CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

December 12, 2005

S. 2020
Tax Relief Act of 2005

As passed by the Senate on November 18, 2005

SUMMARY

S. 2020 would make a number of changes to tax law. It would extend multiple expiring provisions; provide tax benefits for individuals and businesses in areas affected by Hurricanes Katrina, Rita, and Wilma; create incentives for donations to charity and reform tax laws applicable to charitable organizations; and make other various changes.

The Joint Committee on Taxation (JCT) estimates that enacting S. 2020 would reduce federal revenues by $11.0 billion in 2006, by $57.8 billion over the 2006-2010 period, and by $37.5 billion over the 2006-2015 period. Sections 406 and 573 could affect direct spending, but CBO cannot estimate the likely impact of those provisions, which would reserve a portion of Internal Revenue Service (IRS) debt-collection contracts for firms that hire the disabled.

JCT has not reviewed the tax provisions of S. 2020 to determine whether they contain any intergovernmental or private-sector mandates as defined by Unfunded Mandate Reform Act (UMRA). CBO has determined that the non-tax provisions of S. 2020 contain no intergovernmental or private-sector mandates as defined in UMRA and would not affect the budgets of state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 2020 is shown in the following table.

	By Fiscal Year, in Millions of Dollars									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
CHANGES IN REVENUES										
Extend Expiring Provisions	-18,081	-29,121	-7,949	-9,247	-3,659	2,181	1,391	815	375	138
Hurricane Relief Provisions	-3,833	-2,796	-715	34	62	-40	-102	-150	-170	-177
Charitable Donation Provisions	-251	-450	-88	69	74	80	94	109	125	138
Economic Substance Doctrine	537	806	1,128	1,273	1,431	1,635	1,881	2,158	2,449	2,647
Other Provisions	10,670	-1,110	2,034	1,129	222	523	821	1,041	1,131	1,218
Estimated Revenues	-10,958	-32,672	-5,590	-6,740	-1,870	4,380	4,086	3,974	3,910	3,964

SOURCE: Joint Committee on Taxation.

BASIS OF ESTIMATE

Revenues

S. 2020 would make a number of changes to tax law. It would extend multiple expiring provisions; provide tax benefits for individuals and businesses in areas affected by Hurricanes Katrina, Rita, and Wilma, all of which struck the United States in the late summer and fall of 2005; create incentives for donations to charity and reform tax laws applicable to charitable organizations; and make a number of other changes to tax law, some of which would increase revenue. JCT provided all estimates of revenue effects.

Expiring Provisions. The bulk of the revenue reductions from S. 2020 come from extensions of 17 expiring provisions, either for one year or for multiple years. Taken together, these provisions would reduce revenues by $18.1 billion in 2006, by $68.1 billion over the 2006-2010 period, and by $63.2 billion over the 2006-2015 period.

Among these provisions, S. 2020 would extend for one year and expand the increased exemption amounts for the alternative minimum tax (AMT) that are set to expire at the end of 2005. As a result, the exemption amounts would be higher in 2006 than allowed under current law by $8,750 for single taxpayers and $17,550 for married taxpayers who file joint tax returns. S. 2020 would also extend for one year the provision that allows taxpayers to use certain nonrefundable personal credits to reduce their AMT liability, which also expires at the end of 2005. JCT estimates that the two provisions would reduce revenues by $12.8 billion in 2006 and $20.6 billion in 2007.

S. 2020 would modify and extend through December 31, 2006, a research credit of 20 percent of the amount by which a taxpayer's qualified research expenses exceed the base amount for that taxable year. This provision is estimated to reduce revenues by $3.3 billion in 2006, by $9.9 billion over the 2006-2010 period, and by $10.1 billion over the 2006-2015 period.

The act would extend for four years the deduction for qualified tuition and other higher education expenses ($2,000 to $4,000, depending on gross income) through December 31, 2009. This provision would decrease revenues by an estimated $420 million in 2006 and $7.4 billion over the 2006-2010 period.

It would also extend the saver's credit, a nonrefundable tax credit available to certain taxpayers for contributions to qualified retirement savings plans. S. 2020 would extend the credit for three years through 2009. JCT estimates that enacting this provision would reduce revenues by $4.1 billion over the 2007-2010 and 2007-2015 periods.

The act would also extend for two years through 2009 the increased amounts and types of investment that qualify for immediate deductibility ("expensing") under section 179 of the Internal Revenue Code. This provision would reduce revenues by $7.3 billion dollars over the 2008-2010 period and by $271 million over the 2008-2015 period.

Extending the deduction of state and local sales taxes through 2006 is estimated to reduce revenues by $649 million in 2006 and $1.9 billion in 2007.

Hurricane Relief Provisions. Hurricane relief provisions also account for a large portion of revenue reductions in S. 2020. All in all, they would reduce revenues by $3.8 billion in 2006, by $7.2 billion over the 2006-2010 period, and by $7.9 billion over the 2006-2015 period.

The act would provide for an additional first-year depreciation deduction of 50 percent of the adjusted basis of qualified Gulf Opportunity Zone property. Qualifying property must have been purchased after August 27, 2005 and before December 31, 2007 (for equipment) or December 31, 2008 (for structures). This provision would reduce revenues by $1.3 billion in 2006, by $2.9 billion over the 2006-2010 period, and by $2.1 billion over the 2006-2015 period.

