RSC Republican Study Committee

Rep. Jeb Hensarling (R-TX), Chairman
Russ Vought, Executive Director

132 Cannon House Office Building
Washington, DC 20515

www.house.gov/hensarling/rsc

ph (202) 226-9717 / fax (202) 226-1633

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H.R. 1424—Emergency Economic Stabilization Act & The Tax Extenders and Alternative Minimum Tax Relief Act

Order of Business: H.R. 1424 is scheduled to be considered on Friday, October 3, 2008, likely under a closed rule.

Division A is essentially identical to H.R. 3997, the Emergency Economic Stabilization Act, which failed by a vote of 205-228, on September 29, 2008. However, Division A now includes new language pertaining to FDIC coverage limits (see below).

Division B is essentially identical to the energy tax extender portion of H.R. 6049, that passed the Senate by a vote of 93-2, on September 23, 2008.

Division C is essentially identical to the non-energy tax extender portion of H.R. 6049, that passed the Senate on September 23rd, including the one-year AMT "patch" (from H.R. 7005), disaster tax relief (from H.R. 7006), mental health parity (from H.R. 6983), and secure rural school language.

Summary of Division A—The Emergency Economic Stabilization Act

Division A provides the Treasury Department with the authority to purchase illiquid, troubled assets on the books of private financial institutions, in an effort to resolve the current financial crisis. The *highlights* include the following:

- **Purchase Authority**: Provides $700 billion in purchase authority *at any one time* to Treasury to purchase "troubled assets from any financial institutions," of which $250 billion would be made immediately available and another $100 billion once the President certifies that Treasury needs the authority. The final $350 billion is authorized, but Congress could halt the authority by passing a joint resolution *disapproving* the action (under fast-track procedures). However, such joint resolutions require the signature of the President to take effect. While provided in installments or "tranches," the bill provides the full $700 billion, as initially requested by the Administration to calm the financial markets.

- **Troubled Assets:** Broadens the Treasury Department's original request for mortgage-related assets to a larger class of "troubled" assets." Such assets are defined as "any residential or commercial mortgages any securities, obligations, or other instruments that are based on or related to such mortgages" and "*any other financial instrument* that the Secretary…determines the purchase of which is necessary to promote financial market stability" (emphasis added). This definition significantly expands the scope of the purchasing program to potentially many more classes of securities (e.g.., those backed by car loans, credit-card debt, etc.).

- **Insurance Component:** Requires the Treasury Department to establish a federally-backed insurance program, similar to the Federal Deposit Insurance Corporation (FDIC), for holders of troubled assets, *if* it utilizes its purchase authority (which it is expected to do). Treasury would guarantee up to 100% of the timely payment of principal and interest on certain classes of troubled assets, presumably those worth more than the ones which will be immediately purchased. A risk-adjusted premium would be assessed to holders of these assets to self-finance the program through the participants. The total amount of assets insured by the program, minus the premiums, would offset the purchase authority available to Treasury. However, it is unclear whether the insurance program would be set up quickly or effectively (with a large enough class of assets) to ensure that it can be used to substantially offset Treasury's purchase authority.

- **Private Firms as Financial Agents:** Authorizes Treasury to designate private financial institutions as its agents to carry out such duties as may be required in exercising its new authority. The bill directs Treasury to solicit bids from a broad range of qualified firms and to "take appropriate steps to manage conflicts of interest, including requiring potential firms to indentify and disclose… potential conflicts." The FDIC would be among the candidates chosen to manage the purchased assets.

- **Priorities:** Requires the Treasury Secretary to exercise its authority in a manner that will protect the taxpayer, provide stability and prevent disruption to the financial market system, the need to help families keep their homes and to stabilize their communities, etc. (in that order).

- **Executive Compensation:** Sets executive compensation limits on two classes of firms, 1) those which the federal government directly takes over "AIG-style" and 2) those who sell $300 million or more in assets to the federal government, so-called "high-volume sellers." For those firms directly taken over, the Secretary would establish limits on compensation for taking unnecessary and excessive risk, a prohibition on "golden parachute" payments, and a process for recouping any incentive payments made to "senior executives" (top 5 executives of a public company) based on earning statements later proven to be materially inaccurate. For high-volume sellers, the legislation would also ban golden parachute payments and lower the current deduction for executive compensation from $1 million to $500,000. Many conservatives may be concerned that, while aimed only at participating firms, this change to tax law sets a dangerous precedent since liberals have pushed for years to lower this deduction. It should be noted that the limit on the deduction itself is one of the main reasons for corporations to structure incentives-based compensation that may cause corporate actors to take excessive risks to boost share prices.

