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ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 1998–2002

PREPARED FOR THE

HOUSE COMMITTEE ON WAYS AND MEANS

AND THE

SENATE COMMITTEE ON FINANCE

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This report[1] on tax expenditures for fiscal years 1998–2002 is prepared by the staff of the Joint Committee on Taxation ("Joint Committee staff") for the House Committee on Ways and Means and the Senate Committee on Finance. The report also is submitted to the House and Senate Committees on the Budget.

As in the case of earlier reports,[2] the estimates of tax expenditures in this report were prepared in consultation with the staff of the Office of Tax Analysis in the Treasury Department ("the Treasury"). The Treasury published its estimates of tax expenditures for fiscal years 1996–2002 in the Administration's budgetary statement of February 1997.[3] The lists of tax expenditures in this Joint Committee staff report and the Administration's budgetary statement overlap considerably; the differences are discussed in Part I of this report under the heading "Comparisons with Treasury."

The Joint Committee staff has made its estimates (as shown in Table 1) based on the provisions in tax law as enacted through December 12, 1997. Expired or repealed provisions are not listed unless they have continuing revenue effects that are associated with ongoing taxpayer activity. Proposed extensions or modifications of expiring provisions are not included until they have been enacted into law.

Part I of this report contains a discussion of the concept of tax expenditures. Part II is a discussion of the measurement of tax expenditures. Estimates of tax expenditures for fiscal years 1998-2002 are presented in Table 1 in Part III. Table 2 shows the distribution of tax returns by income class, and Table 3 presents distributions of selected individual tax expenditures by income class.

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[1] This report may be cited as follows: Joint Committee on Taxation, *Estimates of Federal Tax Expenditures for Fiscal Years 1998–2002* (JCS–22–97), December 15, 1997.

[2] Joint Committee on Taxation, *Estimates of Federal Tax Expenditures*, October 4, 1972, June 1, 1973, July 8, 1975, March 15, 1976, March 16, 1977, March 14, 1978, March 15, 1979, March 6, 1980, March 16, 1981, March 8, 1982, March 7, 1983, November 9, 1984, April 12, 1985, March 1, 1986, February 27, 1987, March 8, 1988, February 28, 1989, March 9, 1990, March 11, 1991, April 24, 1992, April 22, 1993, November 9, 1994, September 1, 1995, and November 26, 1996.

[3] Office of Management and Budget, "Tax Expenditures," *Budget of the United States Government: Analytical Perspectives, Fiscal Year 1998*, February 6, 1997, pp. 71–98.

I. THE CONCEPT OF TAX EXPENDITURES

Overview

"Tax expenditures" are defined under section 3(3) of the Congressional Budget and Impoundment Control Act of 1974 ("the Budget Act") as "revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability."[4] Thus, tax expenditures include any reductions in individual and corporate income tax liabilities that result from special tax provisions or regulations that provide tax benefits to particular taxpayers.

Special income tax provisions are referred to as tax expenditures because they are considered to be analogous to direct outlay programs, and the two can be considered as alternative means of accomplishing similar budget policy objectives. Tax expenditures are most similar to those direct spending programs that have no spending limits, and that are available as entitlements to those who meet the statutory criteria established for the programs.[5]

Estimates of tax expenditures are prepared for use in budget analysis. They are a measure of the economic benefits that are provided through the tax laws to various groups of taxpayers and sectors of the economy. The estimates also may be useful in determining the relative merits of achieving specified public goals through tax benefits or direct outlays.

The legislative history of the Budget Act indicates that tax expenditures are to be defined with reference to a normal income tax structure (referred to here as "normal income tax law"). The Joint Committee staff has used its judgment in distinguishing between those income tax provisions (and regulations) that can be viewed as a part of normal tax law and those special provisions that result in tax expenditures. A provision traditionally has been listed as a tax expenditure by the Joint Committee staff if there is a reasonable basis for such classification and the provision results in more than a de minimis revenue loss, which solely for this purpose means a total revenue loss of at least $50 million over the five fiscal years 1998–2002. The Joint Committee staff emphasizes, however, that in the process of listing tax expenditures, no judgment is made, nor any implication intended, about the desirability of any special tax provision as a matter of public policy.

If a tax expenditure provision were eliminated, Congress might choose to continue financial assistance through other means rather than terminate all Federal assistance for the activity. If a replace-

[4] Congressional Budget and Impoundment Control Act of 1974 (P.L. 93–344), sec. 3(3).

[5] There are a few tax expenditures that have statutorily imposed limits. One example is the tax credit for low-income rental housing. This credit is available only to those who have received credit allocations from State housing authorities. There are statutory limits on the total amounts of credit allocations that the States can make each year.

ment spending program were enacted, the higher revenues received as a result of the elimination of a tax expenditure might not represent a net budget gain. A replacement program could involve direct expenditures, direct loans or loan guarantees, a different form of tax expenditure, or a general reduction in tax rates. Joint Committee staff estimates of tax expenditures do not anticipate such policy responses.

The Budget Act uses the term tax expenditure to refer to the special tax provisions that are contained in the Federal individual and corporate income taxes. Other Federal taxes such as excise taxes, employment taxes, and estate and gift taxes may also have exceptions, exclusions, and credits, but those special tax provisions are not included in this report because they are not part of the income tax. Thus, for example, the income tax exclusion for employer-paid health insurance is included, but the Federal Insurance Contributions Act (FICA) tax exclusion for employer-paid health insurance is not treated as a tax expenditure.[6]

Some provisions in the Internal Revenue Code provide for special tax treatment that is less favorable than normal tax law. Examples of such provisions include (1) the denial of deductions for certain lobbying expenses, (2) the denial of deductions for certain executive compensation, and (3) the 2-percent floor on itemized deductions for unreimbursed employee expenses. Tax provisions that provide treatment less favorable than normal law are not shown in this report because they are not included in the statutory definition of a tax expenditure.

Individual Income Tax

Under the Joint Committee staff methodology, the normal structure of the individual income tax includes the following major components: one personal exemption for each taxpayer and one for each dependent, the standard deduction, the existing tax rate schedule, and deductions for investment and employee business expenses. Most other tax benefits to individual taxpayers can be classified as exceptions to "normal income tax law."

Personal exemptions and the standard deduction are treated as part of normal income tax law because one may consider these amounts as approximating the level of income below which it would be difficult for an individual or a family to obtain minimal amounts of food, clothing, and shelter. Those itemized deductions that are not necessary for the generation of income are classified as tax expenditures, but only to the extent that they exceed the standard deduction level.

Under present law, all employee compensation is subject to tax unless the tax code contains a specific exclusion for the income. There are specific exclusions for the following employer-provided

[6] In its budget statement, the Treasury Department identifies tax expenditures in the Unified Transfer Tax (the estate and gift tax and the generation-skipping transfer tax). See, Office of Management and Budget, "Tax Expenditures," pp. 96–98. Other analysts have explored applying the concept of tax expenditures to the payroll and excise taxes. See, Jonathan Barry Forman, "Would a Social Security Tax Expenditure Budget Make Sense?" *Public Budgeting and Financial Management*, 5, 1993. 311–335, and Bruce F. Davie, "Tax Expenditures in the Federal Excise Tax System," *National Tax Journal*, XLVII, March 1994, pp. 39–62.

benefits: health insurance and medical care,[7] accident and disability insurance, group term life insurance, educational assistance, transportation benefits (parking, van pools, and transit passes, subject to certain limits), child care, meals and lodging (furnished for the convenience of the employer), employee awards, death benefits, and other miscellaneous fringe benefits (e.g., employee discounts, services provided to employees at no additional cost to employers, tuition reductions, and de minimis fringe benefits). Each of these exclusions is classified as a tax expenditure in this report.

Under normal income tax law, employer contributions to pension plans and income earned on pension assets would be taxable to employees as the contributions are made and as the income is earned, and employees would not receive any deduction or exclusion for their pension contributions. Under present law, employer contributions to qualified pension plans and employee contributions made at the election of the employee through salary reduction are not taxed until distributed to the employee during retirement, and income earned on pension assets is not taxed until distributed during retirement. The tax expenditure for "net exclusion of pension contributions and earnings" is computed as the taxes forgone on current tax-excluded pension contributions and earnings less the taxes paid on current pension distributions to retirees.

