CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

July 20, 1999

H.R. 2488
Financial Freedom Act of 1999

As ordered reported by the House Committee on Ways and Means on July 14, 1999

SUMMARY

H.R. 2488 would provide for a variety of phased-in tax reductions, including a 10 percent across-the-board cut in income tax rates and a repeal of the alternative minimum tax, an increase in the standard deduction for married couples, an exclusion for some interest and dividend income, a new deduction for some health insurance expenses, a reduction in the capital gains rate, and a repeal of estate taxes. The Congressional Budget Office and the Joint Committee on Taxation (JCT) estimate that H.R. 2488 would decrease governmental receipts by $4.5 billion in fiscal year 2000, by about $200 billion over the 2000-2004 period, and by about $860 billion over the 2000-2009 period. In addition, the legislation would increase direct spending by $25 million over the 2000-2004 period and by $73 million over the 2000-2009 period. Because the bill would affect receipts and direct spending, pay-as-you-go procedures would apply.

H.R. 2488 contains two new intergovernmental mandates, the costs of which would not exceed the threshold for intergovernmental mandates ($50 million in fiscal year 1996, adjusted annually for inflation) established in the Unfunded Mandates Reform Act (UMRA). The bill also contains 11 new private-sector mandates. The costs of those mandates would exceed the threshold established by UMRA for private-sector mandates ($100 million in fiscal year 1996, adjusted annually for inflation) in fiscal years 2000 through 2004.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of the bill is shown in the following table.

	By Fiscal Year, in Millions of Dollars					
	1999	2000	2001	2002	2003	2004
CHANGES IN REVENUES						
Estimated Revenues						
On-Budget	0	-4,543	-25,515	-46,728	-57,713	-65,259
Off-Budget	0	0	-31	-46	-49	-52
Total Change in Revenues	0	-4,543	-25,546	-46,774	-57,762	-65,311
CHANGES IN DIRECT SPENDING						
Estimated Budget Authority	0	2	0	2	2	6
Estimated Outlays	0	2	2	6	5	9

a. Implementing the bill would also increase spending subject to appropriation, but CBO estimates that such costs would not be significant.

Sources: Congressional Budget Office and Joint Committee on Taxation.

BASIS OF ESTIMATE

All estimates, with the exception of the following provisions, were prepared by JCT.

Revenues

Accelerate the Repeal of the FUTA Surtax. The Federal Unemployment Tax Act (FUTA) imposes on employers an effective tax of 0.8 percent on the first $7,000 in wages paid annually to each employee. This 0.8 percent includes a 0.2 percent surtax scheduled to expire on December 31, 2007. The bill would accelerate the expiration date to December 31, 2004.

Revenues from the FUTA tax are deposited into federal unemployment trust funds, which are statutorily capped. Under current law, CBO projects that the amounts in the federal trust funds will exceed the caps beginning in 2003. Amounts above the caps are transferred to state unemployment compensation trust funds. Since the state funds are included in the unified federal budget, this transfer will have no net budgetary effect. However, CBO expects that states would respond to this transfer by lowering their unemployment taxes so that their trust fund balances would remain constant.

The bill would lower the amount of revenues deposited into the federal trust funds and thus would reduce the amounts flowing to the state funds. CBO assumes that in the year following each lowered transfer, states would respond by not lowering their uemployment taxes as much as they would have, thus increasing revenues relative to current law. CBO estimates that the measure would reduce governmental receipts by $1,029 million in fiscal year 2005 and by lesser amounts in 2006 and 2007. CBO estimates increases of receipts in fiscal years 2008 and 2009. Over the 2005-2009 period, CBO estimates that the measure would have no net impact on governmental receipts.

IRS User Fees. The bill would adjust and extend the authority of the Internal Revenue Service (IRS) to charge taxpayers fees for certain rulings by the Office of the Chief Counsel and by the Office for Employee Plans and Exempt Organizations. The bill would eliminate the fee the IRS currently charges on determination letter requests regarding small business pension plans beginning on December 31, 2000. The bill also would extend for six years beyond its current expiration date of September 30, 2003, the authority of the IRS to charge taxpayers fees for certain rulings. CBO estimates that the adjustment and extension of IRS fees would increase governmental receipts by $5 million over fiscal years 2001 through 2004 and by $244 million during the 2001-2009 period, net of income and payroll tax offsets. CBO based its estimate on recent collections data and on information from the IRS.

