve on the hospital's Child Protection Team. Doctors, social workers, nursing staff, psychologists, and psychiatrists assist in evaluating and coordinating suspected cases of child abuse and neglect.

—Because of IPCAN's role in child advocacy, Duquette, who serves as director of the U-M Law School's Child Advocacy Law Clinic, had filed suit in the Michigan Supreme Court, on behalf of a large number of child advocates in the state, alleging "serious deficiencies" in the Wayne County Juvenile Court.

The major complaint in the suit was that legal paperwork involving 64 children had never been forwarded to the Department of Social Services for adoption proceedings to begin. Duquette also claimed that frequent court adjournments, failure of the court to make written recommendations in cases, and the court's failure to provide legal counsel for Protective Services staff often worked against the best interests of children in abuse cases.

Duquette's charges sparked an investigation of the Wayne court by the state Supreme Court Administrator's Office. In a September 1979 report, the court administrator found the initial allegations substantially correct. In addition, the report listed a total of 140 children (not 64, as originally claimed by the plaintiffs) who had been made permanent wards of court and whose files were not transferred for adoptive placement.

Grand Jury Reform Suggested By Scholar

In a criminal trial in this country, the guilt of a defendant must be proved "beyond a reasonable doubt."

In actual practice—because the modern jury trial is so expensive and time-consuming—pressure is placed on most criminal defendants to plead guilty prior to trial, in return for concessions from the state.

Today, this system of "plea-bargaining" has replaced the jury trial "as our primary method of determining legal guilt" in criminal cases, a study in a U-M Law School publication points out.

But the system poses serious risks to the rights of defendants, says author Peter Arenella, because the "presumption of innocence" of the jury trial is replaced with the "presumption of guilt" at the pre-trial stages.

Arenella, a professor at Rutgers Law School, examines the problem in a *Michigan Law Review* article titled "Reforming the Federal Grand Jury and the State Preliminary Hearing To Prevent Conviction Without Adjudication."

He suggests that the suspect's rights can be fully protected only through "a fundamental reassessment of our pre-trial screening processes," including the preliminary hearing and the grand jury. At both these pre-trial screenings, the prosecutor supposedly screens out cases in which there is insufficient evidence to prove guilt at trial.

But Arenella argues that, in actuality, "several circumstances—the seriousness of the crime, the reputation of the accused, and the possibility of conviction through plea bargaining—may lead the prosecutor to indict a defendant when the government's proof of legal guilt is marginal at best.

"Since the pre-trial process does not require the government to present compelling evidence of factual guilt to an independent fact-finder or demonstrate that its evidence could satisfy the trial's formal proof requirements, prosecutors can and sometimes do get indictments despite insufficient evidence to support a conviction."

One key to possible reform, suggests Arenella, would be to check the prosecutor's charging discretion and strengthen the grand jury's ability to make a preliminary determination of guilt.

Congress should require the prosecutor "to present the indicting grand jury with a prima facie case of legal guilt. Furthermore, to ensure that the prosecutor has presented the grand jury with sufficient legally admissible evidence to warrant a conviction, the trial court should have the authority to dismiss any indictment where the indicting grand jury's transcript reveals that the prosecutor has not met that burden," writes the professor.

By contrast, under present pre-trial practices, the public's participation in determining guilt is "limited to a grand jury that is dominated by the prosecutor," says Arenella.

"While the state is supposed to develop its case against the accused independently, the prosecutor need only make a minimal showing of probable cause before using the state's panoply of permissible pressures to induce the defendant to admit guilt 'voluntarily' and plead guilty."

The grand jury's present tendency to "rubber-stamp" the prosecutor's decisions stems largely from the "limited role the Supreme Court has assigned to it and the type of evidence it receives," argues the professor.

"An inexperienced and untrained body of citizens cannot possibly screen out unwarranted prosecutions in an ex parte proceeding where they hear only the government's side of the case and depend on the prosecutor for all legal advice and direction."

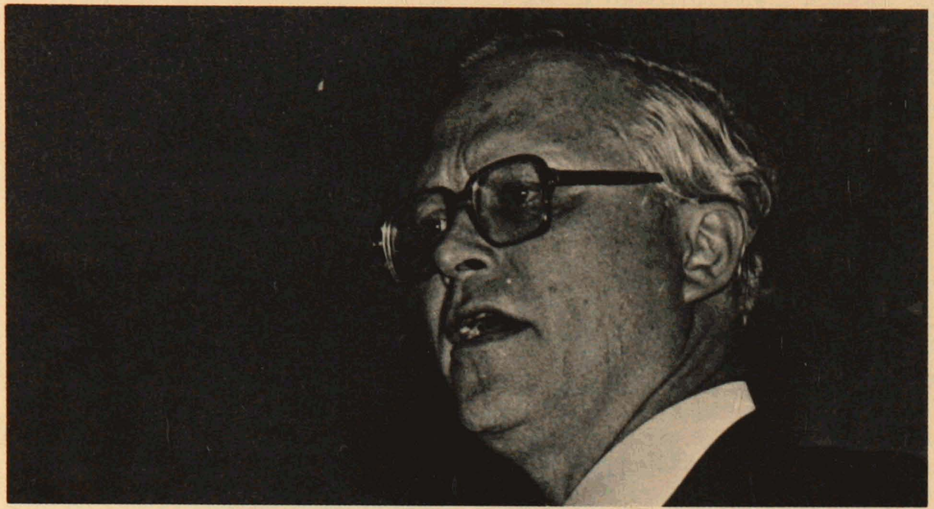
Among other reforms suggested in the article:

—The government should be required to develop independent evidence of a defendant's "factual guilt" before it encourages the defendant to plead.

—A "neutral adjudicator" should evaluate the government's evidence to determine if it can satisfy the trial's formal proof requirements.

—Whenever possible, the community should be given the opportunity to participate in this preliminary adjudication of legal guilt, "so that the disposition of society's most serious sanction is not left exclusively in the hands of professionals."

—The defense attorney should have sufficient access to the prosecution's case to make an informed prediction about the likely outcome at trial before advising the client to plead.



Benjamin R. Civiletti

events

Law School "Senior Day"

U.S. Attorney **Benjamin R. Civiletti,** addressing graduating U-M law students in May, said the Justice Department will begin prosecuting individuals in cases where industrial hazardous wastes threaten the environment and the public.

Civiletti outlined a program of increased "civil and criminal" enforcement of environmental laws in a speech at the Law School's "Senior Day" ceremonies in Ann Arbor.

He said the most likely target of such prosecution will be individuals who falsify reports in corporate waste-monitoring programs.

As part of the more rigid enforcement program, Civiletti said:

—Litigation will not be limited to those who own or operate waste dumpsites. "Those who generated toxic wastes and those who transported the wastes to a dumpsite will also be held responsible where appropriate."

—Rather than waiting for actual harm to occur, the Justice Department will take action "whenever it is determined that harm is likely to occur in the absence of remedial action."

—Polluters "can expect to see the development of a system of environmental audits to check the maintenance and operation of equipment."

—Compliance with environmental laws will be interpreted to mean the provision of adequate budgets to meet the expense of pollution control.

Civiletti said corporate officers will be held personally responsible for violations of environmental laws.

"It is self-evident that the work of corporations is carried out by individuals," Civiletti told graduating students. "Congress has specifically recognized this by including in the criminal provisions of the pollution control laws a definition of the term 'person' that includes 'responsible corporate officers.

"Thus, we shall attempt to identify the corporate officers responsible for corporate acts so that the law may be truly enforced and its real deterrent effect mobilized."

Civiletti noted that the government "has neither the desire nor the resources to review and police every industrial operation in the country. To ensure the integrity of self-reporting, our enforcement program will put special emphasis on prosecuting those who falsify their reports."

Civiletti said two new environmental enforcement units have been established in the Justice Department—a Hazardous Wastes Section, created October, 1979, under provisions of the Resources Conservation and Recovery Act, and a second section established February, 1980, to enforce air and water pollution laws.

This marks the first time in history, said the attorney general, that "special units will exist within the Department of Justice dedicated to the enforcement of the pollution control laws with the same seriousness that we give to enforcement of the tax laws or the laws against bank robbers."

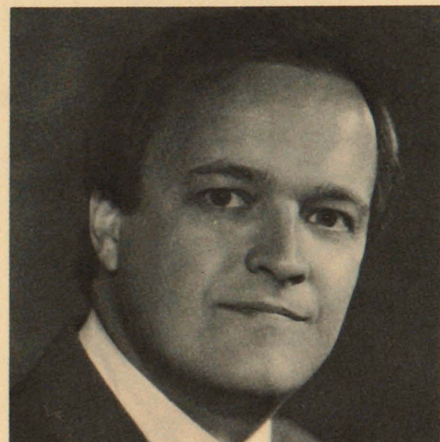
Civiletti said that at the present time, enforcement in the hazardous waste area will focus on section 7003 of the 1976 Resources Conservation and Recovery Act, which "gives the government a right to make the corporation that created the hazard take whatever action is necessary to eliminate it."

The Law School ceremony honored 321 graduating U-M law students, including 286 receiving the Juris Doctor degree, 9 the Master of Comparative Law, and 24 the Master of Laws.

alumni notes

Michael J. Davis

Peter Hay



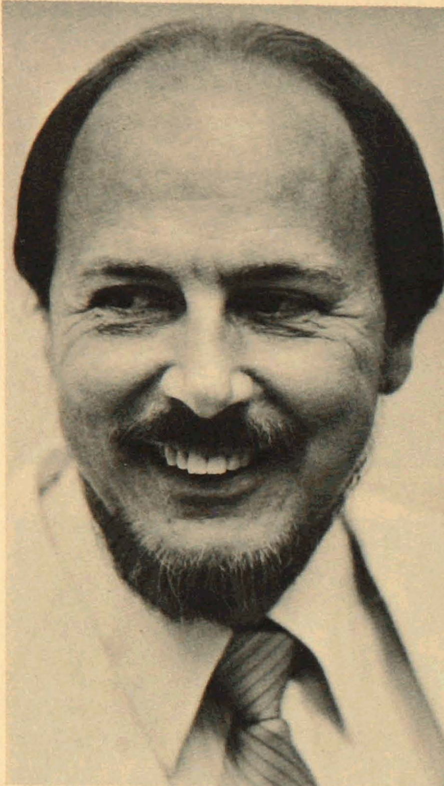
J. Kirkland Grant

☐ Over the years, many Michigan Law School alumni have served as law school deans at various institutions. During the 1980-81 academic year alone, five U-M law alumni have joined that elite group.