- **Reverse Auctions:** Requires the Secretary to use methods, such as auctions or "reverse" auctions, in purchasing firms' troubled assets, in order to minimize the cost to taxpayers. Treasury intends to use a process whereby it indicates its intent to buy a certain class of troubled assets and competing firms provide the terms for which they would sell. If the process works, Treasury would choose the seller with the lowest sticker price. When these assets are later sold, the proceeds would flow into general revenues. However, some conservatives may be concerned that this process may not work in practice because: 1) all sellers have an incentive to hold onto to their assets until the government offers an inflated price over what the market would currently bear (since firms are undercapitalized and there is a limit to the losses that they can sustain by selling their assets at market or below-market rates), and 2) the classes of assets may not be particularly large or homogenized, since many of these securities are so complex and unique, perhaps making it difficult to attract a large pool of willing sellers to drive down prices.

- **Warrants:** Requires the Treasury to receive warrants for non-voting, common or preferred stock in firms that sell more than $100 million in troubled assets to the government. A warrant is a certificate that entitles the holder to purchase securities at a certain price. Giving the federal government a warrant to shares of participating firms provides a mechanism for taxpayers to recoup a portion of the initial price if share prices increase and the shares can later be bought and sold for a profit. However, it also sets a dangerous precedent in that it allows the federal government to *own* shares in private companies, if the warrant is exercised instead of being sold. While the warrants could only purchase *non-voting* shares, minimizing any authority that comes with such ownership, some conservatives had recommended that the federal government only be able to sell these warrants and never exercise them. This would have allowed for similar levels of taxpayer recoupment without setting a dangerous precedent of the federal government inevitably owning large swaths of the U.S. financial sector.

- **5-Year Recoupment Plan:** Requires the President after five years to determine whether taxpayers have suffered a net loss as a consequence of the purchase program, and if so, to submit a legislative proposal to recoup that amount from participating firms. There is nothing in the bill to ensure that the President's proposal is considered or passed by Congress, casting doubt on the efficacy of this provision—a variation of the Blue Dogs' initial proposal to place an indiscriminate tax on the entire financial sector, regardless of whether a firm's assets where purchased by the Treasury. But to the extent that this provision does lead to legislation, some conservatives may be concerned that it could result in a tax increase.

- **Market and Program Transparency:** Requires the Secretary to make information regarding each purchase available to the public in an electronic form, including a description, amounts, and pricing of such assets. The language also requires the Secretary to make public the mechanisms for purchasing troubled assets, the methods of valuing assets, the process for hiring asset managers, and the criteria for identifying troubled assets for purchase.

- **Debt Limit:** Increases the limit statutory debt limit from $10.615 trillion to $11.315 trillion, an increase of 6.6%. If enacted, the 110th Congress will have presided over three debt limit increases—a total of $2.33 trillion *or 26.2%*.

- **Foreign Banks and Financial Authorities**: Defines a participating financial institution to include foreign banks if "established and regulated under the laws of the U.S. or any State…and having significant operations in the U.S." A central bank or institution owned by foreign government would generally be excluded. However, the Treasury would also be required to coordinate with foreign financial authorities and central banks to establish similar programs in other countries, and to the extent that such foreign institutions lend money to firms with troubled assets that have failed or defaulted, they would be made eligible.

- **Oversight Board:** Establishes a five-person Financial Stability Oversight Board, including the Chairman of the Federal Reserve, the Treasury Secretary, the Director of the Federal Home Finance Agency, the Chairman of the SEC, and the Secretary of Housing and Urban Development, to review the exercise of authority under this legislation and make recommendations to the Treasury.

- **Bank Losses on GSE Stock**: Allows banks to treat losses on shares of preferred stock in Fannie Mae and Freddie Mac as ordinary losses to offset ordinary income, not as capital losses (which is capped). This provision is targeted at many community banks who hold GSE preferred stock and sustained heavy loss after Treasury placed Fannie and Freddie in conservatorship.

- **Discharge of Mortgage Debt:** Extends for two years the exclusion (set to expire on January 1, 2010) from a taxpayer's gross income any discharge of indebtedness income, as long as the debt is for the acquisition, construction, or substantial improvement of the taxpayer's principal home (in addition to certain refinancing).

- **Affordable Housing Earmark:** Does *not* include the provision proposed by Democrat negotiators to earmark 20% of any funds recouped from the disposition of the purchased assets for the Affordable Housing Fund, whose funds flow to many non-profit entities such as ACORN or La Raza. It should be noted that this provision was not part of the original Treasury plan.