Federal Spending

IRS User Fees. H.R 2488 would adjust and extend the authority of the IRS to charge taxpayers fees for certain rulings by the Office of the Chief Counsel and by the Office for Employee Plans and Exempt Organizations. The IRS has the authority to retain and spend a small portion of these fees without further appropriation. CBO estimates that the adjustment and extension of fees would decrease direct spending by $1 million over the 2001-2004 period but would increase direct spending by $9 million over the 2001-2009 period.

Sport Fish Restoration. Repealing the excise tax on fishing tackle boxes would reduce budget authority of the Sport Fish Restoration account. CBO estimates that this provision would reduce mandatory federal outlays by $1 million in fiscal year 2001, by $2 million in fiscal year 2002, and by $3 million annually beginning in fiscal year 2003.

National Vaccine Injury Compensation Fund and Medicaid. The bill would add conjugate vaccines against streptococcus pneumoniae to the list of taxable vaccines and thus would allow for compensation for injuries related to those vaccines from the National Vaccine Injury Compensation Trust Fund. CBO estimates that this provision would increase outlays by $4 million over the 2000-2004 period. This provision would also increase federal Medicaid outlays by $21 million over the 2000-2004 period because Medicaid would be required to pay the excise tax on purchases of vaccines against streptococcus pneumoniae. The federal government purchases about one-half of all vaccines through its Vaccines for Children program.

Also, by adding conjugate vaccines against streptococcus pneumoniae to the list of taxable vaccines, the bill would increase the cost of vaccines purchased under section 317 of the Public Health Service Act. Section 317 authorizes grants to states for the purchase of vaccines under federal contracts with vaccine manufacturers. Any increase in spending under this section would be subject to the annual appropriation process; CBO estimates that the additional costs would not be significant.

Reduced PBGC Premiums for New Plans. Under current law, single-employer defined benefit pension plans pay two types of annual premiums to the Pension Benefit Guaranty Corporation (PBGC). All covered plans are subject to a flat-rate premium of $19 per participant. In addition, underfunded plans must also pay a variable premium that depends on the amount by which the plan's liabilities exceed its assets.

H.R. 2488 would reduce the flat-rate premium from $19 to $5 per participant for plans established by employers with 100 or fewer participants during the first five years of the plan’s operation. According to information obtained from the PBGC, approximately 3,000 plans would qualify for this reduction. Those plans contain an average of about 10 participants each. CBO estimates that the premium change would reduce PBGC's premium income, which is classified as an offsetting collection, by about $0.4 million annually beginning in 2002 or by about $1.3 million over the 2000-2004 period.

Reduction of Additional PBGC Premium for New and Small Plans. H.R. 2488 would make two changes affecting the variable-rate premium paid by underfunded plans. First, for all new plans that are underfunded, the bill would phase in the variable-rate premium the plans must pay. In the first year, they would pay nothing. In the succeeding four years, they would pay 20 percent, 40 percent, 60 percent, and 80 percent, respectively, of the full amount. In the sixth and later years, they would pay the full variable-rate premium determined by their funding status. On the basis of information on premium payments to the PBGC in 1996-1997, CBO estimates that this change would affect the premiums of approximately 400 plans each year. It would reduce PBGC's total premium receipts by about $4.2 million over the 2000-2004 period.

The bill would also reduce the variable-rate premium paid by all underfunded plans (not just new plans) established by employers with 25 or fewer employees. Under the bill, the variable-rate premium per participant paid by those plans would not exceed $5 multiplied by the number of participants in the plan. CBO estimates that approximately 8,300 plans would have their premium payments to PBGC reduced by this provision in 2000. Premium receipts by the PBGC would decline by $1.5 million in 2002 and by about $4.6 million over the 2000-2004 period.

