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Budget Materials - Tax Proposals FY99

Budget - tax proposals FY99

Kate P. Donovan
09/30/98 06:23:12 PM

Record Type: Record

To: See the distribution list at the bottom of this message

cc:
Subject: DRAFT SENATE TAX SAP (HR 4579)

This week, the Senate is expected to begin consideration of H.R. 4579 - Taxpayer Relief Act. We turned the House floor SAP that was released on 9/25/98 into a Senate SAP. The only change is in the 2nd par (in bold for your review). Please provide comments/clearance by 11am tomorrow (Thurs.). Thank you.

September 30, 1998
(Senate)

H.R. 4579 - Taxpayer Relief Act of 1998
(Archer (R) Texas)

The Administration strongly opposes H.R. 4579. If the bill were presented to the President, either as a stand-alone bill or combined with other legislation, he would veto it. By draining billions out of projected budget surpluses, this bill violates the President's unwavering commitment to save Social Security first. None of the surpluses should be touched until the long-term solvency of Social Security has been fully secured. We must not squander this unique opportunity to save Social Security.

Last February in the FY 1999 Budget, the President proposed tax cuts targeted to help American families -- and proposed offsets to fully pay for the tax cuts. The Administration urges the Congress to consider tax cuts only if we can do so in a manner that **-- like the Democratic substitute --** adheres to the budget rules, maintains fiscal discipline, and meets the President's commitment to reserve the entire surplus until we have strengthened Social Security.

H.R. 4579 would cut taxes by $85 billion over five years and $176 billion over 10 years. Virtually none of the bill's costs have been paid for. This blatantly violates the pay-as-you-go fiscal discipline of the Budget Enforcement Act -- discipline which has been an essential component of our remarkable economic revival.

The bill's exemption from the Budget Enforcement Act evades this fiscal discipline. The Administration strongly opposes this exemption from the fundamental budget laws.

Senate Democrats -- Possible Alternative

Budget - tax proposals FY99

Key Components:

- **Marriage Penalty**
    - Same as Daschle amendment to tobacco bill.
    - 20% second earner deduction; phased out for couples with incomes between $50,000-60,000.
    - $7 billion over five years.

- **Self-employed health**
    - Accelerate 100% deduction -- they may do it over two years.
    - $4 billion over five years.

- **School construction**
    - Our proposal.
    - $3 billion over five years (JCT scoring)

- **Extenders**
    - Through 12/31/99 (Archer has two more months). R&D tax credit; Welfare-to-work; WOTC; Contributions of appreciated stock to private foundations.
    - $4-5 billion over five years

- **Low Income Housing Tax Credit**
    - Considering including our proposal.
    - $1 billion over five years.

- **Farmers**
    - Similar to Archer package, slightly sweetened.
    - Components include extend permanently income averaging; carryback of net operating losses (7 years); accelerate $25,000 expensing just for farmers.
    - Roughly $1 billion over five years.

- **TOTAL $20-25 billion roughly over five years (JCT)**

From our Budget:

IN:

- School Construction
- Possibly Low Income Housing Tax Credit
- Extenders

OUT:
- Climate Change
- Child Care
- Pensions

Raisers:

- Currently they are at around $17-18 billion in pay-fors over five years. We are working with them on additional (Raisers include REITs, Superfund, other cats and dogs from our budget)

Issues:

- Long-term care -- Final decision to keep it out?

- Marriage Penalty -- is it big enough?

- Overall guidance for Senate Democrats:

  1) Focused approach for clarity of message (bigger marriage penalty, school construction, extenders).

  2) Broader approach -- possibly diluted but it would include more our proposals, such as low income housing tax credit.

Budget-tax proposals FY99

DRAFT --- NOT FOR RELEASE

September xx, 1998
(House)

H.R. 4579 - Taxpayer Relief Act of 1998
(Archer (R) Texas)

The Administration strongly opposes H.R. 4579. If the bill were presented to the President, he would veto it.

H.R. 4579 would cut taxes by $85 billion over five years and $176 billion over 10 years. With the exception of only one offsetting provision, none of the bill's costs have been paid for. This blatantly violates the pay-as-you-go fiscal discipline of the Budget Enforcement Act -- discipline which has been an essential component of our remarkable economic revival. The President will veto any tax cut or spending bill that changes the budget rules in order to evade fiscal discipline.

In addition, the billions of dollars this bill would drain out of projected budget surpluses violates the President's unwavering commitment to save Social Security first. None of the projected surpluses should be touched until the long-term solvency of Social Security has been fully secured. We must not squander this unique opportunity to save Social Security.

Last February in the FY 1999 Budget, the President proposed tax cuts targeted to help American families -- and proposed offsets to fully pay for the tax cuts. The Administration urges the Congress to return to the path of fiscal responsibility and to consider only tax cuts which have been fully paid for.

Pay-As-You-Go-Scoring

H.R. 4579 would affect revenues; therefore it is subject to the pay-as-you-go requirement of the Budget Enforcement Act. Under the Budget Enforcement Act, OMB would be required by law to impose automatic spending cuts on Medicare and other non-exempt mandatory spending programs in amounts sufficient to offset the revenue losses projected for FY 1999. In the absence of offsetting legislation, these automatic budget cuts would be triggered again in each of the following four years. These automatic cuts would affect: the special milk program, vocational rehabilitation, Stafford loans, foster care and adoption assistance, Medicare (up to 4 percent), and could also affect CCC, Child Support Enforcement, Social Services Block Grants, Immigration Support, Crop Insurance, Veterans Education and Readjustment Benefits, and others.

Budget - tax proposals FY99

Kate P. Donovan
09/24/98 02:45:20 PM

Record Type: Record

To: See the distribution list at the bottom of this message

cc:
Subject: REVISED TAXPAYER SAP

We have revised the draft SAP that was circulated yesterday on H.R. 4579 - Taxpayer Relief Act of 1998. The new language is in bold (please note the revised veto threat in the 2nd sentence). We still aim to get the SAP to the Hill this evening. Please provide comments by 5:30pm tonight.