- **Mortgage "Cram-Down":** Does *not* authorize bankruptcy judges, as part of creating plans for debtors facing foreclosure to repay their subprime or nontraditional (e.g. interest-only) mortgage debts to reduce or delay adjustments to adjustable-rate subprime or nontraditional mortgages, set a new, fixed interest rate, extend repayment periods, etc.

- **Foreclosure Mitigation:** Directs the Secretary of the Treasury, as an owner of mortgages underlying troubled assets, to implement a plan to maximize assistance to homeowners and to encourage servicers of the underlying mortgages to take advantage of foreclosure prevention programs. In addition, the language requires the Secretary to consent to "reasonable requests" (undefined) from loan servicers for mortgage term extensions, rate reductions, principal write-downs, increases in the proportion of loans within a trust, or the removal of other modification limits.

- **Expiration of Authority:** Terminates the Secretary's authority to purchase and insure troubled assets on December 31, 2009, but allows for extensions until two years after the date of enactment. These sunset dates do not apply to the Secretary's ability to hold purchased assets, since many of these assets may still not be able to be sold by that point.

- **Mark to Market Accounting:** Restates current law that authorizes the SEC to suspend mark-to-market accounting with respect to any class or category of transactions. The bill also requires the SEC to study the impact of mark-to-market regulations on the balance sheets of financial firms and the advisability and feasibility of potential modifications. Some conservatives had been previously concerned with the lack of stronger language, requiring the SEC to promulgate new rules that allow firms to better reflect the true economic value of the mortgage-related assets on their books. However, on September 30th, the SEC issued new guidance to companies, stating that:

  > When an active market for a security does not exist, the use of management estimates that incorporate current market participant expectations of future cash flows…is acceptable….[and] the results of disorderly transactions are not determinative when measuring fair market value. The concept of fair value measurement assumes an orderly transaction between market participants. An orderly transaction is one that involves market participants that are willing to transact…Distressed or forced liquidation sales are not orderly transactions.

  As a result, these new guidelines may resolve many of the concerns expressed by conservatives about the effect of mark-to-market accounting.

- **Exchange Stabilization Fund:** Requires the Secretary to replenish the Exchange Stabilization Fund for any funds used to provide a temporary guarantee program for the money market fund industry and bars it from ever being used that way again.

- **FDIC Coverage Limits:** Temporarily increases the standard maximum deposit insurance limit from $100,000 to $250,000 through December 31, 2009, but this increase "shall not be taken into account…for the purpose of setting assessments," meaning the provision increases the program's liability without also increasing the program's reserves. In addition, the bill temporarily lifts the $30 billion limitation on the FDIC's borrowing authority from the Treasury. These provisions apply to credit unions backed the National Credit Union Administration, as well as the FDIC.

Conservative Concerns: No one would argue that the question before Congress of whether to give Treasury the authority to nationalize mortgage-related and other troubled assets is an easy one. Financial markets are clearly in turmoil, and many large—previously thought to be impregnable—financial firms have and may fail in the weeks to come. Many experts and news reports also warn that without some federal action to bolster market confidence there will continue to be either stagnation in the capital markets or worse, a run on all depository institutions. No one wants those fears to be realized.

However, many conservatives may be concerned that authorizing the Secretary of Treasury to purchase up to $700 billion amounts to an indirect tax of $6,034 per American household, and it will likely forever change the landscape of the nation's free-market system. Institutions, policies, and precedents—right or wrong— enacted in crisis tend to become permanent fixtures.

As Luigi Zingales, a professor at the University of Chicago, writes:

> The decisions that will be made this weekend matter not just to the prospects of the U.S. economy in the year to come; they will shape the type of capitalism we will live in for the next fifty year. Do we want to live in a system where profits are private, but losses are socialized? Where taxpayer money is used to prop up failed firms? Or do we want to live in a system where people are held responsible for their decisions, where imprudent behavior is penalized and prudent behavior rewarded? For somebody like me who believes strongly in the free market system, the most serious risk of the current situation is that the interest of few financiers will undermine the fundamental workings of the capitalist system. The time has come to save capitalism from the capitalists.

Some conservatives may believe that Treasury is right, and given the present circumstances, the risk of inaction is so grave as to warrant such new authority. Others may indeed wonder whether in this moment of crisis, America is on the brink of something far worse—forfeiting its free-market system by placing an implicit guarantee on all economic failure. The message to rational actors with a bail-out of this magnitude is that your profits will be private but your losses socialized. But the system often does not work that way, at least not for long. If losses are socialized, it is likely that profits will soon be on the way, meaning Americans will no longer be free, not just to fail, but to succeed.