Michael J. Davis, 1967 *cum laude* graduate of the Law School, is the new dean of the University of Kansas School of Law. A member of the Kansas law faculty since 1971, Davis also served as the University of Kansas general counsel for the past six years while holding a concurrent faculty post. Among other previous posts he served with the legal services program of the Office of Economic Opportunity in Washington, D.C., was the Reginald Heber Smith Fellow at the Kansas City, Mo., Legal Aid and Defender Society, and was an associate of the Washington, D.C. law firm of Arent, Fox, Kintner, Plotkin and Kahn. He is a 1964 *magna cum laude* graduate of Kansas State University. At U-M he was assistant editor of the *Michigan Law Review.*

Peter Hay, member of the Law School class of 1958, is the new dean of the College of Law, University of Illinois at Urbana-Champaign. Hay had been acting law dean at Illinois for the past year and associate dean since 1974. He joined the Illinois law faculty in 1963, after teaching law at University of Pittsburgh and the U-M. A German native and a naturalized U.S. citizen, Hay is a specialist in Common Market Law, conflicts of laws, contracts, and international trade and investment. He is the author of many books in the international trade field, including three works co-authored with Prof. Eric Stein of the U-M Law School. Among other activities, Hay has served as the U.S. expert to the Hague Conference on Private International Law, as consultant to the U.S. Department of State, and as board member of the American Association for the Comparative Study of Law, the *American Journal of Comparative Law,* and the Cahiers de Droit European. As a student, Hay was on the editorial board of the *Michigan Law Review;* he also received an undergraduate degree from U-M.

Serving as dean of the Delaware Law School of Widener University, Wilmington, Del., is **J. Kirkland Grant,** 1967 *cum laude* graduate of U-M Law School. Grant was named to the Delaware post after serving on the University of South Carolina law faculty since 1972. Previously he was associate counsel with the firm of Sullivan and Cromwell in New York and served on the law faculties of the University of Toledo and Georgia State University School of Business Administration. From 1973 to 1980



William R. Jones

Karl P. Warden

Helen Wilson Nies

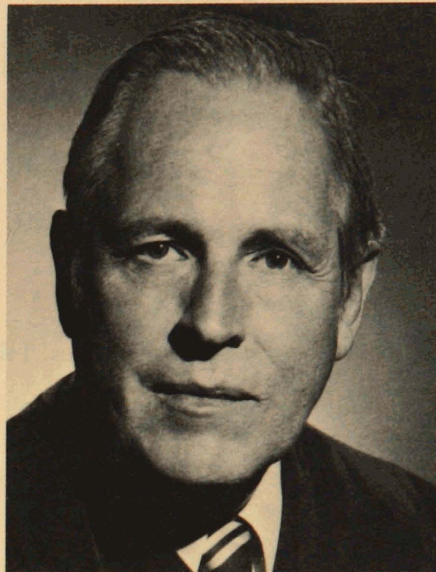
Grant served as reporter on a South Carolina Bar Association project to revise the state's Business Corporation Act of 1962. Before being named to the deanship, he was visiting scholar at Columbia University Law School. He specializes in the areas of agency, partnership, corporation law, corporate finance, securities law, and insurance law. In 1965, Grant received the bachelor's degree from the U-M School of Business Administration.

At Salmon P. Chase College of Law at Northern Kentucky University, Covington, Ky., the new dean is **William R. Jones,** who received the Master of Laws degree in 1970 from the U-M, where he was a Cook Fellow. Since 1970, Jones has taught law at various institutions, including Indiana University School of Law at Indianapolis, and Nova University's Center for the Study of Law. He has also been lecturer at the Indiana State Police Academy and Indiana Judicial Center programs for probation and parole officers. His teaching has focused on criminal procedure, evidence, search and seizure, drug abuse and the criminal process, property, and contracts. The 58-year-old native of Murphysboro, Ill., is a 1950 graduate of University of Louisville. He received his law degree from the University of Kentucky in 1968 after working as a real estate broker and businessman in Kentucky.

Karl P. Warden, who received the Master of Laws degree from U-M in 1959, is the new dean of University of North Dakota Law School at Grand Forks. He has served on the law faculties at University of Papua, New Guinea (where he was a Fulbright-Hays Fellow), Vanderbilt University, and University of Denver, and as visiting professor at several institutions. He practiced law in West Virginia and Tennessee. Among other posts, he was a police training officer, special assistant attorney general for Tennessee, city attorney in Fayetteville, W. Va., and served in the U.S. Navy from 1949 to 1953. Among his more unusual assignments, Warden performed legal work for the Zuni Indian tribe in New Mexico and Mayan tribes in Guatemala, and has done considerable consulting work regarding corrections and prison riots. He is author or co-author of books dealing with criminal law, legal medicine, and trial procedure, and is currently working on a book about problems of introducing western medicine into non-western developing nations. Warden attended Washington and Lee University and received a law degree from West Virginia University before pursuing an advanced law degree at Michigan.

□ **Helen Wilson Nies,** a 1948 Michigan law alumna, was sworn in as Associate Judge of the U.S. Court of Customs and Patent Appeals in Washington, D.C. The appointment makes her the third Michigan alumna among 12 women serving on the federal appellate bench nationwide. The other Michigan graduates are Judge Amalya Kearse of the U.S. Court of Appeals for the Second Circuit, and Judge Cornelia Kennedy of the U.S. Court of Appeals for the Sixth Circuit. Judge Nies, who had most recently been a partner in the Washington, D.C., firm of Howrey & Simon, was born in Birmingham, Ala., and obtained both her undergraduate and law degrees from Michigan. She began her legal career with the U.S. Department of Justice in 1948. She retired to raise a family, but later resumed her career in private practice, becoming a partner of the Chicago-based frim of Pattishall, McAuliffe & Hofstetter. She joined Howrey & Simon in 1978. Practicing in the field of patent, trademark, and copyright law, she held leadership posts in that area with the American Bar Association and other groups. She is married to John Dirk Nies, a member of the U-M law class of 1948 and a partner in the firm of LeBlanc, Nolan, Shur & Nies of Arlington, Va.

Sheila Gallagher



Horace W. Gilmore

Gerald B. Helman

□ **Sheila Gallagher,** member of the Law School class of 1965, has just completed service as president of the National Association of Women Lawyers during 1979-80. The oldest organization of women lawyers in the country, the association began as the Women Lawyers' Club in New York City in 1899, and then enlarged into a nationwide group in 1911. Today it has a membership of women lawyers from every state, and was one of the pioneering organizations in seeking equal rights for women. Gallagher is presently in private law practice in Anchorage, Alaska, with emphasis on real estate, contract, and labor law. She had previously been attorney for the Greater Anchorage Area Borough School District and the Greater Anchorage Area Borough, and has also served as law clerk for Chief Justice Buell A. Nesbett of the Alaska Supreme Court. A 1962 graduate of Northwestern University, Gallagher has served on the American Bar Association's council of the section of urban, state, and local government, and other groups.

□ **Horace W. Gilmore** of the U-M law class of 1942 has been elevated to judge on the U.S. District Court for the Eastern District of Michigan. The appointment fills a vacancy on the district court created when U-M law alumna Cornelia G. Kennedy became judge on the U.S. Court of Appeals for the Sixth Circuit. Judge Gilmore had been a member of the Wayne County Circuit bench since 1956 and had been serving as alternate chief judge. Judge Gilmore is the author of *Michigan Civil Procedure Before Trial,* published in 1964 with a second edition published in 1975. He chaired the 1,578-member National Conference of State Trial Judges of the American Bar Association Judicial Administration Division. Before his judicial career, Judge Gilmore was in private practice, a deputy attorney general for Michigan, and a member of the State Board of Tax Appeals. Among other groups, he holds memberships in the American Judicature Society and the American Law Institute, and has represented the American Bar Association on the board of trustees of the Institute for Court Management. He has chaired the Michigan State Bar Special Committee for the Revision of the Criminal Code. Gilmore received his undergraduate degree from Michigan in 1939.

□ **Gerald B. Helman,** 1953 U-M graduate and 1956 Michigan law alumnus, was appointed by the President as U.S. Representative to the European Office of the United Nations and Other International Organizations. Helman is serving in Geneva in the ambassador-level post. A member of the U.S. Foreign Service since 1956, Ambassador Helman has served in Milan, Vienna, Barbados and at the U.S. Mission to the North Atlantic Treaty Organization in Brussels. From 1973 to 1974 he was a Woodrow Wilson Fellow at Princeton University. Prior to his recent appointment, Helman had served as deputy assistant secretary of state for international organization affairs since 1977, and for two years was director of the Office of United Nations Political Affairs in the Bureau of International Organizations at the State Department. From 1974-76 he was deputy director of the Office of NATO-Atlantic Political-Military Affairs at the State Department. His daughter, Deborah Helman, has finished her first year at U-M Law School.

ON THE IMPORTANCE OF BEING ECCENTRIC

by James J. White
Associate Dean and Professor of Law,
The University of Michigan

[The following address was delivered by Dean White at the U-M Law School Honors Convocation in the spring of 1980]

I come today like an unwelcome dinner guest. To the extent that I deviate from the character of this meeting as a celebration of success and outstanding achievement, I hope you will forgive me. My remarks are about lawyer character and they can properly be regarded as criticism of today's law students and today's young lawyers. Some will perceive them to be unwarranted criticisms.

I wish to apply the hypotheses of David Riesman concerning American character to the current crop of law students and young lawyers. In his great book, *The Lonely Crowd*, Riesman identified two conflicting and important types within the American character. He concluded that some of us were "inner-directed" and that others, a larger group in modern America, were "other-directed." Let me first read two passages from Riesman's book so that those of you who are not familiar with it will have an understanding of what I am saying. Describing American culture, Riesman writes as follows on page 22:

> In the smaller families of urban life, and with the spread of "permissive" child care to ever wider strata of the population, there is a relaxation of older patterns of discipline. Under these newer patterns the peer-group (the age- and class-graded group in a child's school and neighborhood) becomes much more important to the child, while the parents make him feel guilty not so much about violation of inner standards as about failure to be popular or otherwise to manage his relations with these other children. Moreover, the pressures of the school and the peer-group are reinforced and continued—in a manner whose inner paradoxes I shall discuss later—by the mass media: Movies, radio, comics, and popular culture media generally. Under these conditions types of character emerge that we shall here term other-directed. To them much of the discussion in the ensuing chapters is devoted. What is common to all other-directeds is that their contemporaries are the source of direction for the individual—either those known to him or those with whom he is indirectly acquainted, through friends and through the mass media. This source is of course "internalized" in the sense that dependence on it for guidance in life is implanted early. The goals toward which the other-directed person strives shift with that guidance: it is only the process of striving itself and the process of paying close attention to the signals from others that remain unaltered throughout life. This mode of keeping in touch with others permits a close behavioral conformity, not through drill in behavior itself, as in the tradition-directed character, but rather through an exceptional sensitivity to the actions and wishes of others.