Also, we aim to release the SAP for H.R. 4578 - Save Social Security Act of 1998 at the same time. The draft that was circulated yesterday has not been modified at all. Please call me as soon as possible if you have any problems with that SAP as well. Thank you.

H.R. 4579 - Taxpayer Relief Act of 1998
(Archer (R) Texas)

The Administration strongly opposes H.R. 4579. If the bill were presented to the President, **either as a stand-alone bill or combined with other legislation**, he would veto it. By draining billions out of projected budget surpluses, this bill violates the President's unwavering commitment to save Social Security first. None of the projected surpluses should be touched until the long-term solvency of Social Security has been fully secured. We must not squander this unique opportunity to save Social Security.

Last February in the FY 1999 Budget, the President proposed tax cuts targeted to help American families -- and proposed offsets to fully pay for the tax cuts. The Administration urges the Congress to consider tax cuts only if we can do so in a manner that adheres to the budget rules, maintains fiscal discipline, and meets the President's commitment to reserve the entire surplus until we have strengthened Social Security.

H.R. 4579 would cut taxes by $85 billion over five years and $176 billion over 10 years. Virtually none of the bill's costs have been paid for. This blatantly violates the pay-as-you-go fiscal discipline of the Budget Enforcement Act -- discipline which has been an essential component of our remarkable economic revival.

Without offsets, the only way to avoid an automatic budget sequester is to spend the surplus. We oppose this bill because neither spending the surplus nor a sequester is acceptable. Any tax cut should be offset.

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Budget - Tax proposals FY99

Kate P. Donovan
09/23/98 03:59:31 PM

Record Type: Record

To: See the distribution list at the bottom of this message

cc:
Subject: Draft SAP: H.R. 4578 - Save Social Security Act of 1998

The House Rules Committee plans to meet tomorrow with floor action scheduled Friday, 9/25 regarding H.R. 4578 - Save Social Security Act of 1998. Please review the draft SAP with the position, **Senior Advisers Veto Recommendation** and provide comments/clearance by 10am tomorrow morning. Thank you.

DRAFT - NOT FOR RELEASE

September 23, 1998
(House)

H.R. 4578 - Save Social Security Act of 1998
Rep. Archer (R) TX

H.R. 4578 violates the President's pledge to save Social Security first. It calls for tens of billions of dollars to be drained out of projected budget surpluses before any action has been taken to strengthen Social Security for the long term or those surpluses happen. The President firmly believes that none of the projected surpluses should be touched until the long-term solvency of Social Security has been fully secured.

The unique opportunity to save Social Security must not be squandered. The Administration, therefore, strongly opposes H.R. 4578. If the bill were presented to the President in its current form, he would veto it.

* * * * * * *

(Do Not Distribute Outside the Executive Office of the President)

This Statement of Administration Policy (SAP) was developed by the Legislative Reference Division (Haskins) in consultation with Director Lew, Associate Directors Chow and Minarik, Assistant Director Emery, EIML (Smalligan/Sauer), OIRA (Chenok), BASD (Lind/Kilpatrick/Locke), OMB-LA (Konigsberg), and BRCD (Rea/Moran) as well as the White House Office of Policy Development (Rice) and the National Economic Council (Orszag/Marr/Liebman). The Departments of Health and Human Services (Wallace), Justice (Jones), Labor (McCarthy), the Treasury (Dorsey) and the Social Security Administration (Chesser) concur in this position.

OMB/LA clearance:

Background

In his January 27, 1998, State of the Union Address, the President proposed that 100 percent of the Social Security surplus be reserved "until we have taken all the necessary measures to strengthen the Social Security System for the 21st century." He announced his schedule for achieving Social Security reform, inviting every American to participate in the reform process. The President called for nonpartisan regional forums followed by a White House Conference on Social Security in December 1998. In addition, the President declared that he would convene the leaders of Congress to draft "bipartisan" Social Security reform legislation in January 1999.

Summary of H.R. 4578

H.R. 4578 was introduced on September 16, 1998, and ordered reported, as amended, by the House Committee on Ways and Means on September 17, 1998.

Within ten days of enactment, H.R. 4578 would require the Secretary of the Treasury, in consultation with the OMB Director, to project the estimated total Federal budget surplus during each of FYs 1998 through 2008. At the end of each of those fiscal years, the bill would require the Treasury Department to transfer funds from the General Fund into a special reserve account, the "Protect Social Security Account", an amount totaling 90 percent of the Federal budget surplus projected by the Department for that period. As under current law, the funds would be invested in non-marketable securities.

H.R. 4578 would define "total" Federal budget to include all spending and receipt accounts of the United States Government that are designated as "on-budget" or "off-budget" accounts.

According to OMB's Budget Review Division:

-- The 90 percent of the surplus for FYs 1998-2008 that is to be transferred to the Treasury "Protect Social Security" account would increase the debt subject-to-limit. Based on the estimates in the Mid-Session Review, H.R. 4578 would require that the debt limit be raised during the fall of 2000, two years earlier than under existing law.

-- Other than raising the debt subject-to-limit, the account has no effect on the budget totals and the "lock-box" does not prevent the Government from spending more than ten percent of the surplus for tax cuts or other purposes.

-- The Joint Committee on Taxation estimates that H.R. 4579, the Taxpayer

Relief Act of 1998, would cost slightly more than ten percent of the cumulative surpluses even before considering the additional debt service costs associated with the tax cuts. If the current surplus projections were to be optimistic, the amounts available to protect Social Security would be well below the ninety percent that H.R. 4578 would place in reserve.

Pay-As-You-Go

According to the Income Maintenance Branch (Sauer), H.R. 4578 would not affect direct spending or receipts; therefore, it is not subject to the pay-as-you-go requirements of the Omnibus Budget Reconciliation Act of 1990.

LEGISLATIVE REFERENCE DIVISION
September 23, 1998 - 12:05 p.m.

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Budget- tax proposals FY99

Kate P. Donovan
09/23/98 05:02:40 PM

Record Type: Record

To: See the distribution list at the bottom of this message

cc:

Subject: H.R. 4579 - Taxpayer Relief Act of 1998

The House Rules Committee also plans to take up H.R. 4579 - Taxpayer Relief Act of 1998 tomorrow with House floor action possible Friday, 9/25. Position: **POTUS will Veto.** Please review and provide changes/clearance to me by 11am tomorrow. Many thanks.

