

Secretary FOWLER. No; in addition to the moral problem that you have properly referred to, there is the conventional wisdom that when you have a special temporary expenditure of the magnitude that this expenditure has now come to be it seems wise to pass special tax measures to fund at least a portion of that special temporary expense out of current revenues. It is a sensible way of dealing with a special and temporary expense.

Mr. BYRNES. Then last year, when you knew that Vietnam expenses were accelerating by some \$10 billion—practically doubling—would have been the time to propose a tax increase if you wanted the increase to coincide with the additional temporary expense.

Secretary FOWLER. Mr. Byrnes, I tried in my statement in discussing the special costs of Vietnam to indicate that we did in early 1966 relate the additional \$4 billion-plus increase over the fiscal 1965 cost to the Tax Adjustment Act and that when it appeared, as my statement indicates, later on in the year that the expenses in Vietnam would be double the \$10 billion, we did decide that it would be necessary to try to fund some additional portion of that.

That was the genesis of the 6-percent surcharge request, but given the condition of the economy, the inventory readjustment Chairman Ackley has described, which was then facing us, the additional tax increase to meet that part of the cost to that degree was scheduled for a July 1 date rather than a January 1 date.

Mr. BYRNES. So you can have some increase in temporary costs without asking for a tax increase. But I don't think this rationale leads either one of us down the right road.

Another item you mentioned as the basis of the tax increase is the inflationary pressures that will result if we don't have a tax increase and cut back expenditures.

I am glad to see that you have generally tied the tax increase to expenditure reductions in your statement.

Secretary FOWLER. Oh, much more than that, Mr. Byrnes. Conceptually, they are wedded.

Mr. BYRNES. I want to go into that and see how closely they are tied together. One of the reasons for this tax increase is inflationary pressures that this kind of a deficit produces; is that correct?

Secretary FOWLER. The pressures that running this kind of a deficit could produce given the kind of an economy that we have today.

Mr. BYRNES. All right. The Chairman has explored the economic indexes in some detail in order to determine whether a tax increase is appropriate to the state of the economy. I would like to read from a letter I received from a Member of the other body and get your general comments on it. It says:

If we leave out the food component of the Consumer Price Index (on the ground that it is subject to its own particular cycle and not general demand) then prices have risen more this year than they did in the same period last year in spite of the fact that the demand is not nearly as strong as it was in 1966. The basic reason for this phenomenon is that services constitute the major element of the price increase in both years, especially medical care. Medical care has been going up for many years, and most other services tend to rise with wage rates. I can see very little relationship between price increase and general demand, at least in the short run. Yet it is widely cited as one of the principal reasons for tax action. Actually our economy is not operating at or near capacity. Capacity utilization is down to 85 percent. Unemployment is at four percent and the work week is the lowest in six years. Our economy could withstand a substantial increase in demand without overextending itself.