Riesman defines inner-direction at page 15 as follows:

> The concept of inner-direction is intended to cover a very wide range of types. Thus, while it is essential for the study of certain problems to differentiate between Protestant and Catholic countries and their character types, between the effects of the Reformation and the effects of the Renaissance, between the puritan ethic of the European and American north and west and the somewhat more hedonistic ethic of the European east and south, while all these are valid and, for certain purposes, important distinctions, the concentration of this study on the development of modes of conformity permits their neglect. It allows the grouping together of these otherwise distinct developments because they have one thing in common: the source of direction for the individual is "inner" in the sense that it is implanted early in life by the elders and directed toward generalized but nonetheless inescapably destined goals.

To use a physical analogy one might compare an inner-directed person to an aircraft that is navigating within an inertial navigation system, a gyroscopic system that determines where it is by reference to its own gyroscope and by its knowledge of where it started. The other-directed person is like an aircraft navigating with radar. The radar operates by sending out constant pulses of energy and by reading and portraying the return pulses.

After he sets out the two character types described above in his book, Riesman takes pains to deny that either is to be more respected than the other. I find Riesman's denials, at least insofar as they are applied to lawyers, to be

unpersuasive. My thesis today is twofold: first that almost all great lawyers are inner-directed; second that most of you, and most young lawyers of today, are insufficiently inner-directed. Some would say that it is obvious why a lawyer is better for being inner-directed, for responding to his gyroscope rather than to his radar but perhaps not all would agree. To some extent the "right" character may be a function of how one defines lawyer. To focus the analysis let me give you three examples of men I believe to be great lawyers.

The first is Clarence Darrow, a person who attended our Law School, a man who is widely regarded as one of the outstanding trial lawyers of the century. Consider one of his most famous cases in which he represented a black family in Detroit who were being tried for conspiracy to commit murder. Dr. Sweet and his family had moved into a white neighborhood of Detroit. In the course of a demonstration, occasioned by their moving into the white neighborhood, someone within the house shot and killed a person on the street and the Sweets were charged with conspiracy to commit murder. Mr. Darrow successfully defended the family on conspiracy and in a second trial procured a verdict of innocence when Henry Sweet was tried alone for murder.

Consider as a second candidate, Joseph Welch, the Boston lawyer who opposed Senator McCarthy in the Senate hearings in the early 1950s. Welch's representation of the people accused by McCarthy was careful and highly effective. His representation had a great deal to do with the decline of McCarthyism, for his skillful work disclosed how baseless were McCarthy's claims and how paranoid and wild-eyed were the charges.

Finally consider Thurman Arnold, in his later years a Washington lawyer whose name remains as the Arnold of Arnold & Porter. Arnold's active opposition of McCarthy was but one in a long line of public and outspoken acts that he took on behalf of and against various causes. It must have been highly frustrating for his partners when Arnold, as he was accustomed to do, would appear as a private citizen to testify against legislation that his clientele wished to have passed.

I suggest that none of these three men, nor any of the thousands of equally able but less fmaous lawyers, could have accomplished what they did, or would have done what they did, had they been primarily other-directed. I suspect that one cannot overestimate the hostility of the white population in the 1920s to the idea that blacks should have a right to live next to them.

By the same token it is difficult in today's climate to conceive the fear that McCarthy spread throughout even powerful institutions in the United States. In that era two members of The University of Michigan faculty left the University under circumstances produced by McCarthyism. People lost jobs in the television and movie industry and in government. No person who depended upon the support and approval of any institution big enough to be the subject of McCarthy's wrath was free to ignore the possibility of being black-listed. Welch took a considerable risk in standing as the leader publicly and on television of the opposition to Senator McCarthy.

Finally consider in today's law profession, commonly now called the law business, the folly of someone such as Thurman Arnold testifying contrary to the interests of his clientele and thus contrary to his own direct economic interest.

I submit that none of the three could have done what he did had he been navigating with radar. Darrow and Welch would have seen the wide-spread hostility in society at large to their positions. Almost every conceivable peer group to which they could have looked for direction would have thought that representing the people they did, if not wrong, was at least exceedingly foolish. It is certain that Thurman Arnold must have received the same message from his peers, namely his colleagues in law practice and his clientele. Had he been looking to those responses and not to his gyroscope, surely he would not have done what he did.

That is my thesis, namely to be a great lawyer one must be inner-directed and not other-directed. From my examples, one can determine how I define a lawyer. He is unique in that he holds himself out principally as a representative of one side in a conflict. By hypothesis, his position will disagree with and perhaps offend those on the other side. Empirically, we know that his position will often offend those not associated with the case at all.

Second, and perhaps less unique, is the lawyer's service on and to legislatures and other appointive and elective public agencies. One cannot expect doctors or businessmen to withstand the heat and controversy that are associated with the workings of such agencies. As in the case of individual conflict involving his client, it is to the lawyer that we look for dispassionate and objective advice about legislative and administrative acts.

I turn now to the second part of my thesis, namely that you, the law students of today and the young lawyers, even the pure and honest post-Watergate lawyers, are insufficiently inner-directed and, in the words of Thomas Wolfe, have too little of the "right stuff."

First some of you will object: "Why, I would oppose Senator McCarthy." "I am against the kinds of restraints on free speech, free thought, and free activities that he would have imposed. I would have been ready to stand up against him." An even greater number will say: "Why of course I would defend a black man accused of murder in connection with a housing dispute. I recognize not only the right of every person to have effective trial counsel, but also the right of anyone to live wherever he wishes to." Some of you might even argue that you would be prepared to appear in public and take a position as a citizen that would be contrary to the interests of one of your clients.

Even if such assertions were to be believed, and by and large I do not believe them, they miss the point. To favor integrated housing today is to be other-directed. Certainly it is a tenet of the upper middle-class educated American

from which most of you are drawn that a person's race should not stand in the way of any important choices. It is equally a part of that group's belief that those accused of a crime should have an effective defense. So to say that you are inner-directed because you believe those things is not persuasive. Those are the things that your peers tell you to believe; things you should say.

It is the espousal of beliefs that are not popular among your peers that proves one capable of following his inner-directions and not those of others. Show me the person who speaks out publicly against the equal rights amendment; show me the one who is willing to take a public position against affirmative action; show me the person who is prepared to defend Nixon in our community and I will show you someone who is inner-directed. Were I more vicious, I might accuse you, you who so eagerly accept today's liberal norms, norms reverberated in your peers and accepted by the larger part of society, to be yesterday's bigots. It is not my thesis that you would have been members of the Tireman Avenue Improvement Association. Rather it is that you would have been on the sidelines at the McCarthy hearings, or back at the office wringing your hands when Thurman Arnold was testifying; that you would have read about the Sweet trial with indifference.

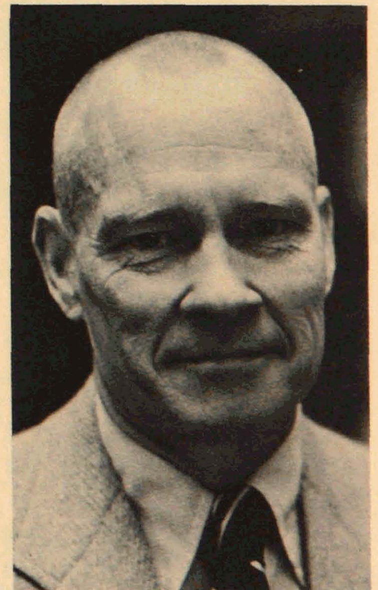
If I am going to be so harsh, perhaps I have the duty of coming forward with a little more evidence of your other-direction. Let me suggest some for you to consider, for I see evidence of conformity in the Law School community everywhere. First is the conformity to standards of dress. Since 1964 when I came to the faculty, we have been through at least one full fashion cycle, perhaps two cycles. It is now standard operating procedure to wear the three-piece suit, a restrained necktie, and carefully groomed hair to interview and to appear in an equally studied but disheveled state during the week. Since 1964 the norms of student appearance have changed as rigidly and compulsively as dress lengths in the New York fashion market.

Second is conformity in course selection. Although we have removed almost all the course requirements in response to student demands, I see you flocking like sheep to specific courses. Moreover, we hear overtones that certain courses such as the clinic, are not elected by students, not because those students believe the clinic is educationally unsound for them but because employers might regard it as an undesirable course on the transcript. For the same reason, we hear that students fail to elect pass/fail in circumstances where they believe it would be educationally sound because they fear the law firms' reaction.

Third, I observe an almost total absence of criticism of the accepted norms in the law student community. Who criticizes the ERA? Who opposes affirmative action? Who publicly favors reinstitution of the draft? I see little evidence of public espousal of unpopular causes among our student body. Finally, I would suggest that my thesis is supported by the ease with which most of our student body seem capable of fitting into large organizations, whether those be corporate law offices, large law firms, or the ACLU. My model inner-directed lawyer is at least sufficiently eccentric that he is slightly uncomfortable in such large organizations. While he may advance and find a place there, he cannot fit too comfortably. So I see more evidence than I would like that you are operating on radar not only in class and job selection, but also in your intellectual and political behavior.

Since this is supposed to be a happy occasion to celebrate your successes, perhaps you were thinking that in conclusion I can find a *Deus ex Machina* to snatch you from the reach of my criticism, to find a way for each of you to become Darrows, Welchs, or Arnolds. I cannot. Your mothers and fathers, your peers, the television and newspapers have made you what you are. Those things I cannot change.

I would only hope that four or five years from now, when each of you is doing very nicely with the law firm or when you are comfortably established in the Justice Department or, worse, in a public interest firm, that you have a twinge of guilt when you do not appear before a public committee to oppose some legislation that would have been in the interest of one of your clients, or that you feel a little uneasy when you reject the opportunity publicly to stand up for someone who deserves your support or who represents your true beliefs, beliefs that are at odds with those popular in your community. In summary, I appear not as the way to salvation but as a stimulus to guilt; guilt that may make you behave a bit more as a lawyer should.



James J. White

Coming Radical Changes in our Federal Tax System

Introduction

Radical change? Why would powerful competing forces now be deploying for what could be this decade's most important federal tax battle?

I say "most important" because the battle will focus on radical change, that is, change in our system of allocating the tax burden, for at stake are possibly significant shifts in the relative burdens borne by capital versus labor and by the various income classes. I say "most important" also because the battle may have much to do with the future quality of life within our shores.

