E. REDUCE TAX EXPENDITURES

46. Modify the home mortgage interest expense deduction

CURRENT LAW

Current law allows homeowners to deduct mortgage interest expenses from the Federal income tax. The Tax Reform Act of 1986 phased out deductions for other interest expenses incurred for personal purposes and not incurred for the production of income (such as interest on auto or education loans). There is currently a $1 million limit on the amount of principal eligible for the mortgage interest deduction. Current law also allows the deduction of interest on a second home, if the principal amount of the mortgage (combined with the mortgage on the primary residence) does not exceed $1 million. Current law also permits deduction of interest on home equity loans up to $100,000 regardless of the purpose of the loan.

OPTIONS

(a) Reduce the maximum mortgage principal eligible for interest deductions to $300,000. This option would lower the limit on the amount of principal eligible for the home mortgage interest expense deduction from $1 million to $300,000. The median price of a new home sold in the U.S. was $126,500 in 1993. The prices of 9 percent of all new homes sold were in excess of $250,000 in 1993. However, the median price for certain areas of the country is considerably higher (*e.g.*, San Francisco was about $255,000 in 1992).

(b) Eliminate the deduction. This option would eliminate the deduction for home mortgage interest expenses and interest expenses on home equity loans.

These options would take effect starting in 2000 and would be phased in over five years. They would apply to new and existing mortgages. Other possible approaches would place the cap at some intermediate dollar value, such as $500,000, or apply the rules only to new mortgages.

EFFECT

Percentage of Gross Domestic Product

	2000	2010	2020	2030
a. Revenue increase	*	0.06%	0.07%	0.07%
b. Revenue increase	0.15%	0.74%	0.74%	0.74%

45. Reform the budget process

CURRENT LAW

The Congressional Budget Act requires that Congress pass a concurrent budget resolution. The resolution sets targets for total receipts and outlays by budget function and allocates amounts of budget authority and outlays to the committees that have jurisdiction over spending programs. Points of order can be raised to block consideration of bills that exceed a committee's allocation and require votes if the objections are to be waived. Budget resolutions do not require approval by the President and do not have the force of law.

Authorizing bills establish substantive policies. Under the rules of the House and Senate, programs and agencies are supposed to be authorized before appropriations. Authorizing legislation may be annual, multiyear, or permanent in duration. It can provide a specific dollar or an indefinite amount of funding. Amounts must be appropriated, however, before spending can occur.

Thirteen annual **appropriations bills** reported by the Senate and House Appropriations Committees provide the funding for so-called discretionary spending programs. The Congressional Budget Act requires that Congress complete action on all regular appropriations bills before the start of the new fiscal year. If this requirement is not met, interim funding is provided in continuing resolutions.

Reconciliation bills conform tax and spending legislation to the levels set in a budget resolution. Reconciliation bills are not annual requirements. If reconciliation instructions are included in a budget resolution and apply to more than one authorizing committee, the Budget Committees from each chamber report an omnibus budget reconciliation bill.

OPTION

This option would make several changes to the budget process. The major changes would be: (1) the budget process would be on a biennial calendar; (2) concurrent budget resolutions would be replaced by joint resolutions (joint resolutions require approval by the President and have the force of law); (3) appropriations and authorization legislation would not be considered on the floor or in committee before passage and Presidential approval of a joint budget resolution; (4) a vote of two-thirds of both Chambers of Congress would be required if spending is to exceed the level budgeted in the joint resolution in any budget function category; (5) entitlement program spending — except Social Security — would require fixed-dollar appropriations; (6) if Congress failed to enact a joint budget resolution or any appropriations bills by the end of the fiscal year, an automatic continuing resolution would take effect providing spending at the nominal level of the prior year. These provisions were included in H.R. 2929, introduced by Congressmen Cox and Stenholm.

EFFECT

The outlay effects depend on the funds appropriated by Congress for entitlement program spending — except Social Security.

The House of Representatives passed H.R. Res. 235 on August 5, 1993, in connection with the entitlement review provisions. H.R. Res. 235 provided an expedited "House Rules" process for the House of Representatives to respond to the President's proposed offsets for excess entitlement spending. Under House Rules, if the House does not enact legislation to eliminate an overage reported by the President, it must act to increase this spending limit. Failure to increase the limit precludes action on appropriations bills.

Executive Order No. 12858, also signed on August 4, 1993, created a deficit reduction fund to guarantee that the net deficit reduction achieved by OBRA 93 is dedicated exclusively to reducing the deficit.

OPTION

The objective of this option is to lock in any savings derived from the PAYGO procedures.

The specific modifications to the current budget process would be: (1) Social Security would be included in the PAYGO procedures; (2) annual PAYGO credits provided in any legislation enacted into law would be unavailable for use in legislation in subsequent sessions (the credits would be dedicated to the deficit reduction fund established by Executive Order No. 12858); and (3) PAYGO and the deficit reduction fund would be extended through the year 2030.

EFFECT

Outlay effects are not provided because the option is not intended to create savings beyond those scored as part of entitlement reform.

48. Modify the deduction for charitable contributions

CURRENT LAW

Under current law, taxpayers who itemize deductions can deduct the value of contributions they make to qualifying charitable organizations. The amount of deductions may not exceed 50 percent of the taxpayer's adjusted gross income (AGI) in any year. In addition to cash donations, taxpayers can deduct the fair market value of a contribution of property that has appreciated since its purchase, including property they have held for more than 12 months, regardless of how much they paid for the property.