Under present law, social security retirement benefits are fully or partially excluded from gross income.[8] Under normal income tax law, retirees would be entitled to an exclusion for only the portion of social security retirement benefits that represents a return of the social security taxes that they paid during their working years. Thus, the exclusion of social security retirement benefits in excess of social security tax payments is classified as a tax expenditure.

All Medicare benefits are excluded from taxation. The value of Medicare Part A insurance generally is greater than the Health Insurance (HI) tax contributions that enrollees made during their working years, and the value of Medicare Part B insurance generally is greater than the Part B premium that enrollees must pay. The exclusion of the value of Medicare Part A insurance in excess of HI tax contributions is classified as a tax expenditure, and the exclusion of the value of Medicare Part B insurance in excess of premiums paid also is classified as a tax expenditure.

Public assistance benefits are excluded from gross income by law or by Internal Revenue Service regulations. Table 1 contains tax expenditure estimates for workers' compensation benefits, special benefits for disabled coal miners, and cash public assistance benefits (which include Supplemental Security Income (SSI) benefits and Aid to Families with Dependent Children (AFDC) benefits).

The individual income tax does not include in gross income the imputed income that individuals receive from the services provided

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[7] Present law contains an exclusion for employer-provided health care and health insurance for employees (sec. 106) and an exclusion for benefits received by employees under an employer-subsidized health plan (sec. 105(b)). These two exclusions are viewed as a single tax expenditure. Under normal income tax law, the value of employer-provided health insurance would be includable in the income of employees, but employees would not be subject to tax on any health insurance benefits (reimbursements) that they might receive under an employer-provided health insurance plan.

[8] For taxpayers with modified adjusted gross incomes above certain levels, up to 85 percent of social security retirement benefits are includable in income.

by owner-occupied homes and durable goods.[9] However, the Joint Committee staff does not classify this exclusion as a tax expenditure. The measurement of imputed income for tax purposes presents administrative problems and its exclusion from taxable income may be regarded as an administrative necessity.[10]

Under normal income tax law, individuals would be allowed to deduct only the interest on indebtedness incurred in connection with a trade or business or an investment. Thus, the deduction for mortgage interest on a principal or second residence is classified as a tax expenditure.

The Joint Committee staff assumes that, for administrative feasibility, normal income tax law would tax capital gains in full in the year the gains are realized through sale or exchange. Thus, the deferral of tax until realization is not classified as a tax expenditure, but reduced rates of tax, further deferrals of tax (beyond the year of sale or exchange), and exclusions of certain capital gains are classified as tax expenditures.

It is also assumed that normal income tax law would not provide for any indexing of the basis of capital assets for changes in the general price level. Thus, under normal income tax law (as under present law), the income tax would be levied on nominal gains as opposed to real gains in asset values. If, as an alternative, normal income tax law were defined to include full indexing of the basis of capital assets, the capital gains tax expenditure estimates in Table 1 generally would be much lower than those shown.

There are many types of State and local government bonds and private purpose bonds that qualify for tax-exempt status for Federal income tax purposes. Table 1 contains a separate tax expenditure listing for each type of bond.

Business Income Taxation

Regardless of the legal form of organization (sole proprietorship, partnership, or S or C corporation), the same general principles are used in the computation of taxable business income. Thus, most business tax expenditures apply equally to unincorporated and incorporated businesses.

One of the most difficult issues in defining tax expenditures for business income relates to the tax treatment of capital costs. Under present law, capital costs may be recovered under a variety of alternative methods, depending upon the nature of the costs and the status of the taxpayer. For example, investments in equipment and structures may qualify for tax credits, expensing, accelerated depreciation, or straight-line depreciation. The Joint Committee staff generally classifies as tax expenditures cost recovery allowances that are more favorable than those provided under the alternative depreciation system (sec. 168(g)), which provides for straight-line

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[9] The National Income and Product Accounts include estimates of this imputed income. The accounts appear in U.S. Department of Commerce, Bureau of Economic Analysis, *Survey of Current Business*, published monthly.

[10] If the imputed income from owner-occupied homes were included in adjusted gross income, it would be proper to include all mortgage interest deductions and related property tax deductions as part of the normal income tax structure, since interest and property tax deductions would be allowable as a cost of producing imputed income. It also would be appropriate to allow deductions for depreciation and maintenance expenses for owner-occupied homes.

recovery over tax lives that are longer than those permitted under the accelerated system.

As indicated above, the Joint Committee staff assumes that normal income tax law would not provide for any indexing of the basis of capital assets. Thus, normal income tax law would not take into account the effects of inflation on tax depreciation. The expensing and depreciation tax expenditure estimates in Table 1 are larger than would be the case if normal income tax law provided for inflation adjustments in the basis of assets for tax depreciation purposes.

The alternative minimum tax ("AMT") and the passive activity loss rules are not viewed by the Joint Committee staff as a part of normal income tax law. Instead, they are viewed as provisions that reduce the magnitude of the tax expenditures to which they apply. For example, the AMT reduces the value of business tax credits (for those taxpayers subject to the AMT) by not allowing the tax credits to be claimed in the calculation of AMT liability. Similarly, the passive loss rules defer otherwise allowable deductions and credits from passive activities until a time when the taxpayer has passive income or disposes of the assets associated with the passive activity. Exceptions to the AMT and the passive loss rules are not classified as tax expenditures by the Joint Committee staff because the effects of the exceptions already are incorporated in the estimates of related tax expenditures.

Corporate Income Tax

The income of corporations (other than S corporations) generally is subject to the corporate income tax. The corporate income tax includes a graduated tax rate schedule. The lower tax rates in the schedule are classified by the Joint Committee staff as a tax expenditure (as opposed to normal income tax law) because they are intended to provide tax benefits to small business and, unlike the graduated individual income tax rates, are unrelated to concerns about ability of individuals to pay taxes.

Certain income of pass-through entities is exempt from the corporate income tax. The income of sole proprietorships, S corporations, and most partnerships is taxed at the individual level. The special tax rules for these pass-through entities are not classified as tax expenditures because the tax benefits are available to any entity that chooses to organize itself and operate in the required manner in order to avoid the entity-level tax.

Nonprofit corporations that satisfy the requirements of Code section 501 also generally are exempt from corporate income tax. The tax exemption of certain nonprofit cooperative business organizations, such as trade associations, is not treated as a tax expenditure for the same reason applicable to for-profit pass-through business entities. With respect to other nonprofit organizations, such as charities, tax-exempt status is not classified as a tax expenditure because the nonbusiness activities of such organizations generally must predominate and their unrelated business activities are subject to tax. In general, the imputed income derived from nonbusiness activities conducted by individuals or collectively by certain nonprofit organizations is outside the normal income tax base. However, the ability of donors to such non-profit organizations to

claim a charitable contribution deduction is a tax expenditure (because such contributions do not generate income to the donor), as is the exclusion from income granted to holders of tax-exempt financing issued by charities.

Taxpayer Relief Act of 1997

The Taxpayer Relief Act of 1997 ("the Act") (H.R. 2014), signed by the President on August 5, 1997 (P.L. 105–34), adds a number of new tax expenditures to the Internal Revenue Code and modifies a number of existing tax expenditures. The following is a summary of the tax expenditure provisions in the Act.

Child tax credit

The Act provides a new tax credit for taxpayers with qualifying children under the age of 17. The credit is $400 per child for taxable years beginning in 1998 and $500 per child in succeeding taxable years. The total amount of each taxpayer's child credit is phased out at a rate of $50 for each $1,000 of modified adjusted gross income in excess of certain thresholds ($110,000 for married taxpayers filing joint returns, $55,000 for married taxpayers filing separate returns, and $75,000 for taxpayers filing as single or head of household). The credit is nonrefundable for taxpayers with one or two children but refundable for taxpayers with three or more children.