DRAFT --- NOT FOR RELEASE

September xx, 1998
(House)

H.R. 4579 - Taxpayer Relief Act of 1998
(Archer (R) Texas)

The Administration strongly opposes H.R. 4579. If the bill were presented to the President, he would veto it.

H.R. 4579 would cut taxes by $85 billion over five years and $176 billion over 10 years. Virtually none of the bill's costs have been paid for. This blatantly violates the pay-as-you-go fiscal discipline of the Budget Enforcement Act -- discipline which has been an essential component of our remarkable economic revival. The President will veto any tax cut or spending bill that undermines fiscal discipline by changing the budget rules.

In addition, by draining billions out of projected budget surpluses, this bill violates the President's unwavering commitment to save Social Security first. None of the projected surpluses should be touched until the long-term solvency of Social Security has been fully secured. We must not squander this unique opportunity to save Social Security.

Last February in the FY 1999 Budget, the President proposed tax cuts targeted to help American families -- and proposed offsets to fully pay for the tax cuts. The Administration urges the Congress to consider tax cuts only if we can do so in a manner that adheres to the budget rules, maintains fiscal discipline, and meets the President's commitment to reserve the entire surplus until we have strengthened Social Security.

Pay-As-You-Go-Scoring

H.R. 4579 would affect revenues; therefore it is subject to the pay-as-you-go requirement of the Budget Enforcement Act. Under the Budget Enforcement Act, OMB would be required by law to impose automatic spending cuts on Medicare and other non-exempt mandatory spending programs in amounts sufficient to offset the revenue losses projected for FY 1999. In the absence of offsetting legislation, these automatic budget cuts would be triggered again in each of the following four years. These automatic cuts would affect: the special milk program, vocational rehabilitation, Stafford loans, foster care and adoption assistance, Medicare (up to four percent), and could also affect CCC, Child Support Enforcement, Social Services Block Grants, Immigration Support, Crop Insurance, Veterans Education and Readjustment Benefits, and others. ***[Note: the last sentence in this paragraph may need to be revised or deleted following Rules Committee action.]***

* * * * * * * *

(Do Not Distribute Outside Executive Office of the President)

This Statement of Administration Policy was developed by the Legislative Reference Division (Jones), in consultation with the Departments of the Treasury (Dorsey), Justice (Jones), the Social Security Administration (Chesser), the Council of Economic Advisers (Elmendorf), OMB Economic Policy (Minarik), and BASD (Lind, Barth).

The National Economic Council, the Office of White House Counsel, White House Legislative Affairs, OMB GC, HTFD, and OIRA did not respond to our request for comments on the draft SAP.

OMB/LA Clearance:

The House Committee on Ways and Means ordered H.R. 4579 reported by a vote of 23-15, on Sept. 17, 1998.

Administration Position to Date

The President, in a speech to the International Brotherhood of Electrical Workers on September 17th, stated that he would veto any bill "that squanders the surplus on tax cuts before we save social security."

Summary of H.R. 4579

The principal provisions of H.R. 4579, as reported, are described below.

-- Tax Provisions

Reduce the so-called "marriage penalty" by increasing the standard deduction couples can claim from approximately $7,200 to $8,600 (effective for tax years beginning after December 31, 1998);

Make the increase from $625,000 to $1 million of the unified estate tax and gift tax exclusion effective after December 31, 1998. Currently, that exclusion is to increase gradually to $1 million in 2006;

Eliminate Federal income taxes on the first $400 of interest income for couples and $200 for singles (effective for tax years beginning after December 31, 1998);

Allow certain nonrefundable personal tax credits (e.g., child credits, HOPE and lifetime learning credits) to offset an individual taxpayer's minimum tax liability as well as their regular tax liability. (Current law permits these credits to be applied only against the regular tax liability);

Make health insurance costs for self-employed individuals fully deductible, retroactive to January 1, 1998. Current law would make these costs fully deductible for tax years beginning January 1, 2007;

Extend the research tax credit (expired 7/1/98), the Work Opportunity tax credit (7/1/98), and the Welfare-to-Work tax credit (4/30/99) to February 29, 2000; and

Increase the maximum amount of annual investment in qualified property by a small business to $25,000 for taxable years beginning after December 31, 1998. Current law phases in an increase from the current maximum of $18,500 to $25,000 over five years;

Designate 20 "renewal communities" and make businesses in these areas eligible for various forms of tax relief;

Permit private higher education institutions to establish tax-free prepaid tuition programs (Currently, only public institutions may establish such programs);

-- <u>Trade and Tariff Provisions</u>

Extend the Generalized System of Preferences (GSP), which expired on June 30, 1998, to February 29, 2000;

-- <u>Revenue Offsets</u>

Include in the income of certain shareholders dividends distributed to liquidate a real estate invest trust or regulated investment company.

-- <u>Social Security Provisions</u>

Increase to $37,941 in 2008 the amount a social security recipient between the age of full retirement (currently 65) and 70 years old can earn before their benefit amount is reduced. Currently, that amount is $14,500.

Delay the recomputation of benefits for social security recipients who continue to work after normal retirement age until January 1st of the second year following the year of the earnings.

Pay-As-You-Go Scoring

According to BASD (Barth) and the Treasury, H.R. 4579 would affect receipts, and therefore, it is subject to the pay-as-you go rules of the Omnibus Budget Reconciliation Act (OBRA) of 1990. H.R. 4579 would result in net budget costs of $10.6 billion in FY 1999 and $85.5 billion over FYS 1999-2003. The Joint Committee on Taxation estimates that the bill will reduce revenues by $6.6 billion in FY 1999 and $80.1 billion over FYs 1999-2003.

LEGISLATIVE REFERENCE DIVISION
September 23, 1998 - 11:30 AM

Message Sent To:

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Budget — Tax proposals FY99 From 7/10 tax mtg

Possible Democratic Package

A fully paid for Democratic package of tax cuts would likely include a core set of tax cut proposals on marriage penalties, school construction, and extension of expiring tax provisions. Additional proposals could be included to fit available remaining revenues from payfors. A menu of potential tax initiatives is given on **page 2** of the handout.