Yet, if our tax system were to be examined solely on a *comparative* basis and apart from our own economy's current problems, I suspect the average *foreigner* would conclude that radical change was wholly unwarranted. In no other industrial country does a national tax system appear to be so noble in its thrust. For our federal system is based, in general, so preponderently on one's ability to pay. Social Security contributions aside, practically all federal revenues are derived from taxes on income, with progressive rates being applied in both the corporate and individual sectors. In the latter case—for a family of four—on the first $7,400, the tax is 0 and rises then on the next bracket only to a relatively modest 14%, with increasingly higher rates on succeeding higher brackets, ultimately reaching a maximum marginal rate of 70%.

In contrast, again laying social security contributions aside, all major European countries, raise a large part of their tax revenues from regressive excise taxes. In France, over one-half is derived from that source; in Germany, it's over a third.

And on the other side of the tax coin, is there not something noble also about the further fact that in the last 30 years we have used an increasing part of the revenue from our so-called progressive taxes to modify the sometimes harsh income-distribution patterns generated in the private sector, creating for some segments an arrangement akin to a negative tax.

No doubt our country's enormous economic growth per capita over that 30-year period made it a bit easier for taxpayers to view the tax laws as a proper device by which we could transfer income from that group to others. Wilbur Cohen, a former secretary of HEW, would observe that in the 1950s and '60s, the "haves" had only to "share" that net increase in growth with the "have-nots" (rather than sacrifice something they already had) to make possible within that 30-year period Medicare, Medicaid, AFDC, food stamps, and financial aid for students, to say nothing of the dramatic growth in Social Security benefits and beneficiaries. All of these were possible in part because the more than doubling of our gross national product facilitated our more than doubling of federal tax receipts.

And similar to the process involved in compounding interest, that increased abundance, and the wide sharing thereof mandated by law, then made it easier for a relatively idealistic people, not just Ralph Nader, to deflect their concerns away from societal bread-and-butter issues and to focus on costly environmental and safety issues, to enhance the long range quality of future life on this planet. In consequence, came the enactment of major new laws—important here, *expensive* new laws—affecting use of our land, our waters, and our air, and bearing more specifically on such diverse matters as strip mining, location and indeed establishment of nuclear plants, preservation of wildlife and underwater species, and abatement of pollution whether caused by automobile tail pipes, factory sewage, or smoke stacks, or by mere noise.

All of this no doubt contributed to man's belief in this nation's relative goodness, and testified also to what at least appeared to be our ever growing tangible abundance, and

by L. Hart Wright
Paul G. Kauper Professor of Law
The University of Michigan

[The following remarks were delivered at the first annual U-M Law Alumni Reunion and Law Forum on May 30, 1980]

the two together help explain why, among all embassies abroad, only at American embassies do you still find people standing in line "forming there a waiting list"—now 1,000,000 long—of those seeking to migrate to this land.

Current Basic Problem Identified

Two problems coincide

But, it bears repeating, the attractive but expensive programmatic statutes of the 1950s and '60s blossomed into being in part because our governmental leaders and our people then had thought the increments could be paid for out of the supposedly ever larger *net* annual increases in our GNP, generated by our then ever more efficient and then ever more productive enterprises, driven as they then were by cheap energy with their profits being available for modernization and expansion, providing more jobs, more goods, more abundance, and more taxes.

But as we moved into the '70s, those native to this land hardly needed to read an anthology on the world's imperfections to realize that the foregoing American economic dream might not be fulfilled because of the cumulative impact of two considerations.

First, various costs which now have to be shouldered by our economy were proving to be *far* greater, relatively, than the average among us had supposed earlier when those noble programmatic laws first were adopted or expanded.

Second, realization of this began to dawn on us at a time when yet other evidence began to suggest that our economy's own previously growing industrial prowess had come to a halt.

In no other industrial country does a national tax system appear to be so noble in its thrust.

The Economy's Rising Burdens

As to the first of these, that is, the previously unexpected rising costs our economy must now shoulder, any thought that, for example, our economy could continue to run on cheap energy had to be abandoned on a January day early in the '70s.

In contrast to the circumstances 30 years earlier when we imported almost no oil, by 1972 we were importing more than 1 billion barrels a year, but at an average cost of only $2.30 per barrel.

Then OPEC began to raise the price, and by December 31, of the next year—1973—the cost had gone up 50%, to $3.65 per barrel.

It was on the following day, January 1, 1974, that the roof began to fall in, for the average price per barrel was increased 300%, to $10.84.

Then to make matters worse, after six months of consternation and concern, we decided to go on a consumption binge. Between 1972 and 1979, our *annual* consumption of imported oil increased by over a billion barrels.

The consequent enormously escalating burden on our economy escalated again enormously in 1979 alone. In the first quarter of that year, the average price we paid for imported oil was $13.96. By the last quarter, it had almost doubled, to $23.69, with the average price on December 31 being $25.01.

Then, as we moved into the 1980s back in January, our largest supplier, but also the most friendly and traditionally, therefore, the one with the lowest price, Saudi Arabia, upped its price $2 per barrel. And a second comparable increase was applied earlier in May, its benchmark price becoming $28 per barrel, 11 times greater then the average price we paid back in 1972. And the even higher prices now charged by other OPEC countries are expected to be increased at OPEC's June meeting. [*Editor's note:* They were!]

Thus, our economy must produce at least $85 billion to pay OPEC for our imported oil over the next 12 months and the end of the escalating price increases even then will not be in sight.

Earlier Failure to Pay the Piper

Alongside those increases came also, with cause and effect entertwined, the most terrifying inflation to which our economy has been subjected. But among the current costs which increased were several which were attributable to benefits or services actually consumed in earlier years and for which then we simply had failed "to pay the piper."

Who really contemplated, when we first enacted or expanded those earlier programmatic laws, that we also would fail in 19 of the last 20 years fully "to pay the piper," running deficits and that, in consequence, now in an era of high interest rates, over $65 billion in interest must currently be paid on a national debt now crowding $850 billion.

Include also among current costs for earlier consumed services, the $25 billion payable annually out of current revenues to the now retired persons who served earlier as civil servants and another enormous amount for retired military personnel, the earlier promised pensions of both now having swollen further by an escalation clause geared to our unprecedented inflation.

But these are mere dwarfs compared to the $128 billion which must be paid out of current Social Security revenues over the next 12 months to the more than 35 million Social Security recipients whose benefits also rose with inflation.

That the system has to pay out to one generation, almost currently, the very funds which it presently takes in from two others, is evident from the fact that, as of July 31, 1979, the system's total assets equalled only four months' worth of benefit payouts, and constituted, therefore, nothing more than mere current working capital.

Twenty years ago, when Jack Kennedy became president, the ratio of active workers to Social Security recipients was 5 to 1 and the tax rate on those workers was a modest 3% which applied to maximum covered wages of $4,800. Then the maximum annual contribution per employee reached $144, a contribution matched by his employer, and total annual disbursments equalled only $10 billion.

As of January 1, 1981, the rate, compared with Kennedy's time, will have more than doubled (to 6.65%), and the maximum base against which it is applied will have jumped by six times (to $29,700)—the two-component January jump itself, in the case of a person earning $30,000, being 24%.

In part these increases were necessary because now there are only three workers per recipient, not five as in Kennedy's time. Further, benefits currently to be paid out were swollen also by an escalation clause responsive to inflation. Indeed, the latter helps explain why an individual retiring in 1979 at age 65, if then still married to a dependent spouse, would have expected at that time to receive over his retired years 11 times the amount he *personally* paid into the fund.

Who would have expected 20 years ago that the mere increment in this coming fiscal year's payout, attributable *solely* to inflation, would far exceed the total cost of the entire program during the year Kennedy became president.

And the worst, we now know, is yet to come. Forty-five

years from now, when those born during the decade-long baby boom following World War II are on Social Security, there apparently will be only two workers to support each Social Security recipient and even this ratio assumes some improvement in our currently depressed fertility rate.

The Economy's Stagnation

The public's more or less sudden awareness in the '70s of these unexpectedly high costs came, as I have said, almost simultaneously with highly publicized *manifestations* that our economy, relative to that of others, was in trouble.

Tolerable it may have been that the Japanese, by the early part of the '70s, through exports to us, came close to taking over our television industry. But, as to our future life, think twice about the more wide-ranging adverse implications of a comment made to Congress in the middle of that decade by President Ford's secretary of the treasury, to the effect, with respect to a much more basic industry, that a relatively new steel plant in Kimitsu, Japan, was more than twice as productive per worker as the enormous but old United States Steel Company plant in Gary, Indiana.

By the end of the '70s (before the current recession), David M. Roderick, "Big Steel's" chief executive, was acknowledging openly to the press that his company could not come even close to generating enough capital to replace its aging plants with modern mills like those of its "agressive global rivals" in Japan and Western Germany, and that "assuming no changes in steel's cost-price relationship, there is no question that the domestic industry is going to continue to shrink." Indeed, U.S. Steel itself then again put off going forward with construction in Ohio of its first new integrated steel mill in 26 years.

Today, moving into a new decade, we hear as to an illustrative third industry, one which we thought was as American as apple pie—automobiles—that a greater number of cars actually will be produced during 1980 in Japan than we will produce in the United States. Indeed, they now have taken over, through exports to America, almost a quarter of our own domestic market, their total exports throughout the world presently having reached well over four million annually.

The '70s Basic Productivity Problem

But these illustrations, while very disturbing, actually are manifestations of *diverse* problems intertwined. The prime concern on which the tax controversy will focus is singular and basic. In the 1950s and '60s, our economy literally leaped ahead through *productivity* gains—real output gains per man-hour of work. The national income per person employed rose by over 70% in that period, and the consequent benefits were shared widely through new laws. But last year, President Carter's secretary of the treasury reminded us that in the '70s our annual productivity gains began to drop significantly, first down to 2%, then down to 1%, and last year—*before* this recession—zilch.

Effect of Reduction in Productivity Growth

On this count—long-term productivity growth rates—Japan and all our major European competitors except Britain have been outstripping us substantially.

Without real growth in productivity, our total standard of living is certain to go down, and the fact that those foreign countries, with which we do compete on the international marketplace, are enjoying significant growth in productivity could be a contributing factor.

But, looking only at the domestic front, without real growth in our productivity per man hour, as our ratio of active workers to Social Security recipients drops from 3 to 1 down to 2 to 1; either the active working generation or the retired generation will have to take a real and significant cut in the quality of life they had expected, thus creating added tension between the generations. Indeed, this process could begin with the next scheduled substantial increase in the Social Security tax this coming January with the active work force being the certain loser.

And apart from that, without an increase in productivity, no increase in wages is possible without inflation. And any such inflation would simply mean that any causal-related increase in wages in fact would not improve the quality of this nation's material life.

Finally, without growth, no new governmental programs, however needed, could be initiated without sacrificing some program to which some of our people had grown accustomed. The threat of such retrenchments is certain to increase tension and the political in-fighting associated with our governmental processes.