Education tax incentives

The Act contains two new tax credits for tuition and fees for post-secondary education. The HOPE credit is equal to 100 percent of the first $1,000 and 50 percent of the next $1,000 of qualified tuition and fees paid during the year on behalf of a student enrolled in a post-secondary degree program on at least a half-time basis. The credit is available only during the first two years of a student's post-secondary education. The Lifetime Learning credit is equal to 20 percent of qualified tuition and fees paid during the year on behalf of a student who is taking one or more undergraduate or graduate-level classes to acquire or improve job skills. For purposes of the Lifetime Learning credit, qualified tuition is limited to $5,000 per tax return for expenses paid before January 1, 2003, and $10,000 per tax return for expenses paid after that date. The HOPE credit is available for expenses paid after December 31, 1997, and the Lifetime Learning credit is available for expenses paid after June 30, 1998. In Table 1, the HOPE credit and Lifetime Learning credit have been combined into a single tax expenditure estimate for "tax credits for tuition for post-secondary education."

The Act also provides that taxpayers may establish trust or custodial accounts ("education IRAs") for the exclusive purpose of paying the qualified higher education expenses of a named beneficiary. Annual contributions are limited to $500 per beneficiary and are also subject to income limits based on the incomes of the contributors. Earnings on contributions to the accounts are not subject to tax. Distributions from the accounts may be excludable from gross income to the extent that they do not exceed the qualified education expenses of the beneficiary. The accounts may be established in taxable years beginning after December 31, 1997.

The Act also provides an above-the-line deduction for interest on qualified higher education loans. The maximum deduction is $1,000 in 1998, $1,500 in 1999, $2,000 in 2000, and $2,500 in 2001 and succeeding years. The deduction is allowed only with respect to interest paid on a qualified loan during the first five years in which interest payments are required. The provision is effective for interest payments due and paid after December 31, 1997.

The HOPE tax credit, the Lifetime Learning tax credit, the maximum $500 contribution to education IRAs, and the deduction for interest on qualified education loans are all phased out for taxpayers with modified adjusted gross incomes in excess of certain limits. Elections to use the HOPE credit, Lifetime Learning credit, and exclusion from gross income for education IRA contributions are mutually exclusive in the sense that a taxpayer may not benefit from more than one of these three provisions in a taxable year with respect to a given student.

Present and prior law provided for a deferral of tax on the earnings of qualified State tuition programs for post-secondary education and tax-exempt status for such programs. The Act extends these tax benefits to State tuition programs that are used to prepay (or save) for room and board expenses as well as tuition expenses. The Act also broadens the definition of educational institutions eligible to participate in qualified State tuition programs, and liberalizes the rules on tax-free rollovers of credits and account balances in such programs. In general, these changes are effective after December 31, 1997.

Prior law contained an exclusion for employer-provided assistance for undergraduate and graduate education. The exclusion for employer-provided assistance for undergraduate education expired for courses of instruction beginning after June 30, 1997, and the exclusion for assistance for graduate-level education expired for courses beginning after June 30, 1996. The Act extends the exclusion for employer-provided undergraduate assistance to include courses beginning before June 1, 2000. The exclusion for employer-provided graduate-level assistance was not extended.

The Act also liberalizes the rules governing individual retirement arrangements to allow penalty-free withdrawals for qualified higher education expenses of the taxpayer and the taxpayer's spouse, children, and grandchildren. The provision is effective for withdrawals made after December 31, 1997, for education paid for and furnished after such date. (The effects of this provisions are reflected in the tax expenditure estimate for "individual retirement plans" in Table 1.)

The Act also provides a tax credit to certain financial institutions holding "qualified zone academy bonds" that will be issued by State and local governments to finance improvements at qualifying public schools in empowerment zones, enterprise communities, and other areas. The provision is effective for bonds issued after 1997.

The Act also provides an augmented charitable contribution deduction for computer technology and equipment donated by C corporations to elementary and secondary schools. The provision is effective for contributions made in taxable years beginning after 1997 and before January 1, 2001. (The effects of this provision are

reflected in the tax expenditure estimate for "deduction for charitable contributions to educational institutions" in Table 1.)

Individual retirement arrangements

The Act contains a number of changes in the rules governing the tax treatment of individual retirement arrangements ("IRAs"). First, the Act increases the income ranges over which the $2,000 IRA deduction limit is phased out for individuals who are active participants in an employer-sponsored retirement plan. Under the Act, the phaseout ranges are increased each year until the phaseout range for single taxpayers is $50,000 to $60,000 of adjusted gross income (in 2005) and the phaseout range for married taxpayers is $80,000 to $100,000 (in 2007). Second, the Act permits deductible contributions of up to $2,000 per year for spouses of individuals who participate in an employer-sponsored retirement plan. This deduction is phased out for taxpayers with adjusted gross incomes between $150,000 and $160,000. Third, the Act creates a new, tax-free nondeductible IRA called the "Roth IRA." The maximum contribution to a Roth IRA is $2,000 per year, and it is phased out for single taxpayers with adjusted gross incomes between $95,000 and $110,000 and married taxpayers with adjusted gross incomes between $150,000 and $160,000. Distributions of contributions to a Roth IRA are always tax free. Distributions of earnings from a Roth IRA are tax free if made more than five years after the Roth IRA has been established and if the distributions are made after age 59½, or on account of death or disability, or for first-time homebuyer expenses up to $10,000. Individuals with adjusted gross incomes of $100,000 or less may convert an IRA into a Roth IRA. Fourth, the Act permits penalty-free withdrawals from all IRAs for qualified higher education expenses (discussed above under "education tax incentives") and up to $10,000 of first-time homebuyer expenses. The effects of all of these provisions are reflected in the tax expenditure estimate for "individual retirement plans" in Table 1. Education IRAs are viewed as a separate tax expenditure and are listed separately in Table 1 along with other tax expenditures for education and training.

Capital gains provisions

The Act contains a number of changes in the tax treatment of capital gains. First, the maximum tax on the net capital gain of an individual is reduced from 28 percent to 20 percent, and any net capital gain which otherwise would be taxed at 15 percent is taxed at 10 percent. However, the maximum tax on the portion of any long-term net gain from the sale or exchange of real estate that is attributable to depreciation is reduced from 28 to 25 percent, and the maximum tax on any long-term net gain from the sale or exchange of collectibles remains at 28 percent. These changes are effective for sales or exchanges after May 6, 1997. For taxable years beginning after December 31, 2000, and assets which are held more than five years, the maximum capital gains tax rates will be 8 percent and 18 percent rather than 10 percent and 20 percent. In general, the lower capital gains tax rates do not apply to assets held for 18 months or less, and the maximum tax rate of 28 percent remains applicable to assets held more than one year but not more

than 18 months. The effects of all of these provisions are reflected in the tax expenditure estimate for "reduced rates of tax on long-term capital gains" in Table 1.

The Act also changes the tax treatment of gains on the sale of a principal residence. Under the Act, a taxpayer generally is able to exclude up to $250,000 (single taxpayers) or $500,000 (married taxpayers filing joint returns) of gain realized on the sale or exchange of a principal residence. The exclusion is allowed each time a taxpayer meets the eligibility requirements, but generally no more frequently than once every two years. The provision is effective for sales or exchanges occurring after May 6, 1997. This tax expenditure is listed as "exclusion of capital gains on sales of principal residences" in Table 1. It replaces two tax expenditure provisions from prior law, the "deferral of capital gains on sales of principal residences," and "exclusion of capital gains on sales of principal residences for persons aged 55 and over ($125,000 exclusion)," which are no longer listed in Table 1.

District of Columbia tax incentives

The Act designates certain economically depressed census tracts within the District of Columbia as the "D.C. Enterprise Zone." Businesses in this zone are eligible for special tax incentives including a wage credit for wages paid to D.C. residents, additional expensing of qualified zone property, and special tax-exempt financing for certain zone facilities. The enterprise zone designation and associated tax incentives are effective for the period January 1, 1998, through December 31, 2002. In addition, the Act provides a zero-percent capital gains tax rate for capital gains from the sale of qualified assets that are purchased during the five-year enterprise zone designation period, located in District of Columbia census tracts having a poverty rate of 10 percent or more, and held for more than five years.

The Act also provides a tax credit of up to $5,000 to first-time homebuyers of a principal residence in the District of Columbia. The credit is phased out for taxpayers with adjusted gross incomes above certain levels. The credit is available for property purchased after the date of enactment (August 5, 1997) and prior to January 1, 2001.