The revenue raisers listed on **page 3** have been grouped into three categories, plus tobacco. The first grouping is "relatively noncontroversial" items, totaling **$3.5 billion** through 2003. These items have been included in bipartisan tax legislation this year. The second category, totaling **$15.3 billion** through 2003, lists "less noncontroversial" raisers. Given that a tax package needs to be financed, our subjective assessment is that these would be likely additional payfors. The third category (split into two groups) is labeled "controversial." These items would have significant opposition.

Illustrative Packages:

Illustrative package 1 (on **page 4**) includes only the core tax cut proposals: a phased in marriage penalty proposal (that eventually raises the standard deduction for joints filers to twice that of singles), a school construction initiative, and extensions of expiring provisions. The core tax cuts cost **$25.8 billion** through 2003. The first two categories of raisers total **$18.8 billion** through 2003. We have assumed that the reinstatement of the two Superfund environmental taxes are used to make up the difference in the cost of cuts and payfors.

Illustrative package 2 (on **page 5**) adds child care, pension and low-income housing initiatives to the core set of tax cuts. It pays for the additional tax cuts with a 20 cent per pack increase in the cigarette excise tax through 2002 and a 30 cents per pack increase thereafter.

Discussion

Financing even the base package will involve tough choices. Some will object strongly to using the Superfund taxes to pay for tax cuts rather than environmental remediation. A likely alternative, replacing the sales source rule with activity-based rules (which has been in the President's budget the last two years), will be opposed by some who worry that this change could harm international competitiveness.

The financing constraint <u>may</u> be somewhat easier under Joint Committee scoring. Because of baseline differences, the JCT scores the liquidating REIT proposal as raising $4.4 billion more than Treasury through 2003 (and $7.6 billion more through 2008). Cutting the other way, the JCT has not scored the President's budget proposal to modify reserve rules for annuity contracts (CARV-M), which complicates inclusion in a Congressional package. The CARV-M proposal, which affects life insurance companies, would raise $4.6 billion through 2003 and $8.5 billion through 2008.

Menu for Potential Democratic Tax Package
Tax Cuts

	1998-2003	1998-2008
*Core Initiatives (** indicates very rough estimate)*		
Marriage Penalty Relief /1		
Increase the standard deduction for joint filers to double that for singles	-25,846	-55,634
Introduce a 10% second-earner deduction (up to $30k of earnings)**	-60,000	-120,000
Reduce EITC marriage penalties**	-10,000	-20,000
Gramm, Senate-passed marriage penalty proposal (already phased in) /2	-14,400	-38,600
School Construction		
School construction bonds, increase Qualified Zone Academy Bonds	-5,007	-11,552
Extend Expiring Provisions		
R&E tax credit (6/30/99) /3	-2,209	-2,218
Work Opportunity Tax Credit (4/31/00)	-783	-806
Welfare-to-Work tax credit (4/31/00)	-169	-181
Contributions of stock to private foundations (6/30/99)	-67	-67
*Additional Items if Payfors are Available (** indicates very rough estimate)*		
Make Child Care More Affordable		
Increase child and dependent care tax credit	-5,113	-11,785
Employer-provided child-care tax credit	-478	-1,268
Kennelly stay-at-home parent credit**	-3,500	-7,000
Extend Availability of Pensions /4		
3-Year subsidy plus voluntary excludable IRA -- small firms and all qualified plans	-508	-945
Simplified pension plan for small business	-304	-555
Other Pension Initiatives	-145	-395
Education Initiatives		
Extend employer-provided educational assistance and include graduate education	-1,049	-1,049
Increase Low-Income Housing Tax Credit and Urban Initiatives		
Increase per capita cap to $1.75	-1,559	-6,723
Accelerate startup of two new EZ/ECs	-63	-150
Make permanent the expensing of brownfields remediation costs	-534	-1,338
Increase Energy Efficiency and Improve the Environment		
President's climate change technology tax initiative	-3,625	-9,006
Speedup of Self-Employed Health Insurance Deduction		
Acceleration of self-employed health insurance deduction	-5,500	-8,100
Assist Taxpayers with Long-Term Care Needs		
Extend child credit to taxpayers with chronic illness and ill spouse or dependent	-4,700	-11,400
Same provision as above, but $1,000 rather than $500 credit	-9,000	-21,600
$1,000 credit for home or community care	-4,700	-11,800
Capped, 75 percent tax credit for qualified long-term care expenses	-4,600	-10,500
Simplify and Enhance the Progressivity of Capital Gains Taxation		
40 percent exclusion for long-term capital gains	-8,000	-9,000

/1 Each marriage penalty proposal can be "dialed down" to meet a smaller revenue target
/2 JCT scores this as costing $16.1b through 2003 and roughly $46b through 2008
/3 Numbers do not match the Budget because this entry includes costs in 1998 (this is $365 million)
/4 Numbers do not match the Budget because this entry includes costs in 1998 ($42 million)

Revenue Offsets
[$ in millions]