Specifically, many conservatives may have the following concerns with the legislation, because the plan:

- **Fails to adequately penalize the debtholders and shareholders** (including many of the executives themselves), who should bear the risk of any losses, and indirectly infuses capital directly onto the books of these financial institutions.

- **Alters fundamentally the nation's free-market system** in that it broadly socializes firm's money-losing mortgage assets and places the U.S. on a slippery slope whereby profits may also be nationalized.

- **Cedes massive authority to Treasury**. Given the fact that the Presidential election is a mere six weeks away and a new Secretary will take office in January 2009, lawmakers have absolutely no idea what individual will ultimately be exercising this vast new authority over the long-term.

- **Sets up Treasury to pay inflated prices for assets**. Since there is nothing in the proposal that forces the financial institutions to sell their assets at a discount rate or event at all, many of these owners may simply wait on the government to increase their bid, leading to more inflated prices than the market would currently bear.

- **Creates the potential for an enormous bureaucracy** that will be needed to administer the purchase and insurance programs.

- **Increases the federal deficit and national debt.** The new mandatory spending, will cause a massive increase in the national debt and an immediate (although smaller) increase in the federal deficit. These annual deficits are funded by selling government bonds purchased by a host of large investors, including foreign countries. However, there is a limit to the amount of bonds that a government can float without adverse financial effects.

- **Aids financial institutions that may not pose a systemic risk.** Some companies, such as AIG, may truly pose a systemic risk to the entire market. However, there is no requirement under the proposal that a company truly be "too big to fail." Instead, *any* financial institutions with mortgage-related assets would be eligible.

Additional Background: On Friday, September 19, 2008, the Treasury Department requested broad new authority to calm U.S. financial markets and purchase illiquid mortgage-related assets from various financial institutions. According to extensive press reporting, the Administration took this action after a series of repeated federal interventions were unsuccessful and a panic began to spread throughout financial markets.

The market for commercial paper, or short-term corporate bonds, tightened as institutional investors increasingly valued ready cash. These investors, namely money-market funds, continued to hoard cash in preparation of an expected run on their funds, which began as investors withdrew roughly $144.5 billion (compared to $7.1 billion the week before). In many cases, these investors fled to short-term government bonds, accepting little-to-no rate of return in exchange for the knowledge that their cash was secured. One money-market fund, Putnam Prime Money Market Fund, shut down because too many investors sought to take their money out at one time, and another, Reserve Primary Fund, announced that it would suspend redemptions temporarily. Administration officials feared that such a lack of confidence would spread.

The case of Reserve Primary Fund is instructive, because it was this money-market fund which seems to have set off the run due to the amount of corporate debt it held in Lehman Brothers. Lehman Brothers had filed for Chapter 11 bankruptcy protection the day before with more than $613 billion in debt. Between 2004 and 2007, this debt had been used in part to purchase almost $300 billion in securities backed by residential and commercial mortgages, otherwise known as mortgage-backed securities or MBS, which have been significantly devalued since the downturn in the housing market.

These "toxic" mortgage-related assets have been virtually unmovable from the portfolios of many financial institutions, such as Lehman Brothers, in part because the market has no idea what they are worth. This underlying predicament led to the Treasury Department's request for blanket authority for the federal government to purchase them—taking them off portfolios, instilling confidence and capital in those firms who had previously held them, in order that lending and borrowing can resume.

Cost to Taxpayers of Division A: According to a CBO letter to Senate Banking Committee Chairman: "Although it is not currently possible to quantify the net budget impact given the lack of details about how the program would be implemented, CBO has concluded that enacting Division A would likely to entail some net budget cost—which would, however, be substantially smaller than $700 billion."

The funding authorized is not subject to appropriations and constitutes mandatory spending. The bill treats the cost of purchasing the assets under the provisions Federal Credit Reform Act of 1990, ensuring that the net-present value of the purchased securities will be scored instead of the initial outlays. This treatment recognizes that the securities have some value (even if less than the purchase price), but value which may not realized until they are sold. Under credit-reform scoring, the cost of the initial outlays is offset by an estimation of what the eventual sale of the assets will return in receipts, and it is this figure which will impact the federal deficit.

Furthermore, Sec. 204 deems all costs arising under the legislation an emergency for purposes of the Congressional budget process.

