

"Realistic depreciation alone, however, is not enough to provide the essential economic growth. In addition, a specific incentive must be provided if a higher rate of growth is to be achieved. . . . The objective of the investment credit is to encourage modernization and expansion of the Nation's productive facilities and thereby improve the economic potential of the country, with a resultant increase in job opportunities and betterment of our competitive position in the world economy."⁴

QUESTION OF MANIPULATION

It will be recalled that the initial reaction to the investment credit proposal was critical, and even hostile, in many quarters. There were a variety of reasons, only one of which concerns us here. It was charged that once in effect the credit would inevitably be manipulated for economic control purposes.

This charge was indignantly denied by the Administration. Its spokesmen insisted that the credit was designed to be a permanent feature of the tax system, that its purpose was to raise the average level of investment over the long pull, and that there was no intent to employ it as a contracyclical device. As for the Congress, the legislative history strongly suggests that it concurred in the Administration position.⁵

At the time the credit was proposed (1961), and enacted (1962), no one was worrying about excessive capital investment. The whole drive was for expansion. Any possible need for restrictive action was obviously far in the future, and except for the Administration assurances just referred to the problem was treated as academic.

RECENT DEVELOPMENTS

We cite this historical record to indicate the original concept and purpose of the investment credit. But conditions have changed radically since then, and the question is now before us of withdrawing or suspending the credit as a means of curbing a capital goods boom in an overheated economy.

Last January Senator Gore introduced a bill (S. 2806) calling for the outright repeal of the credit. Later he proposed an amendment to the Tax Adjustment Act of 1966 suspending it for two years (rejected by the Senate on March 8). Shortly thereafter, the Joint Economic Committee recommended immediate suspension to a future date prescribed by Congress. Numerous economists, including three former chairmen of the Council of Economic Advisers, have joined in urging suspension, usually for a one-year period. Several bills directed to this objective have been introduced in Congress. Recently the Chairman of the Senate Finance Committee, Senator Long, proposed an amendment to the Foreign Investors Tax Act of 1966 (H.R. 13103), providing for indefinite suspension.⁶ Still more recently, the Administration has proposed suspension for 16 months (H.R. 17607).

PRESENT PROJECT

In view of this altered situation, it is an appropriate time to consider the basic question of the merits of the investment credit as any economic control device. Is it suitable for on-and-off application? This question is the subject of the present inquiry.

It is a safe guess that most of the proponents of on-and-off application have not thought through the problems to which it gives rise, if indeed they are even aware of them. They involve questions of fairness, administrative feasibility, timing, and effectiveness. We suggest that until these questions have been confronted it is irresponsible to urge manipulation, whether by temporary suspension or otherwise.

Since temporary suspension appears to be the most favored form of manipulation, we propose to consider the difficulties associated with that form. Because they are somewhat different at the suspension (cut-out) phase of the operation than at restoration (cut-in), we shall discuss the two phases separately, beginning with suspension.

1. PROBLEMS ASSOCIATED WITH SUSPENSION

As a rule, capital equipment has a long production period. Moreover, a large proportion is produced on order. This means that customers must wait during its fabrication, and that there is normally an extended period between the place-

⁴ Report of the Senate Finance Committee on the Revenue Act of 1962, p. 11.

⁵ Witness the committee reports quoted earlier.

⁶ *Cong. Rec.*, August 30, 1966, p. 20321.