		1998-2003	1998-2008
Relatively Noncontroversial			
Modify Foreign Tax Credit carryover rules*	/1	1,925	3,391
Clarify and expand math-error procedures	/1	672	1,400
Liquidating REITs	/2	500	1,000
Constructive ownership (Kennelly)*		150	300
Clarify the meaning of "subject to" liabilities under section 357(c)	/1	120	439
Restrict special net operating loss carryback rules for specified liability losses	/1	104	255
Subtotal		3,471	6,785
Less Noncontroversial			
Modify reserve rules for annuity contracts (CARV-M)	/3	4,641	8,532
Modify corporate-owned life insurance (COLI) rules		2,455	5,253
Repeal lower-cost-or-market inventory accounting method		1,663	1,947
Reform treatment of FOGI and dual capacity taxpayers*		1,500	3,900
Reinstate Oil Spill excise tax		1,255	2,576
Eliminate non-business valuation discounts		1,008	2,468
Repeal percentage depletion for nonfuel minerals on Federal and formerly Federal lands		478	1,003
Increase proration percentage for P&C insurance companies		380	1,331
Amend 80/20 company rules		249	526
Modify treatment of foreign built-in losses		243	547
Defer deduction for interest and OID on convertible debt		166	549
Eliminate dividends-received deduction for certain preferred stock		157	611
Tighten substantial understatement penalty for large corporations		147	241
Repeal tax-free conversions of large C corporations into S corporations		144	602
Apply 7.7% rate to credit life insurance premiums		125	140
Repeal 14-day rule for vacation homes*		123	274
Extend pro-rata disallowance of tax-exempt interest expense to all financial intermediaries		109	293
Reduce "investment in the contract" for mortality and expense charges		100	1,360
Eliminate "Crummey" rule		87	213
Impose excise tax on purchase of structured settlements		82	212
Increase penalties for failure to file correct information returns		65	131
Modify depreciation method for tax-exempt use property		55	261
Modify foreign office material participation exception		50	111
Stop abuse of CFC exception to ownership requirements of IRS code section 887		30	59
Eliminate gift tax exemption for personal residence trusts		25	525
Include QTIP trust assets in surviving spouse's estate		8	21
Modify Federal Unemployment Act provisions		0	1,511
Subtotal		15,345	35,197
Controversial Ideas			
Replace sales source rule with activity-based rules (subset of Title Passage, below)		6,571	16,273
Superfund AMT tax*		3,800	5,000
Superfund excise tax*		3,600	5,000
Royalties in passive basket of foreign tax credit; 100% R&E allocation +		3,000	6,000
Reduce dividends-received deduction to 50%		1,662	3,835
Variable annuities		929	5,089
Repeal components of cost inventory method		895	2,071
Deny interest deduction on certain debt instruments		649	2,691
Subtotal		21,106	45,959
Controversial CBO & Congressional Ideas			
Excise tax on nonretirement fringe benefits (McDermott) +		**28,900**	**57,800**
Title Passage, tax repatriated FSC income+		**24,100**	**59,683**
Repeal expensing of exploration and development costs+		**4,400**	**9,100**
Repeal percentage depletion +		**2,400**	**5,100**
Minimum tax on foreign-owned business+		**1,800**	**3,600**
Runaway plants (Dorgan) +		**1,500**	**3,000**
Subtotal		**63,100**	**138,283**
Tobacco			
Accelerate cigarette excise tax increase +		3,000	3,000
10-cent tobacco excise tax (could be scaled up) +		7,500	15,000
Disallow deduction for tobacco advertising +		4,000	8,200
Subtotal		14,500	26,200

* = JCT scoring
+ = rough guess
1. Used in the Senate's version of IRS Restructuring
2. JCT estimates at 4.9 b over five years, 8.6 b over 10 years
3. JCT has not estimated this provision

Tax Package I

Tax Cuts

*(** indicates very rough estimate)*

		1998-2003	1998-2008
Marriage Penalty Relief			
Raise joint standard deduction to twice singles (flat phase-in, jump in 2009)**		-18000	-37000
School Construction			
School construction bonds, increase Qualified Zone Academy Bonds		-5,007	-11,552
Extend Expiring Provisions			
R&E tax credit (6/30/99)		-2,209	-2,218
Work Opportunity Tax Credit (4/31/00)		-783	-806
Welfare-to-Work tax credit (4/31/00)		-169	-181
Contributions of stock to private foundations (6/30/99)		-67	-67
Subtotal		-3,228	-3,272
Total		-26,235	-51,824

Raisers

		1998-2003	1998-2008
Relatively noncontroversial			
Modify Foreign Tax Credit carryover rules	/1	1,925	3,391
Liquidating REITs**	/2	500	1,000
Clarify and expand math-error procedures	/1	672	1,400
Constructive ownership (Kennelly)**		150	300
Clarify the meaning of "subject to" liabilities under section 357(c)	/1	120	439
Restrict special net operating loss carryback rules for specified liability losses	/1	104	255
Subtotal		3,471	6,785
Less noncontroversial			
Modify reserve rules for annuity contracts (CARV-M)	/3	4,641	8,532
Modify corporate-owned life insurance (COLI) rules		2,455	5,253
Repeal lower-cost-or-market inventory accounting method		1,663	1,947
Reform treatment of FOGI and dual capacity taxpayers**		1,500	3,900
Reinstate Oil Spill excise tax		1,255	2,576
Eliminate non-business valuation discounts		1,008	2,468
Repeal percentage depletion for nonfuel minerals on Federal and formerly Federal lands		478	1,003
Increase proration percentage for P&C insurance companies		380	1,331
Amend 80/20 company rules		249	526
Modify treatment of foreign built-in losses		243	547
Defer deduction for interest and OID on convertible debt		166	549
Eliminate dividends-received deduction for certain preferred stock		157	611
Tighten substantial understatement penalty for large corporations		147	241
Repeal tax-free conversions of large C corporations into S corporations		144	602
Apply 7.7% rate to credit life insurance premiums		125	140
Repeal 14-day rule for vacation homes**		123	274
Extend pro-rata disallowance of tax-exempt interest expense to all financial intermediaries		109	293
Reduce "investment in the contract" for mortality and expense charges		100	1,360
Eliminate "Crummey" rule		87	213
Impose excise tax on purchase of structured settlements		82	212
Increase penalties for failure to file correct information returns		65	131
Modify depreciation method for tax-exempt use property		55	261
Modify foreign office material participation exception		50	111
Stop abuse of CFC exception to ownership requirements of IRS code section 887		30	59
Eliminate gift tax exemption for personal residence trusts		25	525
Include QTIP trust assets in surviving spouse's estate		8	21
Modify Federal Unemployment Act provisions		0	1,511
Subtotal		15,345	35,197
Controversial			
Superfund AMT tax		3,800	5,000
Superfund excise tax		3,600	5,000
Subtotal		7,400	10,000
Total		26,216	51,982
Net Budget Effect		-19	158

1. Used in the Senate's version of IRS Restructuring
2. JCT estimates at 4.9 b over five years, 8.6 b over 10 years
3. JCT has not estimated this provision