Empowerment zone tax incentives

The Act contains a number of changes to the rules governing empowerment zones. First, the Secretary of Housing and Urban Development is authorized to designate two additional empowerment zones in urban areas that generally will be eligible for the same tax incentives (wage credit, additional expensing, and special tax-exempt financing) that are now provided to the empowerment zones authorized by the Omnibus Budget Reconciliation Act of 1993. The two empowerment zones must be designated within 180 days after enactment (August 5, 1997), but the designations will not take effect before January 1, 2000. Second, the Secretaries of Housing and Urban Development and Agriculture are authorized to designate 20 additional empowerment zones (no more than 15 in urban areas and no more than five in rural areas), under slightly expanded eligibility criteria, which will be eligible

for additional expensing and special tax-exempt financing but not the wage credit. The 20 additional empowerment zones are to be designated prior to January 1, 1999. Third, the Act liberalizes the requirements that enterprise zone businesses must satisfy to be eligible for the various tax incentives, effective for taxable years beginning on or after the date of enactment (August 5, 1997). Fourth, the Act allows "new empowerment zone facility bonds" to be issued for qualifying businesses in the 20 additional empowerment zones, and makes certain modifications to the rules governing special tax-exempt bond financing in all empowerment zones and enterprise communities. Fifth, the Act liberalizes the criteria for designation of empowerment zones and enterprise communities in the States of Alaska and Hawaii. The effects of all of these changes are reflected in the tax expenditure estimate for "empowerment zone tax incentives" in Table 1.

Other new tax expenditure provisions

The Act creates a new welfare-to-work tax credit for employers of qualified individuals who are recipients or former recipients of long-term family assistance (AFDC or its successor program). The credit is equal to 35 percent of the first $10,000 of eligible wages in the first year of employment and 50 percent of the first $10,000 of wages in the second year of employment. The credit is effective for wages paid or accruing to a qualified individual who begins work for an employer on or after January 1, 1998, and before May 1, 1999.

The Act also provides that individual taxpayers may compute their current year regular tax liability by averaging, over the prior three-year period, all or a portion of their taxable income from the trade or business of farming. The provision applies to taxable years beginning after December 31, 1997, and before January 1, 2001.

The Act also contains a deduction for certain environmental remediation expenditures that would otherwise be chargeable to a capital account. The expenditures must be incurred in connection with the abatement or control of hazardous substances at qualified contaminated sites ("brownfields") that are located within targeted areas. The provision applies to eligible expenditures incurred in taxable years ending after the date of enactment (August 5, 1997) and before January 1, 2001.

The Act also contains a provision that provides a tax refund to the National Railroad Passenger Corporation ("Amtrak") based on the carryback of its net operating losses against the tax attributes of its predecessor railroads. The maximum refund payable to Amtrak under this provision is limited to $2.323 billion. The provision became effective on December 2, 1997, upon enactment of Federal legislation that authorizes reforms of Amtrak.[11] This provision is not listed in Table 1 because the revenue effects of the provision are not associated with taxpayer activity during fiscal years 1998 through 2002 (i.e., all of the losses that will be carried back were incurred by Amtrak prior to 1997).

[11] S. 738, the "Amtrak Reform and Accountability Act of 1997," was signed by the President on December 2, 1997 (P.L. 105–134).

Extensions of expiring tax provisions

The Act extends a number of tax expenditure provisions that had recently expired or were scheduled to expire. The tax credit for qualified research expenditures (sec. 41), which expired after May 31, 1997, is extended for the period June 1, 1997, through June 30, 1998, with modifications. The deduction equal to the fair market value of "qualified appreciated stock" contributed to a private foundation, which expired after May 31, 1997, is extended for the period June 1, 1997, through June 30, 1998. (The effects of this provision are reflected in the tax expenditure estimates for "deduction for charitable contributions" in Table 1.) The work opportunity tax credit, which was scheduled to expire after September 30, 1997, is modified and extended through June 30, 1998. The orphan drug tax credit, which expired after May 31, 1997, is reinstated effective June 1, 1997, and made permanent. The Act also extends the exclusion for employer-provided assistance for undergraduate education, as discussed above under "education tax incentives."

Modifications to existing tax expenditures

The Act also contains a number of provisions that modify existing tax expenditures. The following is a partial list:

—The rates of deduction for health insurance expenses of self-employed individuals are increased as follows: the deduction is 40 percent in 1997, 45 percent in 1998 and 1999, 50 percent in 2000 and 2001, 60 percent in 2002, 80 percent in 2003 through 2005, 90 percent in 2006, and 100 percent in 2007 and thereafter.

—The $150 million limit on the amount of tax-exempt bonds that may be issued by a private, charitable (sec. 501(c)(3)) organization is repealed. The repeal is effective for bonds issued after the date of enactment (August 5, 1997) to finance capital expenditures incurred after that date. (Table 1 contains separate tax expenditure listings for the various types of tax-exempt bonds, grouped in accordance with the activities which they finance.)

—The rule that depletion deductions for an oil or gas well may not exceed 100 percent of the net income from the property in any year is temporarily suspended, but only for domestic oil and gas production from marginal properties during taxable years beginning in 1998 and 1999.

—Computer software that is licensed for reproduction abroad is included in the definition of export property for purposes of the foreign sales corporation tax code provisions, effective for gross receipts attributable to periods after December 31, 1997.

—The $70,000 limitation on the exclusion of foreign earned income is increased to $80,000 in increments of $2,000 each year beginning in 1998, and the $80,000 limitation is indexed for inflation beginning in 2008.

—For the purpose of computing charitable deductions for the use of passenger automobiles, the standard milege rate is increased from 12 to 14 cents per mile, effective for taxable years beginning after December 31, 1997.

—The tax treatment of pensions is modified through a variety of provisions. The effects of these provisions are reflected in the tax expenditure estimates for "net exclusion of pension contributions and earnings" in Table 1.

Alternative minimum tax

The Act contains two provisions that make major modifications to the alternative minimum tax. First, the depreciation lives used for purposes of the alternative minimum tax are conformed to the depreciation lives used for purposes of the regular tax, effective for property placed in service after 1998. Second, the corporate alternative minimum tax is repealed for corporations having average annual gross receipts of less than $5 million, effective for taxable years beginning after 1997. These provisions do not directly modify any existing tax expenditures but they allow taxpayers to receive greater benefits from certain tax expenditures. Thus, in Table 1, the estimates for a number of tax expenditures have been increased. The tax expenditure that is most affected is "depreciation of equipment in excess of the alternative depreciation system."

Canceled tax provisions

The Act contains two tax expenditure provisions that were canceled by the President pursuant to the Line Item Veto Act of 1996. The first provision would have provided for a deferral of tax on gains from the sale of stock in a qualified refiner or processor to an eligible farmer's cooperative, effective for sales after December 31, 1997. The second provision would have provided a temporary exception from foreign personal holding company income (for subpart F purposes) for certain income that is derived in the active conduct of an insurance, banking, financing, or similar business, for taxable years beginning in 1998. These provisions are not listed in Table 1.

Comparisons with Treasury Department

The Joint Committee staff and Treasury lists of tax expenditures differ in two respects. First, the Treasury uses a different classification of those provisions that can be considered a part of normal income tax law under both the individual and business income taxes. In general, the Joint Committee staff methodology involves a narrower concept of normal income tax law. The cash method of accounting provides an example. The Treasury considers the cash accounting option for certain businesses as a part of normal income tax law, but the Joint Committee staff methodology treats it as a departure from normal income tax law that constitutes a tax expenditure.

Second, the Joint Committee staff and Treasury estimates of tax expenditures span slightly different sets of years. The Treasury's estimates cover a seven-year period—the last fiscal year, the current fiscal year when the President's budget is submitted, and the next five fiscal years, i.e., fiscal years 1996–2002. The Joint Committee staff estimates cover the current fiscal year and the succeeding four fiscal years, i.e., fiscal years 1998–2002.

For the past six years, the President's budget has contained a section that reviews and tabulates the estate and gift tax provisions that the Treasury considers as tax expenditures. The Joint Committee staff considers estate and gift tax provisions as being outside of the normal income tax structure and thus omits them from its list of tax expenditures.

In some cases, two or more of the tax expenditure items in the Treasury list have been combined into a single item in the Joint Committee staff list, and vice versa. The Table 1 descriptions of some tax expenditures also may vary from the descriptions used by the Treasury.