Summary of Divisions B and C—The Tax Extenders and Alternative Minimum Tax Relief Act (except the Mental Health Parity Provisions)

Divisions B and C include the AMT patch/tax extenders bill (H.R. 6049) that passed the Senate 93-2 two weeks ago. Note that this language contains **far** more tax relief than tax increases (i.e., it is a net tax *cut* by tens of billions of dollars). Americans for Tax Reform remained silent on the Senate-passed extenders bill and said it was NOT a taxpayer pledge violation.

The tax extenders section contains such things as:

- One-year AMT "patch" that passed the House last week;
- About $15 billion over ten years in alternative energy tax extensions;
- About $42 billion in (mostly) two-year extensions of various non-energy tax provisions (research and development, state and local sales tax, etc.);
- Mental health parity language that passed the House last week;
- About $8 billion over ten years in disaster tax relief that passed the House last week; and
- Nearly $42 billion in tax increases over ten years on oil and gas production, unemployment insurance, and investment income.

Tax Relief: Includes several tax decreases, saving taxpayers about $150 billion over ten years, including:

- **AMT:** Provides for a $69,950 AMT exemption amount for married couples in 2008 (it was $66,250 in 2007 and would drop to $45,000 without a "patch") and a $46,200 exemption amount for singles (it was $44,350 in 2007 and would drop to $33,750 without a "patch"). This would prevent for just one year a huge, unintended tax increase, without which more than 25 million taxpayers would be subject to a large tax increase beginning in tax-year 2008. The bill would also prevent taxpayers with AMT credits from paying tax on "phantom" income attributable to incentive stock options (i.e. income that appears on paper but that the taxpayer has not actually exercised). ***The AMT section would save taxpayers $64.61 billion over ten years.***

- **Disaster Tax Relief:** Provides tax relief to individuals affected by federally-declared disasters nationwide, declared after January 1, 2008, and before December 31, 2011. For example, the bill would allow itemizing and non-itemizing taxpayers who have suffered losses as a result of a federally-declared disaster in tax-years 2008-2011 to claim tax deductions for casualty losses without regard to their adjusted gross income. Also, the bill would allow businesses that have been adversely affected by a federally-declared disaster in tax-years 2008-2011 to immediately expense (i.e. deduct) all demolition, repair, clean-up, and environmental remediation expenditures. Additionally, the bill would allow businesses to carry back to the previous five years (as opposed to two years under current law) casualty losses attributable to a federally-declared disaster in tax-years 2008-2011. ***The disaster tax relief section would save taxpayers $8.09 billion over ten years.***

- **Energy Tax Extenders:** Extends and expands a variety of tax provisions to incentivize alternative energy. For example, the bill would extend the renewable energy tax credit (2.0 cents per kilowatt/hour for electricity generated from biomass, geothermal, solar, landfill gas, trash combustion, etc., indexed for inflation) for an additional two years. (Just a one-year extension for wind and refined coal.) The bill would also extend the 30% investment tax credit for solar and fuel cell property for commercial use from the end of 2008 to the end of 2016. Additionally, the bill would extend through the end of 2016 the residential solar and fuel cell credit and increases the $2,000-per-taxpayer cap to $4,000. ***The energy tax extenders section would save taxpayers about $15 billion over ten years.***

- **Non-Energy Tax Extenders:** Extends, and in some cases expands, a multitude of non-energy tax provisions for two years (in most cases). Examples of such non-energy tax extenders include:
  --State and Local Sales Tax Deduction.
  --Research and Development Credit.
  --New Markets Credit (for investments in low-income or developing communities).
  --50% Tax Credit for Certain Railroad Track Maintenance Spending.
  --15-Year Depreciation for Leasehold and Restaurant Improvements.
  --7-Year Depreciation for Motorsports Entertainment Complex Improvements.
  --DC Investment Tax Incentives (such as the first-time homebuyer credit).

  This section would also modify and extend for one year the Section 199 domestic manufacturing tax deduction and the special expensing rules for certain U.S. film and TV productions, and would extend for one year the additional standard deduction for state and local real property taxes paid or accrued in tax-year 2009 for people who claim the regular standard deduction. ***The non-energy tax extenders section would save taxpayers about $42 billion over ten years.***

  This section would also reduce the amount above which the portion of a taxpayer's income is refundable under the child tax credit from about $12,000 to $8,500. ***Gives individuals $3.42 billion in one year (scores as mandatory spending).***

Tax Increases: Includes six main tax increases, costing taxpayers about $42 billion over ten years, as partial offsets for the legislation, including:

- **Tax Increase on Energy**: Denies the scheduled increase in the corporate tax deduction for income attributable to the production, refining, processing, transportation, and distribution of oil, natural gas, or any primary product thereof, beginning in 2010, for all oil and gas companies (not just the largest ones). The deduction rate would be permanently frozen at 6%, instead of rising to 9% in 2010, as scheduled under current law.