Tax Package II

Tax Cuts

*(** indicates very rough estimate)*

			1998-2003	1998-2008
Marriage Penalty Relief				
Raise joint standard deduction to twice singles (phased-in) **			-24,000	-51,000
School Construction				
School construction bonds, increase Qualified Zone Academy Bonds			-5,007	-11,552
Extend Expiring Provisions				
R&E tax credit (6/30/99)			-2,209	-2,218
Work Opportunity Tax Credit (4/31/00)			-783	-806
Welfare-to-Work tax credit (4/31/00)			-169	-181
Contributions of stock to private foundations (6/30/99)			-67	-67
	Subtotal		-3,228	-3,272
Make Child Care More Affordable				
Increase child and dependent care tax credit			-5,113	-11,785
Employer-provided child-care tax credit			-478	-1,268
	Subtotal		-5,591	-13,053
Extend Availability of Pensions				
3-Year subsidy plus voluntary excludable IRA -- small firms and all qualified plans			-508	-945
Simplified pension plan for small business			-304	-555
Other Pension Initiatives			-145	-395
	Subtotal		-957	-1,895
Increase Low-Income Housing Tax Credit and Urban Initiatives				
Increase per capita cap to $1.75			-1,559	-6,723
Accelerate startup of two new EZ/ECs			-63	-150
Make permanent the expensing of brownfields remediation costs			-534	-1,338
	Subtotal		-2,156	-8,211
	Total		-40,939	-88,983

Raisers

			1998-2003	1998-2008
Relatively noncontroversial				
Modify Foreign Tax Credit carryover rules		/1	1,925	3,391
Liquidating REITs**		/2	500	1,000
Clarify and expand math-error procedures		/1	672	1,400
Constructive ownership (Kennelly)**			150	300
Clarify the meaning of "subject to" liabilities under section 357(c)		/1	120	439
Restrict special net operating loss carryback rules for specified liability losses		/1	104	255
	Subtotal		3,471	6,785
Less noncontroversial				
Modify reserve rules for annuity contracts (CARV-M)		/3	4,641	8,532
Modify corporate-owned life insurance (COLI) rules			2,455	5,253
Repeal lower-cost-or-market inventory accounting method			1,663	1,947
Reform treatment of FOGI and dual capacity taxpayers**			1,500	3,900
Reinstate Oil Spill excise tax			1,255	2,576
Eliminate non-business valuation discounts			1,008	2,468
Additional offsets under $500 m through 2003; identical to package I			2,823	10,521
	Subtotal		15,345	35,197
Controversial				
Superfund AMT tax			3,800	5,000
Superfund excise tax			3,600	5,000
	Subtotal		7,400	10,000
Tobacco				
20-cent per pack excise tax increase through 2002, 30 cents thereafter			15,000	37,500
	Total		41,216	89,482
	Net Budget Effect		277	499

1. Used in the Senate's version of IRS Restructuring
2. JCT estimates at 4.9 b over five years, 8.6 b over 10 years
3. JCT has not estimated this provision

Elements of a Democratic Package

A fully paid for Democratic package of tax cuts would likely include a core set of proposals on marriage penalties, school construction, and expiring tax provisions. Additional proposals would be included, subject to available payfors.

Core Tax Cut Proposals (addition material on the core cuts is given on page 5)

- **Marriage Penalty Relief**. There are several options. The first three could be phased in aggressively to minimize their cost through 2003 (the fourth, the Gramm proposal, is already aggressively phased in).

  - **Increase Standard Deduction for Joint Filers**. Increasing the standard deduction for joint filers to double the current level for single filers would cost **roughly $26 billion through 2003.**

    Fifty-four percent of the revenue loss would actually reduce marriage penalties. Couples with income (AGI) under $30,000 would receive 24 percent of the tax cut; couples with AGI over $100,000 would receive only 5 percent of the tax cut. The tax cut in 1999 for a one- or two-earner couple, each with $25,000 in earnings and no other income, and who currently use the standard deduction would be $217.50. This change would also simplify the tax system by reducing the number of taxpayers itemizing deductions by several million.

  - **Two-Earner Deduction**. The second earner deduction that existed between 1982 and 1986 could be reinstated. (This has been introduced by Herger, H.R. 2593.) The deduction was for 10 percent of the first $30,000 of the earnings of the spouse with lower earnings. This would cost **very roughly $60 billion through 2003.**

    Nearly 80 percent of the revenue loss would actually reduce marriage penalties. Couples with income (AGI) under $30,000 would receive 12 percent of the tax cut; couples with AGI over $100,000 would receive 32 percent of the tax cut. The tax cut in 1999 for a two-earner couple, each with $25,000 in earnings and no other income, would be $375.

  - **Reduction in Marriage Penalties in the EITC**. H.R. 3995 (Neal, McDermott, and Kennelly) would reduce marriage penalties in the EITC by raising the endpoint of the "plateau" for married couples filing a joint return by $3,510 (in 1999), which would also raise the income level at which the EITC is fully phased out by the same amount. This would cost **very roughly $10 billion through 2003.**

    Less than 40 percent of the revenue loss would actually reduce marriage penalties. Couples with income (AGI) under $30,000 would receive 92 percent of the tax cut; couples with AGI over $100,000 would receive none of the tax cut. The tax cut in 1999 for a one- or two-earner couple with $24,000 in total earnings, no other income, and one child would be $561.

- **Senator Gramm's Amendment to the Tobacco Bill.** The Gramm amendment would give a new deduction to married couples filing a joint return who have combined incomes below $50,000. The deduction would be equal to the difference between the sum of the standard deductions for a single filer and a head of household filer, and the standard deduction for a joint filer (this difference is $3,450 in 1999). The deduction would be available to all such couples, whether or not they itemized deductions (i.e., the deduction would be "above-the-line"). The deduction would also reduce income for purposes of the phaseout of the Earned Income Tax Credit (EITC), so couples with incomes in the phaseout range of the EITC would get a larger credit. The $50,000 income limit would be indexed for inflation after 2007. The deduction would be phased in over 10 years. This would cost **$14.4 billion through 2003** and approximately **$9 billion per year** when fully phased in.