Tax expenditure items in the Joint Committee staff list that are not classified as tax expenditures by the Treasury are shown below.[12]

Energy

—Expensing of tertiary injectants
—Credit for enhanced oil recovery costs

Agriculture

—Exclusion of cost-sharing payments
—Cash accounting for agriculture

Insurance companies

—Deduction of unpaid property loss reserves of property and casualty companies
—Special treatment of life insurance company reserves
—Exclusion of investment income from structured settlement amounts

Business and commerce

—Expensing of magazine circulation expenditures
—Special rules for magazine, paperback book, and record returns
—Completed contract rules
—Cash accounting, other than agriculture
—Exception from net operating loss limitations for corporations in bankruptcy
—Deferral of gain on like-kind exchanges

Employment

—Exclusion of miscellaneous fringe benefits
—Exclusion of employee awards

Health

—Exclusion of untaxed Medicare benefits
—Hospital Insurance, Supplementary Medical Insurance

[12] This list does not include the tax expenditures that were enacted after the February 1997 publication of the Treasury's tax expenditure report (footnote 3, *supra*).

II. MEASUREMENT OF TAX EXPENDITURES

Tax Expenditure Estimates Generally

A tax expenditure is measured by the difference between tax liability under present law and the tax liability that would result from a recomputation of tax without benefit of the tax expenditure provision. Taxpayer behavior is assumed to remain unchanged for tax expenditure estimate purposes.[13]

The tax expenditure estimates in this report are based on Congressional Budget Office and Joint Committee staff projections of the gross income, deductions, and expenditures of individuals and corporations for calendar years 1997–2002. These projections are used to compute tax liabilities for the present-law revenue baseline and tax liabilities for the alternative baseline that assumes that the tax expenditure provision does not exist.

Internal Revenue Service ("IRS") statistics from recent tax returns are used to develop projections of the tax credits, deductions, and exclusions that will be claimed under the present-law baseline. These IRS statistics show the actual usage of the various tax expenditure provisions. In the case of some tax expenditures, such as the earned income tax credit, there is evidence that some taxpayers are not claiming all of the benefits to which they are entitled, while others are filing claims that exceed their entitlements. The tax expenditure estimates in this report are based on projections of actual claims under the various tax provisions, not the tax benefits to which taxpayers are entitled.

Some tax expenditure estimates are based partly on statistics for income, deductions, and expenses for prior years. Accelerated depreciation is an example. Estimates for this tax expenditure are based on the difference between tax depreciation deductions under present law and the deductions that would have been claimed in the current year if investments in the current year and all prior years had been depreciated using the alternative (normal income tax law) depreciation system.

Each tax expenditure is estimated separately, under the assumption that all other tax expenditures remain in the tax code. If two or more tax expenditures were estimated simultaneously, the total change in tax liability could be smaller or larger than the sum of the amounts shown for each item separately, as a result of interactions among the tax expenditure provisions.

Year-to-year differences in the estimates for each tax expenditure reflect changes in tax law, including phaseouts of tax expenditure provisions and changes that alter the definition of the normal in-

[13] An alternative way to measure tax expenditures is to express their values in terms of "outlay equivalents." An outlay equivalent is the dollar size of a direct spending program that would provide taxpayers with net benefits that would equal what they now receive from a tax expenditure. The Treasury Department presents estimates of outlay equivalents in the President's budget in addition to presenting estimates in the same manner as the Joint Committee staff.

come tax structure, such as the tax rate schedule, the personal exemption amount, and the standard deduction. Some of the estimates for this tax expenditure report may differ from estimates made in previous years because of changes in law and economic conditions, the availability of better data, and improved estimating techniques.

Tax Expenditures versus Revenue Estimates

A tax expenditure estimate is not the same as a revenue estimate for the repeal of the tax expenditure provision for two reasons. First, tax expenditure estimates do not incorporate any changes in taxpayer behavior, whereas revenue estimates incorporate the effects of the behavioral changes that are anticipated to occur in response to the repeal of a tax provision. Second, tax expenditure estimates are concerned with changes in the tax liabilities of taxpayers. Because the tax expenditure focus is on tax liabilities as opposed to Federal government tax receipts, there is no concern for the timing of tax payments. Revenue estimates are concerned with changes in Federal tax receipts, which are affected by the timing of tax payments.

If a tax expenditure provision were repealed, it is likely that the repeal would be made effective at the beginning of a calendar year. In this case, the revenue estimate for repeal would show a smaller revenue gain in the first fiscal year than in subsequent years, because the repeal would be occurring after the start of the government's fiscal year. The revenue estimate might also reflect some delay in the timing of the revenue gains as a result of the taxpayer tendency to postpone or forgo changes in tax withholding and estimated tax payments.

III. TAX EXPENDITURE ESTIMATES

Tax expenditures are grouped in Table 1 in the same functional categories as outlays in the Federal budget. Estimates are shown separately for individuals and corporations. Those tax expenditures that do not fit clearly into any single budget category have been placed in the most appropriate category.

Several of the tax expenditure items involve small amounts of revenue, and those estimates are indicated in Table 1 by footnote 1. For each of these items, the footnote means that the tax expenditure is less than $50 million in the fiscal year.

Table 2 presents tax return information for each of nine income classes on the number of all returns filed, the number of all returns and taxable returns with itemized deductions, and the amount of tax liability.

Table 3 provides distributional estimates by income class for some of the tax expenditures that affect individual taxpayers. Not all tax expenditures that affect individuals are shown in this table because of the difficulty in making reliable estimates of the income distribution of items that do not appear on tax returns under present law.

Table 1.—Tax Expenditure Estimates By Budget Function, Fiscal Years 1998–2002

[Billions of dollars]

Function	Corporations					Individuals					Total 1998–2002
	1998	1999	2000	2001	2002	1998	1999	2000	2001	2002	
National Defense											
Exclusion of benefits and allowances to Armed Forces personnel	....	....	....	....	....	1.9	1.9	1.9	2.0	2.0	9.7
Exclusion of military disability benefits	....	....	....	....	....	0.1	0.1	0.1	0.1	0.1	0.5
International Affairs											
Exclusion of income earned abroad by U.S. citizens	....	....	....	....	....	1.8	1.9	2.0	2.2	2.3	10.2
Exclusion of certain allowances for Federal employees abroad	....	....	....	....	....	0.2	0.2	0.2	0.2	0.2	1.0
Exclusion of income of foreign sales corporations (FSCs)	1.6	1.7	1.9	2.0	2.1	....	....	....	....	....	9.3
Deferral of income of controlled foreign corporations	1.2	1.3	1.3	1.4	1.5	....	....	....	....	....	6.7
Inventory property sales source rule exception	3.8	3.9	4.0	4.1	4.2	....	....	....	....	....	20.0
General Science, Space, and Technology											
Tax credit for qualified research expenditures	1.6	1.1	0.7	0.4	0.1	(1)	(1)	(1)	(1)	(1)	3.9
Expensing of research and experimental expenditures	2.6	2.8	3.0	3.2	3.4	(1)	(1)	(1)	(1)	(1)	15.0
Energy											
Expensing of exploration and development costs:											
Oil and gas	0.2	0.2	0.2	0.2	0.2	(1)	(1)	(1)	(1)	(1)	1.0
Other fuels	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.2
Excess of percentage over cost depletion:											
Oil and gas	0.4	0.4	0.4	0.4	0.4	0.1	0.1	0.1	0.1	0.1	2.4
Other fuels	0.2	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	1.5
Tax credit for enhanced oil recovery costs	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.3