Need for Increased Capital Investments

Greater productivity in terms of output per man hour of work, is itself dependent on many factors, including even education that affects, for example, the quality of our scientists and engineers who make use of research and development expenditures, and of our managers whose business decisions ultimately can affect the productivity per hour of our workers.

[Our] economy must produce at least $85 billion to pay OPEC for our imported oil over the next 12 months.

But in the end, since we cannot stretch the length of one hour, and are not likely to increase the number of regular hours each employee is to work in a given day or to carry around a whip, technological breakthroughs and better and more industrial equipment become musts, suggesting there must be more capital investment therein.

Additional capital investment is needed not only to provide better plant and equipment so that each existing employee becomes more productive, but also to provide for expansion, i.e., for additional plant and equipment which in turn will provide the needed additional jobs to accommodate our expanding labor force.

In this latter connection, observe that since 1973, annual non-residential fixed investments in plant and equipment, as a proportion of our annual gross national product, have not increased. Indeed even the rate of increase based on constant non-inflated dollars has been only half as fast as the rate of increase in the size of our civilian work force, i.e., in the group who have or want jobs. Thus, our capital investments, completely contrary to our earlier experience in the '60s, have been lagging behind the rate of increase among those seeking jobs.

Thus, the question: From where is the necessary capital to come?

Sources of Capital Formation

First Source: Personal Savings

A significant part always has come from the personal after-tax savings of individuals who either invest directly or

deposit their savings in banks which then lend them to investors.

And given the inflation and its threat to our individual sense of security, one might have expected, beginning say in 1975, that we as individuals would have started to save an increased percentage of our after-tax incomes.

In fact, however, we seem to have gone on a consumption-spending spree, perhaps "to buy consumers goods before prices rose even higher." Whatever the reason, over this recent five-year period, from 1975 to the present, the share of our *personal* after-tax incomes actually saved dropped annually from 7.7% to 5.8%, then to 5.0%, 4.9%, and in 1979 to 4.5%, with the figure being only 3.3% in 1979's last quarter.

In recent years, comparable personal savings rates in each of the other major industrial countries, including even Britain, was *far in excess* of our percentage rate, with Japan, Germany, and France leading the list.

Further, here, to make matters worse, household borrowings exploded. Outstanding consumers' installment credit alone, home purchases aside, had increased by an additional $40 billion in 1979 alone. Moreover, adding in borrowings to purchase homes, whereas the ratio of personal savings to household borrowings in the peak year 1975 stood at 2 to 1; in 1978, it was just the reverse.

Finally, observe that, in any event, personal savings (which do include savings invested in a home) are less available to the business sector for investment in machinery—to the extent those savings are invested in homes.

Second Source: Corporate Sector's Internal Sources

A second source of new capital involves the corporate sector's own internally generated funds.

To finance acquisition of new equipment and buildings, this sector has available two internal sources.

The first and largest comes from that part of this sector's business receipts representing capital allowances, principally depreciation deductions. In 1979, these capital allowances amounted to $187 billion, a sum much larger than 1979's $73.8 billion of personal savings.

However, investment funds generated by capital allowances are intended, over the long haul, merely to accommodate replacement and modernization, not increments. Unfortunately, in recent years, because depreciation deductions are geared to our plants' and equipments' *original* cost, even the contemplated aim of mere replacement cannot be achieved if only because of inflation and the consequent enhanced cost of new substitute machinery and industrial buildings.

Turn now to the corporate sector's second largest internally generated source of investment funds—its retained after-tax profits *not* distributed as dividends.

This differs from the first source (capital allowances) in that, in theory at least, the former (retained after-tax profits) should have enabled this sector to make *net new* investments in plant and equipment.

But over much of this decade that actually has not been possible. While we treat a corporation's entire nominal profit as "income" in the sense of taxing the whole; now for a number of years, a portion of the after-tax profit retained after paying dividends actually represented what some described as "phantom profit" in the sense that it actually was not available for incremental investments. This was because a portion—in 1979, $16.7 billion—was consumed by the previouslymentioned inflation-generated short-fall in capital allowances to accommodate mere replacements.

Even more unfortunately, an even larger portion of the cash flow generated by 1979's $91.9 billion of after-tax retained profits. Namely, $41.8 billion, was needed to meet the inflation-generated increased cost necessary merely to replace inventory previously sold.

Thus, in the end, of 1979s' $91.9 billion in retained after-tax profits, only $34.4 billion actually was available for net new capital investments.

Type of External Funds Sought by Corporations

Adding to these worries is another: the possibility that corporations, in seeking funds from outside sources, may be creating yet another related problem.

For years new stock issues have accounted only for a very minor part—on average, only about 3 to 4%—of the capital investments made by non-financial corporations.

To a much greater extent, on looking to the outside, corporations have obtained new funds by going further into debt. Perhaps this was in part because individuals in deploying their personal savings had departed from the equities market, a phenomenon most pronounced among younger investors who simply headed for the nearest bank or were willing only to purchase secure bonds, the interest rates on which, as a new phenomenon, had started to outstrip the so-called "total return" from stocks.

Whatever the reason might be, some fear that the resulting substantial increase in the corporate sector's debt-equity ratio—which has more than doubled over the last 25 years—leaves it uncomfortably vulnerable when we encounter the downward side of a business cycle.

And this worrisome change brings me to a question: Is this particular corporate practice due at all to the impact of our federal tax law on the corporate sector, and does that impact otherwide unfortunately and unfairly impede capital formation?

Relative Biases of U.S. Tax System

In General

In respect to that general question, our tax system does include three relevant biases and all three will be points of concern in the coming tax battle.

I. The *corporate* income tax itself does contain a bias against equity funding, favoring debt financing;

II. Our income tax system, now viewed as a *whole*, also does contain two significant biases against ordinary income derived from capital, when compared to that derived from services; and

III. Our *entire* federal tax system relies much more heavily on income taxes than do most of the other industrial nations and, when viewed *comparatively among nations*, relatively does reflect a bias against capital formation.

U.S. Corporate Tax System's Bias

As to our corporate income tax's bias against equity funding, note that such part of an incorporated factory's operating profits that is used to pay *interest* on borrowed capital is *deducted* from its gross profit in arriving at the corporation's own net tax base. In effect, a zero tax rate is applied at the corporate level to that portion of the factory's operating profit used to pay that interest. Thus, such profit is taxed only once, to the recipient-creditor at that marginal rate appropriate to his income.

In contrast, to the extent that corporation obtained its capital from shareholders, profits attributable to that capital do suffer a tax at the corporate level, most of it at a stated rate of 46%.

Additionally, that portion of the corporate sector's profit remaining after allowance for its own income tax will, if distributed to individual shareholders, be piled on top of their other incomes and be taxed at their highest marginal rates. Immunity from this second tax traditionally was confined by statute to the first $100 of dividends received each year by an individual. Thus, if a husband and wife owned their shares jointly, together they could exclude only the first $200 of dividends. These quite modest immunities were doubled by a bill enacted in April 1980 and were extended to interest received from bank deposits and corporate bonds.

Nevertheless, the great bulk of the $52 billion in dividends declared in 1979, to the extent received by individuals and not by tax exempt organizations, did suffer a second and substantial tax on being received by the individual recipients.

Thus, while there is but *one* tax on distributed *interest*, there are *two* significant taxes on most *distributed* corporate profits, and this must be taken as a given fact however one otherwise feels about a complementary and arguable question: Who actually bears the economic burden of those two taxes?

Income Tax System's Biases Against Income from Capital

This so-called double tax on that portion of corporate profits distributed as dividends tends, standing alone, to make our whole federal income tax system biased against income from capital, for no such double tax is applied to the income from wages.

Further exacerbating that bias is the fact that, at the *individual* level, marginal tax rates on ordinary income from capital reach 70%, where-as a normal marginal ceiling of 50% has been placed on marginal rates applicable to wages.

Foreign Systems Mitigate Their Double Tax

Among major industrial countries, the United States stands almost alone in continuing to impose two full taxes on that share of corporate profits distributed as dividends to individual shareholders. Almost all of the other industrial nations have adopted one of two basic devices which have the effect of reducing the bias favoring debt financing, by whittling down on the so-called double tax we apply to profit distributed as a dividend.

The first method is illustrated by the so-called dual-rate approach of Germany. There the regular corporate rate of 56% is applied solely to *undistributed* profits; the corporation itself need pay only 36% on any profit it distributes.

Belgium, France, England, and Canada illustrate the second method. There, a corporation's own tax is unaffected by whether its after-tax profit is to be retained or distributed. The French rate, for example, is 50% in either case. The difference comes at the shareholder level. Stockholders there, after applying their own marginal rates to dividends received, reduce the resulting tentative tax by a credit allowed them for a significant portion of the tax which the corporation itself actually had suffered. In France, the formula is designed so that a shareholder whose "grossed-up" dividend tentatively would suffer a top marginal rate of 50% would, because of the credit, only pay a net tax equal to 25% of his actual dividend. In America, he would pay 50%.

Eisenhower's administration concluded that we should, over a transition period, move toward the second of these systems and, with this in mind, it secured enactment of an initially modest arrangement permitting shareholders, on receiving a dividend, to take a credit, in effect, for what intially was to be a small part of the tax the corporation had paid. But several years later with President Kennedy's backing, Congress terminated the earlier tentative move toward one of the European systems.

Observe that both devices used abroad have the effect, initially, of increasing the net after-tax yield of stocks, making them more attractive to investors. Germany, though formerly utilizing only one of those two devices, recently adopted both. Now the shareholder, on receiving a dividend, gets a credit for the *reduced* tax which the corporation itself paid on profits distributed. In net effect, in Germany there now is only one tax on *distributed* corporate profits, and that is the tax fixed by the shareholder's own marginal rate.

Foreign Nations' Greater Reliance on Excise Taxes

Finally, when a tax system is viewed as a whole, there is another reason why all tax systems in Europe have a relatively stronger element of bias favoring capital formation than does our own federal system.

This follows from the fact that, relatively speaking, we rely on *income* taxes for a far greater proportion of our revenue than do they. And as you know, as a *general* proposition, income is included in the recipient's tax base whether the after-tax amount is spent or invested.

But it is otherwise with respect generally to *sales* taxes on *consumers* goods. In the latter instance, that portion of one's income which is deposited in interest-earning bank accounts, or used to purchase corporate stocks, is free of that tax.

Thus, this type of tax, in contrast to income taxes, includes some incentive to save and this is so whether or not it proves to be adequate in the face of any given set of counter-incentives.

European legislators, spurred on by the EEC, make substantial use of that incentive effect. Whereas our own federal government derives relatively little revenue from such excise taxes, Social Security contributions aside, France—as previouslymentioned—derives just over half of its other revenue from such excise taxes, and Germany over one-third. There, as in *all other* Western industrial countries, governments rely heavily on what is called a *value added tax*, a sophisticated form of the more familiar sales tax.