  The new deduction would be phased in, 25 percent in 1999; 30 percent in 2000, 2001, and 2002; 40 percent in 2003, 2004 and 2005; 50 percent in 2006; 60 percent in 2007; and 100 percent in 2008 and subsequent years.

  Only 35 percent of the revenue loss would actually reduce marriage penalties. Couples with income (AGI) under $30,000 would receive 62 percent of the tax cut; couples with AGI over $100,000 would receive none of the tax cut. The tax cut when fully phased in at 1999 levels for a one- or a two-earner couple with $50,000 in total earnings and no other income, would be $518.

- **School Construction**. The Budget proposal would allow state and local governments to issue up to $9.7 billion of "qualified school construction bonds" in each of 1999 and 2000. It would also increase the limit for "qualified zone academy bonds" by $1 billion in 1999, authorize $1.4 billion of such bonds in 2000, and allow bond proceeds to be used for school construction. These provisions would cost **$5.0 billion through 2003.**

- **Extenders**. The research and experimentation tax credit, the work opportunity tax credit (WOTC), and the deduction for contributions of appreciated stock to private foundations all expired June 30. The welfare-to-work tax credit expires April 30, 1999. Extending these provisions as proposed by the President would cost **$3.2 billion through 2003.**

The Menu of Payfors

The revenue raisers (see the third page of the handout) have been grouped into three categories, plus tobacco. The first grouping is "relatively noncontroversial" items. These items have been included in bipartisan tax legislation this year. The second category are "less noncontroversial" raisers, but given that a tax package needs to be financed, our subjective assessment is that these would be likely additional payfors. The third category (split into two groups) is labeled "controversial." These items have significant opposition.

Possible Additional Tax Cut Proposals

Some of the following proposals could be included in a Democratic package, within the constraint of revenues from payfors remaining after the core proposals.

- **Child Care.** There are at least two options:

  - **Budget Proposal.** The Budget proposal would increase the maximum rate of the child and dependent care tax credit from 30 percent to 50 percent and extend eligibility for the maximum credit from $10,000 to $30,000. The proposal would also provide a new credit to employers of up to $150,000 for 25 percent of expenses incurred to build or acquire a child care facility for employee use or for providing child care services for employees. These proposals would cost **$5.6 billion through 2003.**

  - **Stay-at-home parent provision.** H.R. 4030 (Kennelly) includes the Budget proposal, and a provision that would make taxpayers with children under the age of four eligible for an expanded child credit that would be roughly equal to the average proposed increase in the child and dependent care tax credit for taxpayers under the age of four. A taxpayer could not claim both the expanded child credit and the child and dependent care tax credit. The stay-at-home piece of the Kennelly child care package would cost roughly **$3.5 billion through 2003.**

- **Pensions.** The Budget proposed promoting IRA contributions through payroll deduction, providing a tax credit to small businesses for 50 percent of the costs (up to $2,000 in the first year and $1,000 in the second year) for expenses of administering or providing employee education for a new qualified plan, the establishment of a new small business plan, and enhancing pension portability, disclosure, and simplification. These proposals would cost **$1.0 billion through 2003.**

- **Education.** Extending employer-provided educational assistance (Section 127) by one year (to 6/1/2001) and reinstating the exclusion for graduate education (effective 6/30/98 through 6/1/2001) would cost **$1.0 billion through 2003.**

- **Low Income Housing Tax Credit and Urban Initiatives.** The Budget proposal would increase the per capita limitation from $1.25 to $1.75 at a cost of **$1.6 billion through 2003.** Making the brownfields expensing provision permanent would cost **$0.5 billion through 2003.** Accelerating the startup date for the two new empowerment zones created by TRA97 by one year (to 1/1/99) would cost **0.1 billion through 2003.**

- **Climate Change.** The tax proposals in the Budget are intended to reduce energy consumption and greenhouse gas emissions by encouraging the deployment of technologies that are highly energy efficient and that use renewable energy sources. The nine initiatives in total would cost **$3.6 billion through 2003.**

- **Speedup of 100 Percent Deduction for Self-Employed Health Insurance**. Currently, the percentage of health insurance expenses that may be deducted by a self-employed individual is 45 percent. This percentage is scheduled to increase to 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. Accelerating this schedule by making the deduction 100 percent beginning in 1999 would cost **$5.5 billion through 2003**.

- **Long-Term Care**. The following are three options that might be considered:

  - **Option 1**. Providing a tax credit of $500 for taxpayers who are chronically ill, or who care for a chronically ill spouse or dependent would cost approximately **$5 billion through 2003**. Increasing the credit to $1,000 would cost approximately **$9 billion through 2003**.

  - **Option 2**. Creating a new, nonrefundable tax credit of $1,000 for taxpayers who pay for or provide home-based or community long-term care services for themselves or a chronically ill spouse or dependent would cost approximately **$4.7 billion through 2003**.

  - **Option 3**. Creating a new, nonrefundable tax credit for 75 percent of the first $2,000 of qualified long-term expenses for taxpayers with a chronic illness or chronically ill spouse or dependent would cost approximately **$4.6 billion through 2003**.

- **Capital Gains**. If it were thought desirable to have a capital gains counter to the Republican proposal, an alternative could be fashioned that would provide greater simplicity and equity.

  - One possibility would be to substitute a 40 percent exclusion for the current system of special rates. This would hold harmless or cut taxes for people in the 15 percent and 28 percent brackets (in particular, it would give taxpayers in the 15 percent bracket a rate of 9 percent on gains vs. 10 percent under current law, and taxpayers in the 28 percent bracket a rate of 16.8 percent on gains). Taxpayers in the 39.6 percent bracket would have a rate of 23.76 percent on gains (versus 20 percent under current law). Current rates are scheduled to fall to 8 percent and 18 percent for property held more than five years. The cost of a 40 percent exclusion would be roughly **$8 billion through 2003**.