Tax credit for production of non-conventional fuels	1.1	1.1	1.1	1.0	1.0	0.3	0.3	0.3	0.3	0.2	6.7
Tax credits for alcohol fuels [2]	[1]	[1]	[1]	[1]	[1]	....	....	....	....	....	[1]
Exclusion of interest on State and local government industrial development bonds for energy production facilities	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.1	0.1	1.2
Expensing of tertiary injectants	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	0.1
Exclusion of energy conservation subsidies provided by public utilities	....	....	....	....	....	[1]	[1]	[1]	[1]	[1]	0.2
Tax credit for investments in solar and geothermal energy facilities	0.1	0.1	0.1	0.1	0.1	[1]	[1]	[1]	[1]	[1]	0.5
Tax credit for electricity production from wind and biomass	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	0.3
Tax credit for electric vehicles	[1]	[1]	0.1	0.1	0.1	[1]	[1]	[1]	[1]	[1]	0.3
Deductions for clean-fuel vehicles and refueling property	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	0.1
Natural Resources and Environment											
Expensing of exploration and development costs, nonfuel minerals	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	0.1
Excess of percentage over cost depletion, nonfuel minerals	0.2	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	1.5
Tax credit and 7-year amortization for reforestation expenditures	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	0.1
Expensing of multiperiod timber-growing costs	0.2	0.2	0.2	0.2	0.2	[1]	[1]	[1]	[1]	[1]	1.1
Exclusion of interest on State and local government sewage, water, and hazardous waste facilities bonds	0.2	0.2	0.2	0.2	0.2	0.6	0.6	0.6	0.6	0.6	3.7
Tax credit for rehabilitation of historic structures	0.1	0.1	0.1	0.1	0.1	....	....	....	....	....	0.5
Special rules for mining reclamation reserves	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	0.2
Exclusion of contributions in aid of construction for water and sewer utilities	[1]	[1]	[1]	[1]	[1]	....	....	....	....	....	0.2

Footnotes at end of table.

Table 1.—Tax Expenditure Estimates By Budget Function, Fiscal Years 1998–2002—Continued

[Billions of dollars]

Function	Corporations					Individuals					Total 1998–2002
	1998	1999	2000	2001	2002	1998	1999	2000	2001	2002	
Agriculture											
Expensing of soil and water conservation expenditures	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.2
Expensing of fertilizer and soil conditioner costs	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.2
Expensing of the costs of raising dairy and breeding cattle	(1)	(1)	(1)	(1)	(1)	0.1	0.1	0.2	0.2	0.2	0.8
Exclusion of cost-sharing payments	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.1
Exclusion of cancellation of indebtedness income of farmers	....	....	....	....	....	0.1	0.1	0.1	0.1	0.1	0.4
Cash accounting for agriculture	(1)	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2	1.2
Income averaging for farmers	....	....	....	....	....	(1)	(1)	(1)	(1)	(1)	0.1
Commerce and Housing											
Financial institutions:											
Bad-debt reserves of financial institutions	(1)	(1)	(1)	(1)	(1)	....	....	....	....	....	0.1
Exemption of credit union income	0.8	0.8	0.9	0.9	1.0	....	....	....	....	....	4.4
Insurance companies:											
Exclusion of investment income on life insurance and annuity contracts	1.2	1.2	1.3	1.3	1.3	20.9	21.5	22.0	22.5	23.1	116.2
Small life insurance company taxable income adjustment	0.1	0.1	0.1	0.1	0.1	....	....	....	....	....	0.5
Special treatment of life insurance company reserves	1.9	2.0	2.1	2.3	2.4	....	....	....	....	....	10.8
Deduction for unpaid property loss reserves for property and casualty insurance companies	2.8	3.0	3.1	3.3	3.5	....	....	....	....	....	15.7
Special deduction for Blue Cross and Blue Shield companies	0.4	0.4	0.4	0.4	0.3	....	....	....	....	....	1.9

Item											
Housing:											
Deduction for mortgage interest on owner-occupied residences	....	....	....	....	....	43.0	44.7	46.4	48.3	50.2	232.6
Deduction for property taxes on owner-occupied residences	....	....	....	....	....	16.6	17.3	17.9	18.7	19.5	89.9
Exclusion of capital gains on sales of principal residences	....	....	....	....	....	5.6	5.7	5.9	6.1	6.3	29.6
Exclusion of interest on State and local government bonds for owner-occupied housing	0.6	0.6	0.7	0.7	0.7	1.6	1.7	1.8	1.9	1.9	12.2
Exclusion of interest on State and local government bonds for rental housing	0.3	0.3	0.3	0.3	0.3	0.8	0.8	0.9	0.9	0.9	5.8
Depreciation of rental housing in excess of the alternative depreciation system	1.1	1.0	1.0	1.0	1.0	0.8	0.7	0.7	0.7	0.7	8.7
Tax credit for low-income housing	1.1	1.2	1.4	1.5	1.6	2.1	2.3	2.5	2.8	3.0	19.6
Tax credit for first-time homebuyers in the District of Columbia	....	....	....	....	....	(1)	(1)	(1)	(1)	(1)	0.1
Other business and commerce:											
Reduced rates of tax on long-term capital gains	....	....	....	....	....	30.8	29.4	29.0	38.8	35.0	163.1
Depreciation of buildings other than rental housing in excess of the alternative depreciation system	2.6	1.9	1.5	1.2	1.2	1.1	0.9	0.7	0.5	0.5	12.1
Depreciation of equipment in excess of the alternative depreciation system	25.3	26.9	28.2	28.8	29.0	6.8	7.4	7.8	7.8	7.7	175.7
Expensing of depreciable business property	0.7	0.6	0.6	0.8	0.8	0.4	0.3	0.3	0.4	0.5	5.4
Exclusion of capital gains at death	....	....	....	....	....	18.0	19.2	20.5	21.9	23.4	103.0
Carryover basis of capital gains on gifts	....	....	....	....	....	1.8	1.9	1.9	2.0	2.1	9.7
Amortization of business startup costs	(1)	(1)	(1)	(1)	(1)	0.3	0.3	0.3	0.3	0.3	1.6
Reduced rates on first $10,000,000 of corporate taxable income	4.2	4.3	4.4	4.5	4.7	....	....	....	....	....	22.1

Footnotes at end of table.

Table 1.—Tax Expenditure Estimates By Budget Function, Fiscal Years 1998–2002—Continued

[Billions of dollars]

Function	Corporations					Individuals					Total 1998–2002
	1998	1999	2000	2001	2002	1998	1999	2000	2001	2002	
Permanent exemption from imputed interest rules	(1)	(1)	(1)	(1)	(1)	0.2	0.2	0.2	0.2	0.2	1.1
Expensing of magazine circulation expenditures	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.2
Special rules for magazine, paper-back book, and record returns	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.1
Deferral of gain on non-dealer installment sales	0.5	0.5	0.5	0.5	0.5	0.4	0.4	0.4	0.4	0.4	4.5
Completed contract rules	0.2	0.2	0.2	0.2	0.2	(1)	(1)	(1)	(1)	(1)	1.1
Cash accounting, other than agriculture	(1)	(1)	(1)	(1)	(1)	0.1	0.1	0.1	0.1	0.1	0.6
Exclusion of interest on State and local government small-issue industrial development bonds	0.1	0.1	0.1	0.1	0.1	0.3	0.3	0.2	0.2	0.2	1.7
Deferral of gain on like-kind exchanges	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.3	0.3	0.3	3.5
Exception from net operating loss limitations for corporations in bankruptcy proceedings	0.5	0.5	0.5	0.5	0.4	....	....	....	....	....	2.4
Tax credit for employer-paid FICA taxes on tips	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2	1.4
Deferral of gain on involuntary conversions resulting from Presidentially-declared disasters	....	....	....	....	....	(1)	(1)	(1)	(1)	(1)	0.1
Transportation											
Deferral of tax on capital construction funds of shipping companies	0.1	0.1	0.1	0.1	0.1	....	....	....	....	....	0.5
Exclusion of employer-paid transportation benefits	....	....	....	....	....	3.3	3.2	3.2	3.2	3.2	16.1
Exclusion of interest on State and local government bonds for high-speed rail	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.1