OPTIONS

(a) Allow a deduction for charitable contributions only if they exceed 2 percent of AGI. This option would allow taxpayers to deduct only those contributions in excess of 2 percent of adjusted gross income. These options would take effect starting in 2000 and would be phased in over five years. If it was effective in 1995 (rather than 2000), the charitable deductions of about 20 million taxpayers and reduce allowed deductions for an additional 14 million taxpayers.

(b) Deny the deduction. This option would eliminate the deduction for charitable contributions altogether.

These options would take effect starting in 2000 and would be phased in over five years.

EFFECT

Percentage of Gross Domestic Product

	2000	2010	2020	2030
a. Revenue increase	0.02%	0.11%	0.11%	0.11%
b. Revenue increase	0.05%	0.24%	0.24%	0.24%

49. Limitations on itemized deductions

CURRENT LAW

Under current law, taxpayers may reduce adjusted gross income (AGI) by the amount of their itemized deductions, including home mortgage interest expense, charitable contributions, State and local income and property taxes, medical expenses (in excess of a 7.5 percent of AGI), certain moving expenses, and miscellaneous business expenses (in excess of 2 percent of AGI). Current law also requires that the amount of itemized deductions be reduced by $3 for each $100 of adjusted gross income in excess of $108,450 for couples and $54,225 for individual filers (for 1993). This reduction, also known as the "Pease" reduction, is limited to 80 percent of itemized deductions otherwise allowable. It effectively denies a portion of itemized deductions to high-income persons.

OPTIONS

(a) Limit itemized deductions to 15 percent. This option would limit itemized deductions to a rate of 15 percent regardless of the marginal tax rate applicable to the taxpayer.

(b) Limit itemized deductions to 28 percent. This option would limit itemized deductions to a rate of 28 percent regardless of the marginal tax rate applicable to the taxpayer.

(c) Deny 25 percent of itemized deductions. This option would allow 75 percent of itemized deductions to be deducted from income, as opposed to 100 percent under current law.

(d) Increase the high-income reduction. This option would reduce itemized deductions by $10 for each $100 of adjusted gross income above the thresholds (instead of $3). As in Option (a), it affects the value of itemized deductions for upper-income persons. However, this option has a comparable impact to the other options described here only at very high income levels because of the high AGI thresholds and the gradual nature of the reduction (in 1992, 3.2 million individual income tax returns were subject to the limitation, out of a total of almost 114 million individual returns filed).

These options would take effect starting in 2000 and would be phased in over five years.

EFFECT

Percentage of Gross Domestic Product

	2000	2010	2020	2030
a. Revenue increase	0.16%	0.88%	0.98%	1.07%
b. Revenue increase	Projected revenue increase for this option not available.			
c. Revenue increase	0.10%	0.52%	0.53%	0.54%
d. Revenue increase	0.03%	0.13%	0.13%	0.13%

50. Recognize gain on appreciated property at death

CURRENT LAW

Under current law, the basis of appreciated property held at death is increased to its fair market value. As a result, the decedent's estate or heirs may sell the property and not be taxed on the appreciation that occurred before the date of death. Therefore, the gain on the decedent's appreciated property is permanently excluded from Federal income taxation. The value of the property is, however, included in the estate of the decedent and may be subject to estate taxation if the value exceeds $600,000.

OPTION

This option would include the appreciation on property held at the time of death in the decedent's final tax return as if the property had been sold for its fair market value immediately prior to death. An alternative to this option would defer the taxation of appreciation until the property is sold by the estate or the heirs.

This option would take effect starting in 2000 and would be phased in over five years.

EFFECT

Percentage of Gross Domestic Product

	2000	2010	2020	2030
Revenue increase	0.02%	0.11%	0.11%	0.11%

51. Modify accelerated depreciation

CURRENT LAW

Under current law, businesses may amortize the cost of depreciable property using recovery periods that are less than the useful life of the property. In addition, the method of depreciation (200 percent declining balance method for 3-, 5-, 7-, and 10-year property, and 150 percent declining balance method for certain other property) accelerates depreciation deductions to the years immediately after the property is placed in service.

OPTIONS

(a) Require straightline depreciation instead of accelerated depreciation. This option would replace accelerated depreciation with straightline depreciation over the useful life of the property.

(b) Eliminate 200 percent declining balance method. This option would replace the 200 percent declining balance method used for 3-, 5-, 7-, and 10-year property with the 150 percent declining balance method.

These options would take effect starting in 2000 and would be phased in over five years.

EFFECT

Revenue estimates are not available for this option.

52. Include employer contributions and interest earnings on qualified defined benefit and contribution plans and Keoghs in employee income

CURRENT LAW

Current law places limits on the benefits that an employer can fund in qualified plans for any employee. The limits depend on the type of plan the employer offers. Qualified defined contribution plans (including 401(k), 403(b), and other plans) specify how much the employer may contribute for each employee's retirement. Keogh plans specify how much a self-employed person may contribute for their retirement. Defined benefit plans specify the pension amount employees will receive in retirement, (usually a percentage of pre-retirement earnings).

Employer contributions to all three types of plans are tax deductible for the employer, and are not taxed to the employee until funds are withdrawn. Income earned on plan assets is also not subject to income taxation until the funds are withdrawn. This defers the taxation of contributions relative to cash wages and defers the taxation of income on plan assets relative to assets held directly.

OPTION

This option would include employer contributions and interest earnings on defined benefit pensions, qualified pensions, Keoghs, and earnings on plan assets in the employee's income. This change would eliminate the deferral of compensation and earnings on assets for pension plans. Alternatively, the limits on contributions or employee retirement benefits could be reduced.

This option would take effect starting in 2000 and would be phased in over five years.

EFFECT

Revenue estimates are not available for this option.

53. Include the value of employer-paid health insurance and health care expenses in income for income tax purposes

See Option 15 in the Health Programs section.