FROM: Phyllis Schlafly

68 FAIRMOUNT, ALTON, ILLINOIS 62002 / (618)462-5415

RELEASE: FEBRUARY 18, 1983

CAPITAL GAINS ROLLOVER

Federal tax statutes are not merely a means of raising government revenue. Their built-in incentives and disincentives provide powerful inducements -- even coercions -- to motivate/compel Americans to spend their money in certain ways.

The Tax Reform Act of 1969 contained a powerful inducement to Americans to stop investing in equity securities. In effect, the Act's provisions said: Hereafter, if you invest successfully, you will be taxed twice as much; if you invest unsuccessfully, you can write off only half your losses; if you borrow money to invest, you cannot deduct all the interest paid on borrowed funds.

The reaction of American investors was prompt. Prior to that Act, the number of American shareholders had been increasing by 7% a year. Immediately, this trend reversed itself and the number of shareholders decreased by 6-1/2% a year.

More than ten million Americans simply stopped investing in equity securities between 1969 and 1975. This cost the United States some $104 billion in equity capital -- enough to create four million jobs.

This flight from equity investment cut in half the price/earnings ratio of the top 500 industrial companies. This flight from equity investment drove the cost of capital investment up so high that most investments simply could not be made.

Since investment is the primary factor in improving productivity, it is clear why our productivity is suffering.

Dr. William F. Ballhaus, president of Beckman Instruments, Inc., and a keen observer of economic trends, pointed out in speeches that this 1969 law "upset the delicate natural balance between investment and consumption by doubling the risk/reward ratio for investment." When statutory incentives penalized investment and rewarded consumption, billions of dollars were diverted from investment (which creates real economic growth) into consumption (which promotes inflation and exhausts economic resources).

This 1969 tax law severely restricted the mobility of capital -- the ability to

change funds from one investment to another. If you sold one investment, you had to pay a very large capital gains tax before putting your funds into another investment; therefore, you needed to double your rate of return in the new investment in order to justify the switch as a good risk.

The number of companies raising new equity capital dropped from 1,800 in 1969 to 150 in 1975. The number of small companies seeking equity capital dropped from 649 to 9. Since small companies are the principal source of new jobs and innovative technologies and products, this halting of small-company growth was devastating to our economy.

The 1978 tax law took a step in the direction of correcting the problem by reducing maximum capital gains tax rates from 49% to 28%, and by raising the capital gains exemption from 50% to 60%. This was only a start; we have a long way to go.

Dr. Ballhaus makes a persuasive case for a statute that would allow capital investment rollover. That means we would defer all taxes on capital gains from securities until the investor stops investing in securities issued by domestic corporations, at which time the profit would be taxed at capital gains rates (or at averaged earned income rates).

He also recommends that we allow the private investor to write-off all his capital losses against other income, and also to allow full write-off of interest costs on funds borrowed for investment (except for investment in tax-free government securities).

Would this promote investment? You bet it would. With tax considerations removed from long-term investment decisions, the risk/reward ratios would be significantly better, and capital formation and mobility would be increased.

The benefits to our economy would be even more dramatic than the benefits to individual investors. Investment creates jobs by creating new businesses and by expanding established ones. Capital rollover would create three times as many jobs as were created annually under the 1978 law and four times as many as under the 1969 tax law.

The taxes generated by workers holding new jobs would be double the tax revenues generated by the 1978 tax law, and triple the tax revenues created under the 1969 law. Every dollar invested in equities produces two to three times as much in Federal taxes as a dollar spent on consumption.

Since other plans to lift America out of depression haven't worked, it's time to try capital rollover.