Conclusion: Power Blocs Respond

Kennedy's Non-Tax Proposal

Among our own leading political activitists whose ambitions or responsibilities have forced them to outline publicly their own proposed solutions to our disturbing and steadily deteriorating long-range circumstance, some—in their responses—have been more affected than others by the *additional* but hopefully *temporary* complications generated by a *hopefully* temporary recession.

At one extreme, both on this count and also in calling for yet "more government," i.e., more *direct* governmental intervention in connection with both our long- and short-term problems, was Senator Edward Kennedy. In a major policy pronouncement back in May, he called for a massive "Marshall Plan" to re-industrialize our country, envisioning a program at least as large as that which we initiated in Europe after World War II.

He spoke of a new "economic partnership" embracing government, business, labor, and academia. And within the first 100 days following what he hoped back in May would be *his* own coming inauguration, he promised to create a quasi-public corporation empowered to provide grants,

loans, guarantees, and subsidies to individuals, businesses, research organizations, and cities interested in new economic development or revitalization of existing businesses or industries. The corporation's funds would come from Congress and from borrowing in the capital markets.

Additionally, before as well as during the Democratic Convention, he urged adoption of a $12 billion subsidy for job and training programs, while simultaneously urging across-the-board controls on prices, wages, profits, dividends, and rents to get at inflation, and gasoline rationing as a further attack on our energy problem.

Responses of Most U.S. Power Blocs: In General

Most, though not all, other outspoken public figures have called *primarily*, however, for *tax* changes, arguing first that increased capital investments are essential if we are to increase our productivity, implement technological breakthroughs, and simultaneously meet the needs of an expanding labor force. Second, they assert that the requisite increase in capital investments is not likely to be achieved without making fairly radical changes in our tax laws.

But even among these observers, substantial disagreement has existed as to method, that is, as to the type of tax law change which should be adopted from among the possible competing alternatives.

Forty-five years from now, when those born during the decade-long baby boom following World War II are on Social Security, there apparently will be only two workers to support each Social Security recipient and even this ratio assumes some improvement in our currently depressed fertility rate.

One issue separating the observers might be described in terms of how general or how rifle-like the requisite tax response should be.

On one side are public figures whose proposed remedy was shaped in part by an even more broadly based concern regarding America. To them, in complete contrast to Senator Kennedy, the capital-investment problem is only one of many unfortunate consequences springing from expensive and, to them, distasteful "Big Government."

Reagan's Views re Individual Tax Cuts

The antidote, as Governor Reagan puts it, is "to get the government off our backs" and, to that end, he supports to the hilt the broad shotgun approach of the original Kemp-Roth bill. The latter focused *only* on individuals and proposes to reduce by 30% over a three-year period all income tax marginal rates applicable to each of the brackets applied to individuals. At the end of that transition period, illustratively, the top marginal rate would be 50%, in place of the present 70%, and the bottom 10%, in place of the current 14%.

This would have involved a massive tax cut which, *viewed in isolation*, would reduce by $90 billion the revenue which otherwise *annually* would reach the treasury beginning three years hence.

Some, though clearly not all, conservative supporters of that proposed cut appear to be more dedicated "Keynsians" than are those who characterize themselves as such. For some such supporters suggested that individuals, in aggregate, by virtue of such a reduction, then would use the tax saving in a fashion which would revitalize our economy, as did occur, they assert, from a tax cut in John Kennedy's day. Some even went on *also* to imply that the revitalized economy then would generate sufficient additional revenue to offset the aforementioned revenue loss.

As to the first of those two matters, those who, by so stimulating our economy on the *consumer's* side, think they thereby would solve our long-range capital investment and productivity problems are, to say the least, engaging in a questionable comparison to the Kennedy era.

They *ignore* several other *very* substantial but rifle-like incentives which the Kennedy administration fostered for the *supply-side* of our economy, to facilitate increased capital investments—illustratively, the investment credit, more favorable depreciation-allowance practices, and a four percentage-point reduction in the rate structure.

Also overlooked by those who look *only* to Kemp-Roth, and who rely by way of analogy on the Kennedy administration's experience, is a major difference between our economy now and our economy then.

Not the least of these differences is the existence now of terrifying inflation, which an individual tax-reduction stimulant of such massive proportions would tend, absent a counter-weight, to exacerbate given, particularly, the even now projected deficit of $30 billions for fiscal '81.

Some Kemp-Roth supporters, though fully aware of the foregoing, stand fast, nevertheless, in their support of the proposal if only because they actually do not contemplate that this massive tax reduction would be allowed *for long* to create additional artificial purchasing power on the *consumption* side of our economy.

Nor do they contemplate that the resulting drop in revenue would generate, for long, government deficits which, if they did ensue, would force the government to increase its borrowing from banks and investors, thus soaking up the private savings generated by the tax reduction itself.

Indeed, these particular supporters of the original Kemp-Roth bill actually favor tax reduction precisely because, in "getting government off our backs," they also plan to *reduce growth* in government expenditures, by applying some kind of ceiling on the budget.

Mr. Reagan himself, for example, recently acknowledged this would be necessary and promised that, by a "comprehensive assault on waste and inefficiency," he would reduce the otherwise projected inflation-generated growth in the expenditure budget by 2% in '81. In later years, the cut would gradually increase to 7% annually compared with what otherwise would have been spent on the basis of current projections. But even with these expenditure cuts, and after taking account of projected increases in revenue generated by his projected tax cuts, he acknowledges a projected estimated $27 billion deficit in '81 and $21 billion deficit in '82.

Inflation Indexing

Some who otherwise do *not* support Kemp-Roth do believe, nevertheless, that we should neutralize the effect of the "inflation-creep" which, for example, forces the income of individuals to be taxed in increasingly higher rate brackets though their *real* incomes have *not* gone up.

It has been estimated that, with the current inflation rate, the treasury derives an annual revenue windfall or bonus of at least $16 billion (and perhaps as high as $22 billion)—thereby diverting for the public sector's use, and away from

the private sector, a *growing percentage* of our GNP.

Some persons, though critical of Kemp-Roth, would neutralize the effect of this "bracket-creeping" by indexing certain provisions of the tax law to the inflation rate.

On the other hand, Kemp-Roth supporters (including Mr. Reagan) note that the treasury's windfall, generated by bracket creeping, will be *far more* than offset in the case of individuals by that bill's cumulating three-year 30% tax cut in rates.

However, regarding method, these two power blocs will come closer together as of the moment that three-year period ends. For the Kemp-Roth bill, in addressing itself to the end of its three-year tax-cutting period, mandates what only then would become an annual adjustment raising the dollar amounts of the various rate brackets and of the $1,000 per-capita exemption by a percentage increase geared to each year's increase in the consumer price index.

Critics of this narrowly focused index arrangement, while acknowledging that there is merit in the underlying idea, suggest that it renders all too simple what actually is a very complex idea. In truth, the proposal does ignore a tremendous host of obviously related sub-issues, such as whether the *cost* of all investments also should be linked to the consumer price index, and whether indexing, if applied to income, should, in justice, be extended to the debt side of the ledger—in which case gain could arise (though a debt is paid off in full) if, because of inflation, that repayment actually is made with cheaper dollars than those originally borrowed. Otherwise, the tax law would be giving a tax preference to the debtor class.

Senate Finance Committee re Personal Tax Cuts

One month ago, on August 20, the Senate Finance Committee, in unanimously reporting out its own comprehensive tax proposal, in effect rejected indexing to counteract inflation. Also rejected was the Reagan supported Kemp-Roth commitment to a three-year 30% cut in individual rates. Indeed, concern regarding cost in lost revenue *vis-a-vis* a desire to provide significant tax reduction to the supply or business side of our economy led that committee even to forego offering individuals as much as a 10% cut for the single year 1981. But—as to individuals—the committee did go part of the way, by approving for that single year a much less costly reduction, namely, a drop in all marginal rates by variable amounts ranging from one to three percentage points. The top rate would drop from 70% down to 67%, with the bottom 14% rate dropping to 12%—thus slashing treasury receipts for calendar year '81 by $13 billion.

This cut in marginal rates would be supplemented by a $100 increase in the per capita exemption—at a revenue cost of $5 billion—and by modest increases in the zero bracket amounts.

Another almost $3 billion would be lost by increasing the capital gains deduction from 60% to 70%, and by reducing the corporate rate on such gains from 30% to 28%.

Anderson: re Personal Tax Cuts

Ten days later, on August 31, Representative John Anderson indicated not only his opposition to the Reagan supported Kemp-Roth but also his unwillingness even to compromise. He asserts, first, that there should be *no* across-the-board income tax cuts for *individuals* until we have attained a balanced budget. Sacrifice, he says, is appropriate to that noble and necessary end.

Second, he does agree, once that budget is in balance, that the first individual cut which can be afforded should take the form of an indexing arrangement to get at bracket creeping.

Third, to deal more directly with the energy problem, he fosters a 50¢ per-gallon gasoline tax, with the proceeds going into the Social Security Fund, to facilitate a reduction in Social Security taxes which under existing law go up substantially this coming January, and also to help pay the increased amounts to which beneficiaries will be entitled under the law's automatic escalator geared to inflation.

Fourth, otherwise, until the budget is in balance, his aides assert that tax law changes should be confined to the *supply* side of our economy and to its long-range problems. And even as to this, as they see it, some further delay may be in order.

Carter's Opposition to Kemp-Roth

Four weeks ago, on August 27, the third candidate, President Carter, outlined his proposals. Earlier, relying on a combination of inflationary concerns and cost-benefit arguments, he had rejected Kemp-Roth's 30% tax cut for individuals.

Administration spokesmen at that time had asserted that this massive deficit-generating cut was a most inefficient way to accomplish our most important objective—to get at the capital investment-productivity problem.

In short, Carter's advisers note the absence of any built-in link between the dollar amount of such generalized tax reductions and capital investments. They express the fear that an unknown but substantial part of the tax savings achieved by that bill, particularly among the millions of low and lower-medium bracket taxpayers, would simply be spent on more *consumer goods*, not saved for capital investments.

[In] the end, of 1979's $91.9 billion in retained after-tax profits, only $34.4 billion actually was available for net new capital investments.

Carter's Proposed Cut for Individuals

But while the administration says it is opposed to a *general tax cut* for individuals, it also knows, first, that a *recession* is hardly the time to increase taxes and, second, that this coming January, by virtue of a pre-recession 1977 law, our Social Security taxes on employees and employers are going up, both the rates and the base, and to the tune of another $15 billion.