Missing Plan Participants. The legislation would expand the missing participant program. The Retirement Protection Act of 1994 established a missing participant program at PBGC for terminating defined benefit plans. The bill would expand the program to include terminating multiemployer plans, defined benefit plans not covered by PBGC, and defined contribution plans.

The budgetary impact of this provision would be less than $0.5 million annually. PBGC does not expect a high volume of missing participants as a result of this proposal, and the administrative costs of expanding the program would not be high. The net budgetary effect of increased benefit payments would also be small. Amounts paid by a pension plan to PBGC for missing participants are held in PBGC's trust fund, which is off-budget. Amounts paid out by PBGC to participants at the time they are located are funded in the same manner as benefit payments to participants in plans for which PBGC is the trustee—partially by the trust fund and partially by on-budget revolving funds.

Rules for Substantial Owner Benefits in Terminated Plans. The legislation would simplify the guarantee and asset allocation rules as they relate to terminated plans involving a substantial owner (ownership interest of at least 10 percent). All owners other than majority owners (those with an ownership interest of 50 percent or more) would be treated the same as other participants, thus receiving a more generous guarantee than under current law. Majority owners would be subject to simplified special rules. The guarantee for majority owners would be phased in at the rate of 1/10 for each year that the plan has been in effect, which is faster than the current-law phase-in, but the nonguaranteed benefits of majority owners would be given a lower priority in the allocation of assets. Only about one-third of the plans taken over by PBGC involve substantial owners, and the change in benefits paid out by PBGC to owner-employees under this provision would be less than $0.5 million in each year.

PAY-AS-YOU-GO CONSIDERATIONS

The Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. The net changes in governmental receipts and outlays that are subject to pay-as-you-go procedures are shown in the following table. Only changes affecting on-budget outlays and receipts affect the pay-as-you-go scorecard. For the purposes of enforcing pay-as-you-go procedures, only the effects in the current year, the budget year, and the succeeding four years are counted.

	By Fiscal Year, in Millions of Dollars										
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Changes in Receipts	0	–4,543	-25,515	-46,728	-57,713	-65,259	-89,787	-104,672	-114,128	-151,827	-203,233
Changes in Outlays	0	2	2	6	5	9	10	10	10	10	10

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

JCT has determined that the provisions that would add streptococcus pneumoniae to the list of taxable vaccines and would impose a 1.5 percent surtax on state and local entities that deal in distilled spirits are intergovernmental mandates. JCT estimates that the cost of these mandates would not exceed the threshold specified in UMRA ($50 million in fiscal year 1996, adjusted for inflation). Other sections of the bill reviewed by CBO (sections 803, 1205, 1206, 1208) contain no intergovernmental mandates as defined in UMRA. Section 803 would move the expiration date of the federal unemployment surtax back three years and would have implications for state unemployment compensation programs as noted above.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

JCT has determined that 11 provisions in H.R. 2488 contain private-sector mandates. The bill would:

- Add certain vaccines against streptococcus pneumoniae to the list of taxable vaccines;

- Impose a 10 percent vote of value test;

- Change the treatment of income and services provided by taxable subsidiaries of real estate investment trusts (REITs);

- Impose a 1.5 percent surtax on wholesale dealers of distilled spirits;

- Require reporting of information regarding cancellation of indebtedness by nonbank financial institutions;

- Impose a limitation on prefunding of certain employee benefits;

- Modify the treatment of certain closely held REITs;

- Prevent the conversion of ordinary income or short-term capital gains into income eligible for long-term capital gains rates;

- Repeal the installment method for most taxpayers using the accrual basis;

- Limit the use of the nonaccrual experience method of accounting; and

- Exclude like-kind exchange property from nonrecognition treatment on the sale of a personal residence.

JCT estimates that the cost of the private-sector mandates would exceed the threshold established in UMRA ($100 million in fiscal year 1996, adjusted annually for inflation) in each fiscal year of the 2000-2004 period.

Estimated Cost of Private-Sector Mandates

	By Fiscal Year, in Millions of Dollars					
	1999	2000	2001	2002	2003	2004
Cost to the Private Sector	22	671	1,011	828	575	337

Source: Joint Committee on Taxation.

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