Community and Regional Development											
Empowerment zone tax incentives	0.2	0.2	0.3	0.4	0.3	0.2	0.3	0.4	0.4	0.3	3.0
District of Columbia tax incentives	(1)	(1)	0.1	0.1	0.1	(1)	0.1	0.1	0.1	0.1	0.6
Indian reservation tax incentives	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.1	0.1	1.4
Expensing of redevelopment costs in certain environmentally contaminated areas ("Brownfields")	(1)	0.1	0.1	0.1	(1)	(1)	(1)	(1)	(1)	(1)	0.4
Tax credit for rehabilitation of structures, other than historic structures	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.4
Exclusion of interest on State and local government bonds for private airports, docks, and mass-commuting facilities	0.3	0.3	0.4	0.4	0.4	0.8	0.9	1.0	1.1	1.0	6.6
Education, Training, Employment, and Social Services											
Education and training:											
Tax credits for tuition for post-secondary education	....	....	....	....	....	6.2	6.3	7.2	7.7	7.6	35.1
Deduction for interest on student loans	....	....	....	....	....	(1)	0.1	0.1	0.2	0.3	0.7
Exclusion of earnings of trust accounts for higher education ("education IRAs")	....	....	....	....	....	0.2	0.5	0.7	0.8	1.1	3.3
Exclusion of interest on educational savings bonds	....	....	....	....	....	(1)	(1)	(1)	(1)	(1)	0.1
Deferral of tax on earnings of qualified State tuition programs	....	....	....	....	....	(1)	0.1	0.1	0.2	0.2	0.7
Exclusion of scholarship and fellowship income	....	....	....	....	....	0.8	0.9	0.9	1.0	1.1	4.6
Exclusion of employer-provided education assistance benefits	....	....	....	....	....	0.2	0.3	0.2	0.1	....	0.8
Parental personal exemption for students age 19 to 23	....	....	....	....	....	0.8	0.9	0.9	1.0	1.1	4.7
Exclusion of interest on State and local government student loan bonds	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2	0.2	1.6

Footnotes at end of table.

Table 1.—Tax Expenditure Estimates By Budget Function, Fiscal Years 1998–2002—Continued

[Billions of dollars]

Function	Corporations					Individuals					Total 1998–2002
	1998	1999	2000	2001	2002	1998	1999	2000	2001	2002	
Exclusion of interest on State and local government bonds for private nonprofit educational facilities	0.3	0.3	0.3	0.4	0.4	0.8	0.8	0.9	1.0	1.0	6.2
Tax credit for holders of qualified education bonds	(1)	0.1	0.1	0.1	0.1	....	....	....	....	....	0.4
Deduction for charitable contributions to educational institutions	0.9	1.0	1.1	1.2	1.4	2.6	2.7	2.8	2.9	3.0	19.6
Employment:											
Exclusion of employee meals and lodging (other than military)	....	....	....	....	....	0.7	0.7	0.8	0.8	0.8	3.8
Exclusion of benefits provided under cafeteria plans (3)	....	....	....	....	....	5.7	6.5	7.2	7.9	8.7	35.9
Exclusion of rental allowances for ministers' homes	....	....	....	....	....	0.3	0.3	0.3	0.4	0.4	1.7
Exclusion of miscellaneous fringe benefits	....	....	....	....	....	5.8	6.2	6.5	6.9	7.3	32.7
Exclusion of employee awards	....	....	....	....	....	0.1	0.1	0.1	0.1	0.1	0.7
Exclusion of income earned by voluntary employees' beneficiary associations	....	....	....	....	....	0.5	0.5	0.5	0.6	0.6	2.7
Special tax provisions for employee stock ownership plans (ESOPs)	0.8	0.8	0.9	0.9	1.0	(1)	(1)	(1)	(1)	(1)	4.6
Work opportunity tax credit	0.1	0.1	0.1	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.4
Welfare-to-work tax credit	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.1
Social services:											
Tax credit for children under age 17 (4)	....	....	....	....	....	11.6	19.3	20.3	20.2	19.9	91.4
Tax credit for child and dependent care expenses	....	....	....	....	....	2.8	2.8	2.9	2.9	2.9	14.3
Exclusion of employer-provided child care (5)	....	....	....	....	....	0.9	1.0	1.1	1.2	1.2	5.4

Exclusion of certain foster care payments	....	....	....	....	....	(1)	(1)	(1)	(1)	(1)	0.1
Adoption credit and employee adoption benefits exclusion	....	....	....	....	....	0.4	0.4	0.4	0.4	0.2	1.7
Deduction for charitable contributions, other than for education and health	0.9	1.0	1.1	1.2	1.3	16.3	17.0	17.8	18.7	19.5	94.8
Expensing of costs for removing architectural barriers	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.1
Tax credit for disabled access expenditures	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	0.1
Health											
Exclusion of employer contributions for medical care, health insurance premiums, and long-term care insurance premiums (6)	....	....	....	....	....	51.4	54.8	58.1	61.7	65.4	291.3
Exclusion of medical care and CHAMPUS/TRICARE medical insurance for military dependents, retirees, and retiree dependents	....	....	....	....	....	1.5	1.4	1.5	1.5	1.5	7.4
Deduction for health insurance premiums and long-term care insurance premiums by the self-employed	....	....	....	....	....	0.8	0.9	1.0	1.1	1.4	5.2
Deduction for medical expenses and long-term care expenses	....	....	....	....	....	4.4	4.9	5.3	5.9	6.5	27.1
Medical savings accounts	....	....	....	....	....	(1)	0.1	0.1	0.2	0.2	0.6
Exclusion of interest on State and local government bonds for private nonprofit hospital facilities	0.5	0.6	0.6	0.7	0.7	1.5	1.6	1.7	1.9	1.9	11.7
Deduction for charitable contributions to health organizations	0.7	0.7	0.8	0.9	1.0	1.9	2.0	2.1	2.2	2.3	14.6
Tax credit for orphan drug research	(1)	(1)	(1)	(1)	(1)	....	....	....	....	....	0.2
Medicare											
Exclusion of untaxed medicare benefits:											
Hospital insurance	....	....	....	....	....	13.4	14.9	16.5	18.3	20.2	83.2
Supplementary medical insurance	....	....	....	....	....	5.8	6.7	7.6	8.6	9.7	38.4

Footnotes at end of table.

Table 1.—Tax Expenditure Estimates By Budget Function, Fiscal Years 1998–2002—Continued

[Billions of dollars]

Function	Corporations					Individuals					Total 1998–2002
	1998	1999	2000	2001	2002	1998	1999	2000	2001	2002	
Income Security											
Exclusion of workers' compensation benefits	....	....	....	....	....	3.8	3.9	4.0	4.2	4.3	20.2
Exclusion of special benefits for disabled coal miners	....	....	....	....	....	0.1	0.1	0.1	0.1	0.1	0.5
Exclusion of cash public assistance benefits	....	....	....	....	....	0.4	0.5	0.5	0.5	0.5	2.4
Net exclusion of pension contributions and earnings:											
Employer plans	....	....	....	....	....	73.5	76.7	80.0	79.9	78.7	388.8
Individual retirement plans	....	....	....	....	....	9.9	10.8	11.9	13.0	14.3	59.9
Keogh plans	....	....	....	....	....	3.9	4.2	4.4	4.6	4.9	22.0
Exclusion of other employee benefits:											
Premiums on group term life insurance	....	....	....	....	....	1.9	1.9	2.0	2.1	2.1	10.0
Premiums on accident and disability insurance	....	....	....	....	....	0.2	0.2	0.2	0.2	0.2	1.0
Exclusion of employer-provided death benefits	....	....	....	....	....	(1)	(1)	(1)	(1)	(1)	0.2
Additional standard deducation for the blind and the elderly	....	....	....	....	....	2.0	2.2	2.3	2.5	2.6	11.6
Tax credit for the elderly and disabled	....	....	....	....	....	(1)	(1)	(1)	(1)	(1)	0.1
Deduction for casualty and theft losses	....	....	....	....	....	0.3	0.3	0.3	0.3	0.3	1.5
Earned income credit (EIC)(7)	....	....	....	....	....	5.2	5.2	5.3	5.5	5.9	27.2
Social Security and Railroad Retirement											
Exclusion of untaxed social security and railroad retirement benefits	....	....	....	....	....	27.0	28.2	29.5	30.8	32.2	147.8
Veterans' Benefits and Services											
Exclusion of veterans' disability compensation	....	....	....	....	....	1.9	2.0	2.0	2.1	2.1	10.1
Exclusion of veterans' pensions	....	....	....	....	....	0.1	0.1	0.1	0.1	0.1	0.5

Exclusion of GI bill benefits	....	....	....	....	....	0.1	0.1	0.1	0.1	0.1	0.5
Exclusion of interest on State and local government bonds for veterans' housing	(1)	(1)	(1)	(1)	(1)	0.1	0.1	0.1	0.1	0.1	0.5
General Purpose Fiscal Assistance											
Exclusion of interest on public purpose State and local government debt	4.3	4.5	5.1	5.4	5.6	11.7	12.2	13.7	14.7	15.2	92.4
Deduction for nonbusiness State and local governments income and personal property taxes	....	....	....	....	....	29.1	30.2	31.3	32.5	33.8	156.8
Tax credit for Puerto Rico and possession income	3.4	3.7	3.9	4.0	3.6	....	....	....	....	....	18.6
Interest											
Deferral of interest on savings bonds	....	....	....	....	....	1.5	1.5	1.5	1.5	1.5	7.5

Footnotes for Table 1:

[1] Positive tax expenditure of less than $50 million.