To offset the *rate* increase component, the administration now has proposed to allow employers and employees to take a credit against their income taxes, the amount to be equal to 8% of the Social Security taxes they actually pay. This will reduce income tax revenues by about $12 billion.

Whether for political reasons, notions of equity, or because of the President's "born-again-Christian" perspectives, his tax package also takes on a problem ignored by the other two candidates, in that he follows the lead of a Senate Finance Committee proposal in dealing with the so-called "marriage penalty" now suffered by our millions of two-earner families. Half of all women still living with their husbands hold jobs, and 60% of those couples now pay a tax higher than they would pay if they had foregone marriage and had chosen simply to live together in "*sin*", filing separate returns.

Because different rate schedules and different zero bracket amounts are used by married and single persons, two-earner married couples must pay more tax than two singles living together in any case, generally speaking, where the lower-earning spouse earns at least 20% of the couple's income. Indeed the marriage penalty is greatest when they earn exactly equal amounts, 50-50. That penalty disappears completely, however, and, indeed, slowly emerges into a marriage "bonus" as the lower-spouse's earnings begin to fall below 20% of the couple's income.

The President, adhering to a proposal unanimously approved only a bit earlier by the Senate Finance Committee, would reduce, but not completely eliminate, the differential between two-earner married couples and two singles who live together. He would allow the married couple to take a deduction equal to 10% of the lower-earning-spouse's *earned* income, though this deduction could never exceed $3,000.

Because of that ceiling on the deduction, a substantial penalty will remain where the earned income of the *lower*-earning-spouse passes beyond the $30,000 mark. But *most* of the so-called penalty would be eliminated for *most* two-earner married couples, at a cost next year of $4.7 billion in lost revenue.

In the end, however, this arrangement is likely to antagonize the other more traditional one-half of all married couples involving wives who *do not* hold jobs. Will they not feel short-changed once they learn that their deduction will be zero, and that they, if one spouse earns $60,000, will pay tax at their highest marginal rate on $3,000 which has been freed from tax in the case of two-earner families where each spouse earns $30,000.

The unfortunate fact: It is impossible to design a formula which is equitable to all three interested groups.

Synopsis re Cuts for Individuals

A comparative profile synopsizing the *total* reduction effects of the foregoing alternative plans on individuals show Mr. Reagan fostering by far the largest cut, with those in higher brackets enjoying far greater relief, *both* in *dollar amounts* and *proportionately*, than would be the case under the other plans.

This follows from the fact, first, that an across-the-board cut, such as 10% in *marginal* rates provides the greatest percentage point reduction to those in the higher brackets, and second, it so happens that the higher brackets cover wider ranges of income, so that each percentage point reduction in marginal rates affects a larger dollar amount of income.

For example, with reference just to rates, the first-year 10% cut under the Reagan-supported plan would reduce the highest very large bracket by seven percentage points, dropping it from 70% to 63%, whereas the reduction of a taxpayer in the 40% bracket would be only four percentage points.

The Senate Finance Committee's proposed reduction is both less drastic and tilts less toward the upper brackets. While the largest *percentage point* reduction is the three percentage-point drop from 70% to 67%, an additional total dollar reduction—amounting to over one-third of those generated by rate reduction—comes from increases in the exemption deduction and in the zero-bracket amounts.

Mr. Carter's plan is even less drastic and tilts more toward those in middle and lower brackets. This follows from the fact that Carter, basically, opposed a *general* tax decrease but was willing, through an income-tax credit, to neutralize what otherwise would have been a Social Security tax *increase* that could affect *only* the *first* $29,700 of income. Further, his attack on the marriage penalty also has a cap or ceiling, so that the *maximum* cut available is available where the lower earning spouse's earned income reaches $30,000.

Of course, Mr. Anderson's proposal regarding individuals is the least drastic, and tilts not at all, since zero reduction is accorded one and all.

Emerging Agreement on the Supply Side: 10-5-3

Though there are significant differences among the three candidates regarding cuts on the individual *consumer* side of our economy, the otherwise developing substantial popularity of a proposal made by yet others, directed more specifically to the *supply* side and to the capital investment problem, has—as to *that* side—brought the three candidates within visual range of each other.

The story begins with the proposed Jones-Connable Capital Cost Recovery Act, HR 4546, now more popularly characterized as the 10-5-3 Bill, the principal original sponsors of which are two influential members of the House Ways and Means Committee, one being the ranking minority member.

This proposal, in a nutshell and in its original undiluted form, was directed exclusively at the business sector; that is, at the *supply* side rather than the consumption side of our economy. Its preamble is more discreet, however, characterizing the bill's purpose in terms of increasing "capital investment *and* expanded employment opportunities."

But it would seek to accomplish this by increasing enormously the cash flow available to business, accomplishing this by substantially accelerating business' depreciation deductions, telescoping them into a period very much shorter than the actual useful life of the affected property and thereby reducing substantially the time span over which, for tax purposes, business now must spread its depreciation deductions.

Residential type buildings would be unaffected. Otherwise the formula is simple enough. The cost of commercial and industrial buildings could be written off over 10 years, equipment over 5 years, and autos and light trucks over 3 years, with the limitation that, as to this third category, acquisitions to the extent exceeding $100,000 in any one year would not qualify.

Carter's Objections to 10-5-3

The administration opposes this bill while simultaneously conceding that our present depreciation arrangements warrant change.

The administration charges, first, that the tax break and, thus, the investment stimulant would vary widely among different industries. This would occur because, in practial terms, the bill offers *proportionately* a much larger tax break to long-life property, such as a steel mill furnace, than to a shorter-life machine which, if it had an actual useful life of only five years, would get no additional break at all. Further, so the administration asserts, there is no evidence that productivity is increased more by a bit earlier replacement of long-life property than by a bit earlier replacement of shorter-life property. Thus, contend the bill's opponents, that proposal's lack of neutrality between industries will artificially and, according to the administration, also irrationally distort the relative thrust and potential growth of the diverse segments that make up our economy.

The second objection goes back to the cumulative impact

of two considerations. The bill would apply *only* to property acquired *after* the bill's effective date. And this is one of two reasons why the bill's impact in the first year would be fairly modest. The second: even as to newly acquired property, the reduction in the longer useful lives which now are used for tax purposes—down to the newly proposed shorter periods—would be staged in over a five-year transition period.

In consequence of these two limiting factors, the first year's revenue loss, and thus the stimulant, would be a modest $4 to $5 billion.

However, the phasing-in transition approach is criticized by the administration becaue the phase-in would create a *perverse* and counter-productive effect, part cularly with respect to buildings or long-life machinery. By postponing an acquisition a year or two—to the detriment of the economy—a taxpayer could obtain a much shorter useful life for depreciation purposes.

Third, an administration spokesman also originally contended that, in one major respect, the 10-5-3 proposal was quite *inefficient*. Non-residential commercial buildings, as distinguished from industrial buildings, though also eligible for this tax break, were said to contribute little if any to increased productivity. On this count at least, the British were more efficient, concentrating on machinery. Indeed, even an earlier labor government, not just Margaret Thatcher's, allowed a full deduction for the cost of machinery in the year of its acquisition.

[W]hile there is but *one* tax on distributed *interest*, there are *two* significant taxes on most *distributed* corporate profits, and this must be taken as a given fact however one otherwise feels about a complementary and arguable question: Who actually bears the economic burden of those two taxes?

Compared with our *existing* practice, the British provide an *enormous* tax break. But our own treasury's statisticians say that the "present value of the [ultimate] tax saving from the combination of the investment credit and [*this bills'*] accelerated deductions is greater than full, first year write-off would be."

Indeed, the enromous size of the ultimate fiscal impact of this proposal has to be the fourth but also the administration's most important concern. While the first-year cost in lost revenue was a modest $4 billion, according to the treasury's statisticians the *annual* revenue loss directly attributable to the resulting increase in deductions would reach $50 billion in 1984 and $85 billion in 1988.

The treasury does acknowledge that, by 1984, when the directly attributable revenue loss reaches only $50 billion, the consequently induced but necessarily lagging economic expansion by then also should have provided new revenue "feedbacks" on the order of $15 billion annually, the net revenue loss in that year being then only $35 billion.

Even so, the administration had to recognize the further probability that, in the end, this amount would represent *only* a *part* of the revenue loss. Why?

The answer is simple enough. In terms of *political feasibility*, this bill probably could not pass unless coupled also with at least some tax cut for individuals. Since the revenue "feedback" is bound to lag, the *magnitude* of the *two cuts together* obviously invites inflationary risks and jeopardizes governmental programs the administration favors.

Connable's Wholesale Alternative: Reagan's New Position

One of the two principal sponsors of the 10-5-3 bill—the politically astute ranking minority member of the House Ways and Means Committee—recognized a year ago that it might not be possible for *business* alone to have the whole cake.

Thus, as a possible alternative to his bill, he introduced HR 5050. It coupled his 10-5-3 depreciation arrangement with a variety of provisions cutting taxes on individuals, including a one-time approximately 10% reduction in marginal rates.

Senate Finance Committee re Supply Side's Depreciation

Something approaching whittled down versions of those two features—at much reduced costs in lost revenue—found their way into the previously mentioned Senate Finance Committee proposal that emerged last month.

On the *business* side, but only as to tangible *personal* property, not buildings, it proposed a "2-4-7-10" depreciation system designed around four open ended cost recovery accounts, in contrast to 10-5-3's more or less single or flat five year rule for such equipment.

Tangible personal property, according to the committee's bill, would be assigned to the particular recovery account which was *at least* 40% shorter than the current mid-point useful life under the present ADR system. For example, assets used to manufacture clothing have a current mid-point life of nine years which this bill would shorten to four years, i.e., the useful life would be telescoped by more than half, since assignment to the seven year class would not quite satisfy the "at least" feature in the "at-least-40%-reduction" rule.

Also as to tangible personal property, a declining balance method of 200%, 150%, or 100% could be elected on an annual basis.

And generally, on a disposition of some such assets, no gain or loss would be recognized; the disposition simply would operate to reduce the balance in the appropriate recovery account.

Public utilities would continue to use the present ADR system except that the ADR variance would b increased to 30%, from the present 20%.

Real property on the other hand could be depreciated, first, as now; second, over a shorter elective 20-year period but only if the taxpayer uses the straight line composite method or; third, if owner-occupied—over a 15-year period using a 150% declining balance method—but in such case the recapture rules applicable to personal property would apply.

Low-income rental housing also could invoke the 15-year period but in such case would be confined to the straight-line method.

Compared with existing practice, these proposals regarding real property would significantly reduce the cost recovery period but, over the long haul, not nearly in the degree which would result from enactment of 10-5-3's even shorter and flat *10-year-useful-life* rule.

Carter's Counter-Proposal re Depreciation

One week after the Senate Finance Committee reported out its depreciation plan, President Carter announced his plan.