- **Another Tax Increase on Energy**: Modifies the method by which oil and gas companies calculate their foreign tax credits, beginning in 2008. Specifically, the provision would require foreign-based income to be reclassified as foreign oil and gas extraction income (FOGEI) for purposes of calculating the foreign tax credit and require "arm's-length" pricing for FOGEI. The Republican staff of the Ways & Means Committee notes that the rules governing FOGEI are more stringent than the general rules governing calculation of foreign tax credits, resulting in a smaller overall foreign tax credit for companies with non-U.S. oil and gas production income.

- **Yet Another Tax Increase on Energy**: Increases the Oil Spill Liability Trust Fund tax from 5 cents per barrel to 8 cents per barrel (2009-2016) and to 9 cents per barrel in 2017, while repealing the requirement that the tax be suspended when the unobligated balance in the Fund exceeds $2.7 billion.

- **Cost Basis Reporting**: Requires mandatory cost basis reporting by brokers for transactions involving stocks acquired after January 1, 2011 (January 1, 2012, in the case of mutual funds; January 1, 2013, for all other publicly traded securities).

- **Unemployment Surtax Extension**: Extends the current-law 0.2-percentage-point surtax on the unemployment insurance tax (0.2-percentage-points of the 6.2% gross tax rate on the first $7,000 paid annually by employers to each employee).

- **Deferred Compensation**: Requires hedge fund managers to pay federal income tax on deferred compensation as it accrues, rather than when it's actually paid. In other words, this provision would impose tax on income before it is received.

Payments in Lieu of Taxes Program (PILT): Increases funding for the PILT program that compensates local governments for federal land (which reduces the tax base), within their jurisdictions. Under current law, PILT is a discretionary program with annual funding levels set through the appropriations process. Last year, this program was authorized at $368.3 million and received $228.9 million through the appropriations process. Section 403 of this bill would provide *mandatory* funding for the program from 2008 to 2012. Furthermore, the bill ***directs*** CBO to treat PILT in its budget baseline as if it had been a mandatory program *prior* to passage of the Balanced Budget Act of 1997. Some conservatives may be concerned that this directed scorekeeping provision is a gimmick designed to avoid PAYGO rules.

"Tax Earmarks": As has been reported (and noted by the Senate Steering Committee), the bill contains a number of targeted tax relief provisions that may be construed as being "tax earmarks." According to a document from the Republican Whip's Office, entitled *"Why the Tax Cut Extenders is Not Pork,"* a number of these provisions—although targeted—may constitute sound tax policy. To quote the document (in italics), with regard to a few examples:

- *The extension of a provision on excise tax cover-over of rum made in Puerto Rico and the Virgin Islands but sold in the U.S. is consistent with general tax policy on the treatment of excise taxes paid.*
- *Similarly, a provision extending the provision giving Section 199 manufacturing treatment to manufacturing in Puerto Rico ensures businesses on that island are not treated less favorably than others in the United States and does not apply to any particular set of taxpayers.*

- *A provision on excise taxes on practice arrows used by Boy Scouts and summer camps that costs less than $2 million over ten years is necessary to ensure that the excise tax on these arrows is not greater than the cost of the arrows themselves.*
- *The extension of provisions giving tax benefits for the purchase of mine safety equipment and the training of mine rescue teams are broadly applicable. These were first enacted in the 2006 Tax Relief and Health Care Act, in the wake of serious underground mining accidents.*
- *A provision relating to the Exxon Valdez case is hardly an earmark; it would allow more than 30,000 victims of the oil spill, who are located across the country, to income average eventual damages and to deposit some of those funds in retirement savings vehicles, like IRAs.*
- *A provision extending current law tax relief for railroad track maintenance will allow short-line railroads, of which there are over 500 today, to make track improvements to accommodate the heavier rail cars being used today.*
- *The Wool Trust Fund provision extends a program already in existence to suspend tariffs on wool fabric, thus reducing costs for U.S. suit makers. At the same time, it creates a fund for U.S. wool fabric makers to provide resources to improve their competitiveness.*
- *The extension of faster depreciation for motorsports tracks benefits dozens and dozens of facilities around the country and represents an effort to conform the depreciation period to the useful life of this type of property. Moreover, this is not a permanent tax cut; it instead allows faster recovery of expenses that would otherwise be deductible. As such, the provision costs less over ten years than it does in its first year.*
- *The film and television provision allows a single-year deduction for all film and television productions up to $15 million ($20 million if the costs are incurred in economically depressed areas). The provision is not limited in scope or geography – it applies to all film and television productions throughout the country, in any state. Also, current law limits qualifying films to those produced directly "by the taxpayer," which excludes partnerships and S corporation shareholders. The provision treats these parties consistently with other taxpayers who produce films.*
- *The District of Columbia tax incentives, including a first-time homebuyer's tax credit and other provisions, has helped revitalize large parts of our nation's capital after years of blight and neglect.*
- *The provision relating to economic development in American Samoa affects a population of nearly 60,000 by providing a tax incentive to U.S. companies with income in the Territory. This credit applies equally across industries; eligibility is not limited open to any employer, provided they meet the tests in the bill of being a U.S. company with a possessions' corporation and actually generate income in American Samoa.*
- *Tax incentives for employment and business expenses on or near Indian Reservations are not earmarks. Native Americans and Alaskan Natives make up 2.1 million people in the United States; forty percent of Native Americans live on reservations.*

