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Domestic Credit by David Goldman

Donald Regan's tax turkey

Changing the rules, when the "recovery" hoax is visibly flaking apart, is like playing with matches near gasoline.

Treasury Secretary Donald Regan offered the President a belated Thanksgiving turkey on Nov. 27, in the form of a scheme to re-juggle the American tax system. The Treasury plan, advertised as a "simplification" of the tax code, will actually create a maximum of confusion and complications.

Regan's plan was represented in the press as if the White House had already rubber stamped it, although the President, in fact, has not had a chance to express a view on it. The treasury secretary, whose former colleagues in Wall Street have ganged up against the White House to demand cuts in the defense budget, is perfectly aware that Congress will not touch the new tax plan.

On the contrary, White House specialists suspect that Donald Regan has pulled a fast one: By proposing tax changes guaranteed to meet congressional rejection, he has thrown the entire burden of pressure back onto the spending side of the budget.

Don Regan showed his true colors on British television before the tax plan came out, hinting at defense budget cuts in a way he would not dare to do before an American audience. "Well, what we're saying is tax increases only as a last resort," Regan said on "The Business Program" of Britain's commercial Channel 4. Asked whether the cuts would include defense, Regan replied: "As far as the Defense Department is concerned, no."

But he noted that Congress had limited the real rate of growth in defense spending in 1983 and 1984. "I would suggest that that's an area that should be looked at," Regan said. His spokesman, Alfred Kingon, said Regan believes defense is a "legitimate area to be looked at for cuts."

In a related development, the Treasury Department leaked to the press that it had virtually ruled out a plan invented by Reagan hardliners to slap on a national sales tax of some kind in order to raise additional revenue to cover the budget deficit while maintaining a large volume of defense spending.

This ham-handed effort to preserve the defense budget was doomed to failure from the start. Not only had the President promised that there would be no tax increases, but the consumption-tax proposal would hit the sagging economy in its most vulnerable spot—consumer spending. Not surprisingly, the hardliners lost.

Having washed out the White House hardliners' plan for tax increases, the Treasury had to come up with its own program. The result is a mishmash which will spread confusion among corporations and investors for an indefinite period of time, as the Treasury plan goes slowly down the congressional meatgrinder.

The central features of the Treasury plan are:

- the elimination of important business investment deductions, including the Investment Tax Credit and accelerated write-offs of the depreciation cost of plant and equipment;
- taxation of various fringe benefits, unemployment insurance, as well as the elimination of the deduction for state and local income tax; and
- replacement of the 14 current tax brackets of 11% to 50% by three new brackets, at 15%, 25%, and 35%.

In and of themselves, none of the specific proposals matter. Accountants all over the country are telling their clients that the present Congress will not digest this turkey before it dissolves in 1986, and they are almost certainly correct.

However, the uncertainty of new tax rules hanging over the economy will, by itself, have an extremely negative impact. The Internal Revenue Service has recently displayed a bad habit of applying tax rules retroactively, and innumerable deals—particularly in real estate and related areas—will stay on the shelf until the dust settles.

What is ominous is that Donald Regan, the stage-manager of the phony "Reagan recovery," has now thrown a monkey wrench into the gears. The supposed recovery was a combination of statistical fraud, massive imports of goods and money, consumer credit expansion, and a tax subsidy (under the 1981 tax rules) for every sort of real-estate speculation imaginable.

In fact, the most devastating evidence that the economy has begun a nose dive is the "improvement" in the merchandise trade deficit during October. At $9.18 billion, the deficit was the lowest since June, due to a sharp contraction of imports of industrial goods, the major source of the deficit all year.

Imports fell 10.6% in October, despite an 11.4% rise of petroleum and related products; the fall was disproportionately larger for industrial goods, demand for which has apparently collapsed.

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