Detailed Descriptions of Core Proposals

Marriage Penalty Relief

- **Increase Standard Deduction for Joint Filers.** The standard deduction for joint filers ($7,250 in 1999) would be increased to double the standard deduction for single filers ($4,350 in 1999). This would give joint filers a standard deduction of $8,700 in 1999, which is $1,450 more than under current law. For joint filers in the 15 percent bracket who use the standard deduction, this increase would reduce their taxes by $217.50. Joint filers in the 28 percent bracket who use the standard deduction would have taxes reduced by $406.

  This proposal would reduce the number of returns with itemized deductions in 1999 by 3.1 million, from 39.2 million to 36.1 million.

- **Two-Earner Deduction** (H.R. 2593; Herger). This proposal would reinstate the second earner deduction that existed between 1982 and 1986. The deduction is for 10 percent of the first $30,000 of the earnings of the spouse with lower earnings.

  This proposal violates the principal in current law that couples with identical total incomes pay identical total taxes, since only couples with two earners would receive the two-earner deduction.

- **Reduction in Marriage Penalties in the EITC** (H.R. 3995; Neal, McDermott, and Kennelly). The proposal would raise the endpoint of the "plateau" of the Earned Income Tax Credit (EITC) for married couples filing a joint return by $3,510 (from $12,510 to $16,020) in 1999. (The "plateau" is the income range in which the EITC is at a maximum.) Raising the endpoint of the "plateau" would also raise the income at which the EITC is fully phased out by the same amount ($3,510 in 1999).

  The proposal would increase "singles penalties" by **over $3 billion per year** (at 1999 income levels), because heads of households with incomes in the proposed EITC "plateau" and phaseout ranges would owe even more tax than a one-earner couple with the same income, deductions, and personal exemptions than under current law.

- **Senator Gramm's Amendment to the Tobacco Bill.** This amendment, which includes a provision to accelerate the full deduction of health insurance premiums by the self-employed, was adopted by the Senate on June 10. The marriage penalty provision would give an additional deduction to married couples filing a joint return who have combined incomes below $50,000. The deduction would be equal to the difference between the sum of the standard deductions for a single filer and a head of household filer, and the standard deduction for a joint filer (this difference is $3,450 in 1999). It would be available to all such couples, whether or not they itemized deductions (i.e., the deduction would be "above-the-line"). The deduction would also reduce income for purposes of the phaseout of the

Earned Income Tax Credit (EITC), so couples with incomes in the phaseout range of the EITC would get a larger credit. The $50,000 income limit would be indexed for inflation after 2007. The deduction would be phased in, 25 percent in 1999; 30 percent in 2000, 2001, and 2002; 40 percent in 2003, 2004 and 2005; 50 percent in 2006; 60 percent in 2007; and 100 percent in 2008 and subsequent years.

In 1999, the additional deduction would be 25% x $3,450 = $862.50, which would be worth $129 for couples with sufficient taxable income (since couples in this income range are in the 15 percent bracket). When fully phased in, the additional deduction (at the 1999 level of $3,450) would be worth $517.50. With the change in the EITC, the fully-phased-in tax reduction for a one- or two-earner couple with $24,000 in total earnings, no other income, and one child would be $1,069.

The proposal would also increase "singles penalties" by **$17 billion per year** (at 1999 income levels), because unmarried taxpayers with incomes below $50,000 would owe even more tax than a one-earner couple with the same income, deductions, and personal exemptions than under current law.

The provision would create a "cliff," whereby couples with $50,000 of income would get a tax cut of $517.50 (when fully phased in) while a couple with $1 more of income would get nothing. This creates large disincentives to earn income or large incentives to misreport income for taxpayers with incomes above the cliff.

School Construction

The Taxpayer Relief Act of 1997 enacted a provision that allows certain public schools to issue "qualified zone academy bonds," the interest on which is effectively paid by the Federal government in the form of an annual income tax credit. The proceeds of the bonds can be used for a number of purposes, including teacher training, purchases of equipment, curricular development, and rehabilitation and repair of the school facilities. The Budget proposes to institute a new program of Federal tax assistance for public school construction. Under the proposal, State and local governments would be able to issue up to $9.7 billion of "qualified school construction bonds" in each of 1999 and 2000. Holders of these bonds would receive annual federal income tax credits, set according to market interest rates by the Treasury Department, in lieu of interest. At least 95 percent of the bond proceeds of a qualified school construction bond must be used to finance public school construction or rehabilitation. The Budget also proposes to expand the amount of qualified zone academy bonds that can be issued in 1999 from $400 million to $1.4 billion and to authorize an additional $1.4 billion of qualified zone academy bonds in 2000, and to allow the proceeds of these bonds to be used for school construction.

Extension of Expiring Provisions

- **Extend the Work Opportunity Tax Credit.** The Work Opportunity Tax Credit provides an incentive for employers to hire individuals from certain targeted groups. The credit equals a percentage of qualified wages paid during the first year of the individual's employment with the employer. The credit percentage is 25 percent for employment of at least 120 hours but less than 400 hours and 40 percent for employment of 400 or more hours. The credit expires with respect to employees who begin work after June 30, 1998. The Budget proposes to extend the Work Opportunity Tax Credit so that the credit would be effective for individuals who begin work before May 1, 2000.

- **Extend for One Year the Welfare-to-Work Tax Credit.** The Welfare-to-Work Tax Credit enables employers to claim a tax credit on the first $20,000 of eligible wages paid to certain long-term family assistance recipients. The credit is 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 eligible wages in the second year of employment. The credit is effective for individuals who begin work before May 1, 1999. The Budget proposes to extend the Welfare-to-Work Tax Credit for one year, so that the credit would be effective for individuals who begin work before May 1, 2000.

- **Extend for One Year the R&E Tax Credit.** The Budget proposes to extend the tax credit provided for certain research and experimentation expenditures, which is scheduled to expire after June 30, 1998, for one year through June 30, 1999.

- **Contributions of Appreciated Stock to Foundations.** The special rule that allows a taxpayer to deduct the full fair market value of qualified stock donated to a private foundation expires with respect to contributions made after June 30, 1998. The Budget proposes to extend the provision to apply to contributions made during the period July 1, 1998 through June 30, 1999.

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