Summary of Mental Health Parity Provisions:

H.R. 1424 would amend the Internal Revenue Code, the Public Health Service Act, and the Employee Retirement Income Security Act (ERISA) to require equity in the provision of mental health disorder benefits for group health insurance plans that offer both mental health benefits and medical and surgical benefits. Previously, the Mental Health Parity Act—first enacted in 1996, and extended in subsequent legislation—required only that plans choosing to offer both mental health and medical and surgical benefits must have equal annual and lifetime limits on coverage for both types of treatments. Specific details of the federal mandates in the bill include the following:

- **Treatment Limits and Beneficiary Financial Requirements**: Requires group health plans to offer a financial benefit structure for mental and substance abuse disorders that is no more restrictive than the predominant requirements applied to substantially all medical and surgical benefits. The federal mandate would apply to overall coverage limits on treatment (e.g. number of days or visits) as well as deductibles, out-of-pocket limits, and similar beneficiary financial requirements.

- **Expansion of Definition**: Expands the definition of "mental health benefits" subject to the federal mandate to include substance abuse and disorder treatments.

- **Medical Necessity**: Permits plans to make coverage decisions for mental health and substance abuse disorders based on medical necessity criteria, but would require employers and insurers to disclose such criteria pursuant to regulations.

- **Out-of-Network Benefits**: Mandates plans that offer out-of-network insurance coverage for medical and surgical benefits provide out-of-network coverage for mental health benefits in a manner consistent with the financial requirements listed above.

- **Increased Cost Exemption**: Raises the level at which employers whose health insurance costs rise as a result of implementing mental health parity in benefits may claim an exemption from the federal mandate. The bill would exempt employers whose costs due to mental health claims rise by more than 2% in the first year of implementation, and by more than 1% in subsequent years. The more limited version of the Mental Health Parity Act first enacted in 1996 exempted employers whose claim costs rose 1%. Employers with fewer than 50 workers would be exempt from federal mandates under the legislation, consistent with current law.

- **GAO Study**: The bill would require a study by the Government Accountability Office evaluating the law's impact on the cost of health insurance coverage, access to mental health care, and related issues.

Differences from Earlier Legislation: On March 5, 2008, the House by a 268-148 vote passed mental health parity legislation in an earlier version of H.R. 1424. Subsequent negotiations with the Senate made modifications to the House-passed language that incorporated several key provisions in bipartisan Senate legislation (S. 558), and removed some provisions objectionable to conservatives. Specifically, the compromise language in H.R. 1424:

- Retains ERISA pre-emption for the large employers (those with more than 50 employees) subject to the law—states would not have the option of enacting more stringent and conflicting laws and regulations, as was originally proposed;
- Remains silent on codifying classes of mental disorders—the compromise language removes earlier provisions requiring group health plans to offer coverage for all disorders under the Diagnostic and Statistical Manual of Mental Disorders, including psycho-sexual disorders many conservatives find objectionable;

- Does not mandate an out-of-network coverage benefit—plans must offer out-of-network coverage for mental disorders only to the extent they do so for medical and surgical benefits; and
- Includes language stating that mental health parity provisions do not affect the "terms and conditions" of insurance contracts to the extent they do not conflict with the bill language—permitting employers and carriers to continue making medical necessity and related determinations—while requiring plans to make information on these medical management practices transparent.

While some conservatives may still have concerns with the mandates imposed by mental health parity legislation and the way in which these mandates would increase health insurance premiums, some segments of the business community have embraced the compromise as a reasonable attempt to achieve the goal of both bills without eroding ERISA pre-emption or imposing undue restrictions on benefit plan design.