In contrast to 10-5-3 which would be phased in over a five-year transition period, the plans of both the committee and the President would be triggered in *full* on January 1, 1980, thereby eliminating disincentives, i.e., eliminating any

incentive to postpone acquisitions so as to obtain a later phased-in more attractive depreciation arrangement.

The President's cost recovery system, labelled Constant Rate Depreciation (CRD), also was designed to avoid yet another consequence, common in this instance—though in different degrees—to both the Senate committee's proposal and the 10-5-3 plan. The Senate committee's system would distort normal competitive forces in our economy, though less so than 10-5-3, in that it would favor one industry over another. This would result because the committee proposes to compress *all* types of equipment into only four open ended accounts geared, respectively, to 2-4-7, and 10-year useful lives, with the particular account appropriate for the entire equipment of a given industry being dependent on which account would result in an "*at least*" 40% reduction in the currently applicable ADR useful life.

The President's plan seeks to avoid such discrimination, first, by having many more classes of assets (a separate class for each of 30 different industries) than the committee's four (though far fewer than ADR's present number—130). Second, though as to any given industry his plan would combine into one depreciation rate both the useful-life and method-of-depreciation factors, greater neutrality as between industries still would result because the plan contemplates that the appropriate rate for a given industry would be determined by reference to an across-the-board 40% reduction rule, using as a point of departure the most favorable depreciation rate now permitted a given industry under ADR.

Most taxpayers with respect to equipment would use only two accounts, one for common assets (such as vehicles and office furniture), and the other for equipment classified by industry (such as agriculture, construction, utilities, and various categories of manufacturing). All such assets purchased, new *and* used, would be added to one open-ended account for each class.

CRD would also apply to industrial and commercial buildings, with a separate account being maintained for each building.

Quite obviously, the President's proposal regarding depreciation is less generous to taxpayers and less costly in lost revenue than the Senate committee's plan.

Reagan Agrees with Senate Committee

For a time, it appeared that Mr. Reagan would support the yet even more costly 10-5-3 plan as an *addition* to his massive three-year 30% rate cut for individuals. More recently, however, releases from his campaign headquarters bearing on a depreciation plan have used revenue-loss figures which are identical to those associated not with 10-5-3, but with the Senate committee's depreciation proposal to which he still would tack on the large Kemp-Roth reduction for individuals.

Senate Committee and the President: Other Differences

However, in contrast to Mr. Reagan, both the Senate committee's and the President's plans include yet additional cuts for business over and above favorable depreciation changes; though here, too, there are differences between their respective proposals.

The President would add these three additional features:

First, a full 10% investment credit would become available for purchases of all new equipment having a useful life of more than one year, in contrast to the present graduated arrangement under which equipment must have a useful life of at least three years to qualify even for 1/3 of the existing 10% credit and must have a useful life of seven years to qualify fully.

Second, instead of accommodating a taxpayer's excess unused credits only by permitting a three-year-carryback and seven-year-carry-forward as now; he proposes further to aid firms experiencing cyclical downturns and newly organized or other rapidly growing firms by making *refundable* 30% of any post-1980 excess unused credits, with carrybacks and carryforwards applying to the remainder. The annual cost: $2.4 billion in calendar 1981.

Third and finally, at a further revenue cost not to exceed $1 billion annually, a new Targeted Investment Credit would be tacked on, permitting an *additional* 10% investment credit for qualifying investments for which, with an eye on declining and high unemployment areas, the Commerce Department agrees to issue certificates of necessity.

The Senate committee, to its 2-4-7-10 depreciation system, would add the following:

First, in the case of interior or exterior renovation, restoration, or re-construction depreciable costs incurred in connection with a building which has been in use for at least 20 years, the so-called rehabilitation tax credit would be increased from its present 10% figure to 25%.

Second, a new 25% *incremental* research and development tax credit would be allowed for research expenditures to the extent they exceeded similar average annual expenditures over a defined earlier base period. To minimize interpretative difficulties, both for this purpose and with reference to the presently allowed deduction for research expenditures, the latter would be defined essentially as they are now defined for accounting purposes by Financial Accounting Standards Board Statement No. 2.

Third, to the foregoing depreciation *and* credit provisions—involving a revenue loss of $10.4 billion for calendar '81—the committee would add corporate rate reduction costing another $1.5 billion in '81 and twice that in '82. Over a two-year transition period, the committee would revise the corporate rate structure by increasing the number of brackets to seven, the bottom bracket ultimately to be 15%, with the top—44% being applicable only to income exceeding $200,000.

Finally, corporations other than those engaged in rendering professional services (health, law, engineering, architecture, accounting, performing arts, or consulting), could accumulate a minimum $250,000 of earnings without running the risk of being charged with the present penalty tax which is applied when accumulated profits exceed the reasonable needs of a business.

Conclusions

In General

The foregoing recital leads me to conclude that among political leaders at the highest level, a consensus is emerging favoring at the least a fairly radical change in our depreciation practices. Even Mr. Anderson, who first and foremost calls for a balanced budget (because of his deep concern regarding inflation) calls—subject to that one limitation—for a fairly early shift in our depreciation practices toward an arrangement similar to that proposed by the Senate committee.

Second, while this consensus, fostering much more favorable depreciation practices, evolved during a pre-election campaign and, thus, also during what hopefully proves to be a temporary recession, the consensus itself is almost certain to survive both the election and even emergence from the recession, for the rhetoric of our political leaders, accompanying the consensus, emphasizes *not* the recession, but rather a different truth—the business

sector's *long-range* burden of improving productivity and of creating new additional jobs for an *expanding* labor force.

Third, given our high inflation rate (which knowledgeable persons tend to concede will be with us in significant degree for several years), it is far from clear, *even if Mr. Reagan is elected*, that a *post-election* Congress will agree to devote the lion's share of our deficit-generating tax-cutting capacity to tax cuts for *individual consumers*, as is contemplated by Kemp-Roth and currently by Mr. Reagan. For that Congress, with the election behind it and with a greater chance to be objective, will have drummed into it, day after day, facts about the enormously important function the business sector performs for our society and the difficulty *that* sector now faces in performing that awesome function at *acceptable* levels in this shrinking and ever more competitive world.

Fourth, neither is it clear, if our inflation rate remains relatively high for several years, that the size of the tax cuts which the "consensus" now envisages for the *business* sector will be sufficiently large to solve, almost alone, that sector's productivity and expansion problems. The point: If within a year or two, the growth in productivity remains unsatisfactory, expect yet another and probably more radical change in our tax system.

Why? As was suggested earlier, many factors (e.g., research, education, labor-management relationships, inflation, capital investments, and even mere attitudes) intertwine in constantly changing ways to affect our productivity and growth. Taxes, also indirectly a contributing factor, happen to be one of those most readily dealt with by a government otherwise disinclined to involve its bureaucracy more directly in managing the market-place. In consequence, if our productivity, etc., does not improve within a year or two, political leaders who bear responsibility for this nation's welfare will seize again on tax stimulants if only because of a reluctance to take the risk that the ship would right itself without some further alteration in the relevant rules which could affect its course. As they would see it, responsiveness to such national problems is in keeping with the stimulating function, the tradition, and the genetics of *all* law, and of the tax law in particular.

And among the alternatives likely to be considered at that time are two which until a month ago were favored for *immediate* implementation by the chairman of the House Ways and Means Committee—Al Ullman.

Until a month ago, he was backing his own proposed Tax Restructure Act of 1980. It called for steep cuts in Social Security taxes and in both individual and corporate income taxes—including in the latter case, *inter alia*, a major shift toward more generous depreciation practices which adds also to our previously mentioned consensus.

Included in the cut for *individuals* was a newly devised method for attacking the double taxation of distributed corporate profits, simultaneously providing a built-in compelling link assuring savings and capital investment. With the aim of enabling corporations to retain a larger part of their cash flow, any domestic corporation would be allowed to establish a plan under which any individual shareholder could elect to receive a dividend in the form of that corporation's newly issued stock rather than cash. An electing shareholder could exclude from income up to $1,500 ($3,000 in a married couple's joint return) of such stock dividends. Those dividend shares would have a zero basis but, if held for over one year, the shareholder on a later sale would enjoy capital gain treatment.

The restructuring which he contemplated until a month ago involved tax reductions of $115 billion. But to make up for that immense loss in revenue, he simultaneously proposed yet another savings or capital-fostering device—a new 10% value added tax.

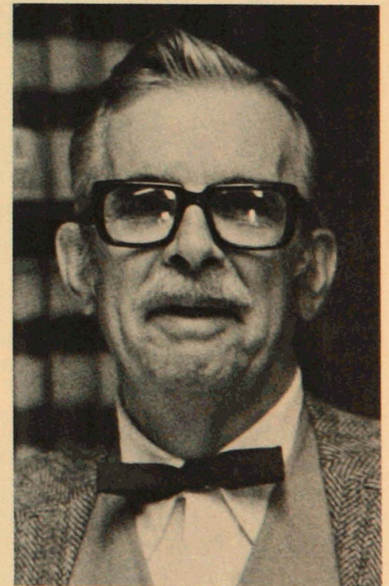
This latter type of levy contains a decided bias favoring capital formation, for in the end it applies only to acquisition of *consumers'* goods. But for that same reason, absent a compensating or ameliorating provision, this type of flat rate tax actually would be quite regressive. That portion of a taxpayer's income which is saved (invested) would be *excluded* from the tax base and, of course, taxpayers in higher income brackets save proportionately more of their incomes than those less fortunate.

Of course, to the extent the revenue from this tax was designed to replace Social Security tax revenues ($43 billion under this bill), we simply would be substituting one regressive tax for another. For the flat rate Social Security levy is also regressive in that it applies only to wages and then only up to a given amount. Excluded from the tax base is that part of a taxpayer's income which is derived from capital and this immunized part tends, proportionately, to increase as total income increases.

But to the extent value-added-tax revenues replace revenues previously produced by individual income taxes (here $40 billion), the new tax obviously would make our federal tax system as a whole less progressive than it now is. Mitigating, but not eliminating this, was the function of one provision in the Ullman bill which differed on this count from most European models. A zero rate would be applied to food, medical care, and certain educational services, as well as to housing.

Not irrelevant to this tax's future is the fact that Senator Long, chairman of the Senate Finance Committee, still says that he favors major restructuring, reducing significantly our reliance on income taxes, using value added taxes to replace the large revenues involved. But adoption of it, added this patient man, would have to be postponed, probably for several years, awaiting two circumstances: (1) education of the American people as to how the tax would work; and (2) demonstration to them that such a tax simply had to become an essential part of our savings or capital-fostering system.

To you, for being equally patient, my thanks. Otherwise, beyond the foregoing this deponent predicteth not.



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