[2] In addition, the 54-cents-per-gallon exemption from excise tax for alcohol fuels results in a reduction in excise tax receipts, net of income tax effect, of $0.5 billion per year in fiscal years 1998 through 2000, and $0.6 billion in fiscal years 2001 and 2002.

[3] Estimate includes revenue losses from amounts of health insurance purchased through cafeteria plans and child care purchased through flexible spending accounts. These amounts are also included in other line items in this table.

[4] The figures in the table show the effect of the child credit on receipts. The increase in outlays is: $0.6 billion in 1998, $1.1 billion in 1999, $1.1 billion in 2000, $1.1 billion in 2001, and $1.1 billion in 2002.

[5] Estimate includes employer-provided child care purchased through dependent care flexible spending accounts.

[6] Estimate includes employer-provided health insurance purchased through cafeteria plans.

[7] The figures in the table show the effect of the EIC on receipts. The increase in outlays is: $21.7 billion in 1998, $22.5 billion in 1999, $23.4 billion in 2000, $24.4 billion in 2001, and $25.4 billion in 2002.

Note.—Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.

Table 2.—Distribution by Income Class of All Returns, Taxable Returns, Itemized Returns, and Tax Liability at 1997 Rates and 1997 Law and 1997 Income Levels[1]

[Money amounts in millions of dollars; returns in thousands]

Income class (thousands)[2]	All returns[3]	Taxable returns	Itemized returns	Tax liability
Below $10	21,496	1,642	130	−$5,364
$10 to $20	24,714	9,122	921	−4,029
$20 to $30	19,926	12,990	2,156	16,455
$30 to $40	16,441	13,966	3,399	33,817
$40 to $50	12,449	11,502	3,947	40,823
$50 to $75	19,605	19,397	10,041	108,548
$75 to $100	9,241	9,206	6,975	92,691
$100 to $200	7,310	7,293	6,441	145,699
$200 and over	1,648	1,644	1,527	208,042
Total	**132,830**	**86,763**	**35,537**	**$636,683**

[1] Tax law as in effect on January 1, 1997, is applied to the 1997 level and sources of income and their distribution among taxpayers. Excludes individuals who are dependents of other taxpayers and taxpayers with negative income.

[2] The income concept used to place tax returns into classes is adjusted gross income (AGI) plus: (a) tax-exempt interest, (b) employer contributions for health plans and life insurance, (c) employer share of FICA tax, (d) workers' compensation, (e) nontaxable Social Security benefits, (f) insurance value of Medicare benefits, (g) alternative minimum tax preference items, and (h) excluded income of U.S. citizens living abroad.

[3] Includes filing and nonfiling units. Filing units include all taxable and nontaxable returns. Nonfiling units include individuals with income that is exempt from Federal income taxation (e.g., transfer payments, interest from tax-exempt bonds, etc.).

Note.—Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.

Table 3.—Distribution by Income Class of Selected Individual Tax Expenditure Items, at 1997 Rates and 1997 Income Levels[1]

[Money amounts in millions of dollars; returns in thousands]

Income class (thousands)[2]	Medical deduction[3]		Real estate tax deduction	
	Returns	Amount	Returns	Amount
Below $10	13	$2	13	$1
$10 to $20	203	61	383	56
$20 to $30	674	217	1,322	221
$30 to $40	961	456	2,534	525
$40 to $50	794	383	3,234	845
$50 to $75	1,424	1,087	8,842	2,964
$75 to $100	514	703	6,357	3,516
$100 to $200	245	657	5,913	4,952
$200 and over	20	181	1,298	2,929
Total	**4,847**	**$3,745**	**29,897**	**$16,009**

Footnotes at end of table.

Table 3.—Distribution by Income Class of Selected Individual Tax Expenditure Items, at 1997 Rates and 1997 Income Levels [1]—Continued

[Money amounts in millions of dollars; returns in thousands]

Income class (thousands) [2]	State and local income and personal property tax deduction		Charitable contributions	
	Returns	Amount	Returns	Amount
Below $10	37	(6)	61	$4
$10 to $20	521	15	1,009	140
$20 to $30	1,657	89	2,475	382
$30 to $40	3,090	351	3,458	724
$40 to $50	3,704	794	4,013	989
$50 to $75	9,709	3,156	9,260	3,455
$75 to $100	6,488	4,579	5,305	3,160
$100 to $200	5,951	8,213	4,417	4,298
$200 and over	1,381	11,100	1,286	7,389
Total	**32,539**	**$28,296**	**31,284**	**$20,541**

Footnotes at end of table.

Table 3.—Distribution by Income Class of Selected Individual Tax Expenditure Items, at 1997 Rates and 1997 Income Levels [1]—Continued

[Money amounts in millions of dollars; returns in thousands]

Income class (thousands) [2]	Child care credit		Earned income credit [4]	
	Returns	Amount	Returns	Amount
Below $10	....	....	5,175	$5,740
$10 to $20	345	118	6,439	12,862
$20 to $30	748	342	5,106	6,773
$30 to $40	958	431	1,650	1,313
$40 to $50	712	298	130	111
$50 to $75	1,568	673	33	47
$75 to $100	981	477	(5)	(6)
$100 to $200	670	332	....	....
$200 and over	82	43	....	....
Total	**6,063**	**$2,714**	**18,534**	**$26,847**

Footnotes at end of table.

Table 3.—Distribution by Income Class of Selected Individual Tax Expenditure Items, at 1997 Rates and 1997 Income Levels [1]—Continued

[Money amounts in millions of dollars; returns in thousands]

Income class (thousands) [2]	Untaxed Social Security and Railroad Retirement benefits		Additional standard deduction for the elderly and blind	
	Returns	Amount	Returns	Amount
Below $10	173	$35	11	$1
$10 to $20	4,153	1,840	251	30
$20 to $30	5,157	5,216	1,663	230
$30 to $40	4,554	6,170	1,903	284
$40 to $50	3,598	5,925	2,202	412
$50 to $75	4,036	5,700	2,640	590
$75 to $100	1,362	598	726	253
$100 to $200	1,065	263	364	134
$200 and over	280	100	34	12
Total	**24,378**	**$25,846**	**9,793**	**$1,945**

Footnotes at end of table.

Table 3.—Distribution by Income Class of Selected Individual Tax Expenditure Items, at 1997 Rates and 1997 Income Levels [1]—Continued

[Money amounts in millions of dollars; returns in thousands]

Income class (thousands) [2]	Mortage interest deduction	
	Returns	Amount
Below $10	20	$3
$10 to $20	373	137
$20 to $30	1,186	463
$30 to $40	2,464	1,312
$40 to $50	3,064	2,234
$50 to $75	8,510	7,799
$75 to $100	6,131	9,436
$100 to $200	5,545	13,391
$200 and over	1,193	7,043
Total	**28,486**	**$41,818**

Footnotes for Table 3:

[1] Tax law as in effect on January 1, 1997. Excludes individuals who are dependents of other taxpayers.

[2] The income concept used to place tax returns into classes is adjusted gross income (AGI) plus: (a) tax-exempt interest, (b) employer contributions for health plans and life insurance, (c) employer share of FICA tax, (d) workers' compensation, (e) nontaxable Social Security benefits, (f) insurance value of Medicare benefits, (g) alternative minimum tax preference items, and (h) excluded income of U.S. citizens living abroad.

[3] Tax expenditure estimate does not include revenue losses attributable to deductions for long-term care and long-term care insurance premiums.

[4] Includes the refundable portion of the earned income credit.

[5] Less than 500 returns.

[6] Less than $500,000.

Note.—Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.