Additional Background on Benefit Mandates: Since the 1960s, state legislatures have considered—and adopted—legislation requiring health insurance products sold within the state to cover various products and services. These benefit mandates are frequently adopted at the behest of disease groups advocating for coverage of particular treatments (e.g. mammograms) or physician groups concerned that patients have access to specialists' services (e.g. optometrists).

A recent survey by the Council for Affordable Health Insurance found that as of 2007, states had enacted a total of 1,961 mandates for benefits and services—an increase of 60 (more than one per state) when compared to the 2006 total. The number of state mandates varies from a low of 15 in Idaho to a high of 64 in Minnesota. However, because employer-sponsored health insurance is pre-empted from state-based laws and regulations under the Employee Retirement Income Security Act of 1974 (ERISA), benefit mandates do not apply to employers who self-fund their health insurance plans—one reason why H.R. 1424 seeks to impose those mandates on group plans (as well as state-regulated individual plans) on the federal level.

The cost and impact of benefit mandates on health insurance premiums have been the subject of several studies in recent years. For instance, the Heritage Foundation prepared an analysis suggesting that each individual benefit mandate could raise the cost of health insurance premiums by $0.75 monthly. Although the cost of a single mandate appears small, the aggregate impact—particularly given the recent growth of benefit mandates nationwide—can be significant: For instance, Massachusetts' 43 benefit mandates would raise the cost of health insurance by more than $30 monthly under the Heritage analysis.

Although well-intentioned, some conservatives may question the argument made by groups who advocate for benefit mandates: that individuals ***should go without health insurance entirely*** rather than purchase coverage lacking the "consumer protection" of dozens of mandates. In addition, some conservatives note that the prospect of increasing the number of uninsured due to rising premium costs resulting from benefit mandates may precipitate a "crisis" surrounding the uninsured, increasing calls for a government-run health system. In short, many conservatives may believe individuals should have the "consumer protection" ***to*** purchase the insurance plan they desire—rather than the "protection" ***from*** being a consumer by a government which seeks to define their options, and raise the cost of health insurance in the process.

Conservative Concerns: Several aspects of this section of H.R. 1424 may raise concerns for conservatives, including, but not necessarily limited to, the following:

- **Increase Health Insurance Costs and Number of Uninsured**: As noted above, benefit mandates generally have the effect of increasing the cost of health insurance. Moreover, some estimates suggest that every 1% increase in premium costs has a corresponding increase in the number of uninsured by approximately 200,000-300,000 individuals nationwide. Therefore, some conservatives may be concerned that H.R. 6983 will actually increase the number of uninsured Americans.

- **Private-Sector Mandates on Businesses; UMRA Violation**: As detailed above, the bill contains multiple new federal mandates on the private sector, affecting the design and structure of health insurance plans. CBO has previously estimated that mental health parity would impose mandates on the private sector totaling $1.3 billion in 2008, rising to $3 billion in 2012, thus exceeding the annual threshold established in the Unfunded Mandates Reform Act or UMRA ($131 million in FY2007, adjusted annually for inflation). These costs will ultimately be borne by employers offering health insurance and employees seeking to obtain coverage.

Cost to Taxpayers of Mental Health Parity: The Joint Committee on Taxation estimates that the mental health provisions would cost the federal $1.3 billion over five years, and $3.9 billion over ten. Most of this cost would stem from a decline in federal revenues due to increases in the cost of health insurance, as employees with group coverage would exclude more of their income from payroll and income taxes; the balance of the costs would stem from direct federal outlays increasing due to higher costs for the Medicare and Medicaid programs.

Does the Bill (All Divisions) Expand the Size and Scope of the Federal Government? Yes, the federal government would now be purchasing billions of dollars worth of troubled securities and imposing new federal mandates with respect to health insurance coverage requirements.

Does the Bill Comply with House Rules Regarding Earmarks/Limited Tax Benefits/Limited Tariff Benefits? A Committee report designating compliance with clause 9 of rule XXI is unavailable.

Constitutional Authority: A Committee report citing Constitutional authority is unavailable. House Rule XIII, Section 3(d)(1), requires that all committee reports contain a statement citing the *specific* powers granted to Congress in the Constitution to enact the law proposed by the bill or joint resolution. *[emphasis added]*

Staff Contacts:

Division A	Russ Vought, 202-226-8681, russ.vought@mail.house.gov
Division B-C	Paul Teller, 202-226-9718, paul.teller@mail.house.gov
Mental Health Parity	Chris Jacobs, 202-226-8585, christopher.jacobs@mail.house.gov