In addition, taxpayers may currently claim deductions for personal casualty losses if they exceed $100 each; also, deductions are allowed only if the aggregate casualty losses exceed 10 percent of the taxpayer's gross income. This act would suspend these thresholds for losses due to Hurricane Katrina (on or after August 25, 2005), Hurricane Rita (on or after September 23, 2005), and Hurricane Wilma (on or after October 23, 2005). According to JCT, this provision would reduce revenues by $528 million in 2006, by $611 million in 2007, and by $35 million in 2008.

Among other changes, the bill would allow the states of Alabama, Louisiana, and Mississippi to issue private activity bonds that would not be subject to the volume cap that applies to the issuance of most such bonds. Each state would be allowed to issue, in the aggregate, $2,500 per capita worth of Gulf Opportunity Zone Bonds. JCT estimates that this provision would decrease revenues by $13 million in 2006, by $440 million over the 2006-2010 period, and by $1.4 billion over the 2006-2015 period.

Charitable Donation Provisions. S. 2020 would provide incentives for charitable giving, as well as reform tax laws applicable to charitable organizations. These provisions include allowing tax-free distributions from IRAs for charitable purposes under certain circumstances, modifying the deduction for donating food, and limiting charitable contributions of clothing. In sum, these provisions would reduce revenues by $251 million in 2006, by $643 million over the 2006-2010 period, and by $95 million over the 2006-2015 period.

Economic Substance Doctrine. S. 2020 would clarify the economic substance doctrine that disallows tax reductions resulting from certain transactions that do not have economic substance or that lack a business purpose other than reducing taxes. The act would also apply certain penalties and deny deductions for interest payments on related underpayments. JCT estimates that those provisions would reduce tax shelters and economic activity undertaken solely for the purpose of reducing taxes, resulting in increased receipts of $537 million in 2006, $5.2 billion from 2006-2010, and $15.9 billion from 2006-2015.

Other provisions. S. 2020 would make a number of other changes to tax law, most of which would result in increases in revenues. All in all, these other provisions would increase revenues by $10.7 billion in 2006, by $13.0 billion over the 2006-2010 period, and by $17.7 billion over the 2006-2015 period.

One of the changes would require large integrated oil companies to revalue their inventories in 2005 using the first-in first-out method, rather than the more favorable last-in, first-out method they have been permitted to use. JCT estimates that the accounting change would increase receipts by $3.5 billion in 2006 and $844 million in 2007.

S. 2020 would also reduce the amount of tax liability for tax year 2006 that certain taxpayers with incomes greater than $150,000 can pay when they file their tax returns without triggering penalties. It would not change the overall amount of tax liability, but would result in an earlier payment of taxes by withholding and estimated payments, shifting about $5.0 billion in receipts from 2007 into 2006.

Other provisions would alter the effective dates for restrictions on inversion transactions and sale-in lease-out transactions that were enacted in earlier legislation; increase the age of minor children whose unearned income is taxed at the parent's tax rate; and require partial payment of tax to the Internal Revenue Service with submissions of offers-in-compromise.

Direct Spending

Sections 406 and 573 (identical provisions) would reserve a portion of IRS debt-collection contracts for firms that hire the disabled. Those contracts, authorized under section 881 of the American Jobs Creation Act of 2004 (Public Law 108-357), will supplement the IRS's resources by retaining private firms to locate and contact certain delinquent taxpayers. The IRS will soon award contracts for the initial pilot phase, with full implementation expected in mid-2006. S. 2020 would set aside 10 percent of future contracts for firms that hire people receiving benefits from any of three federal programs—Social Security Disability Insurance (DI), Supplemental Security Income (SSI), or veterans' disability compensation.

CBO cannot estimate the magnitude or direction of the budgetary effect of the provisions for two reasons. It is unclear whether the provisions would lead to reductions in federal outlays for disability programs. No savings would occur in veterans' disability compensation because those recipients may collect benefits regardless of their employment or earnings. Savings might occur in DI because DI benefits are suspended when recipients have worked for 12 months and have earned a certain minimum amount, but many recipients stop such work to avoid losing benefits. Only in the SSI program do earnings lead to an immediate reduction in benefits, generally at the rate of 50 cents for each dollar of earnings. Furthermore, such savings in benefits would only occur if the disabled recipients would not have filled comparable jobs elsewhere.

There is also a possibility that the provisions would affect the amount of taxes collected by private firms. They would introduce a new criterion into the IRS's selection process, which now focuses solely on selecting firms that will recover the largest amounts of debt while scrupulously following the IRS rules. Contractors chosen under the proposal might be more or less successful at debt recovery than those who will prevail under the agency's current plans. Even a small reduction in collections, though, could more than offset any apparent savings in disability benefits. JCT does not estimate that any significant revenue effect would result from these provisions of S. 2020.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

JCT has not reviewed the tax provisions of S. 2020 to determine whether they contain any intergovernmental or private-sector mandates as defined by UMRA. CBO has determined that the non-tax provisions of the legislation contain no intergovernmental or private-sector mandates as defined in UMRA and would not affect the budgets of state, local, or tribal governments.

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