CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

September 30, 2004

H.R. 1308

Working Families Tax Relief Act of 2004

As cleared by the Congress on September 23, 2004

SUMMARY

H.R. 1308 makes several changes to existing tax law. Specifically, it extends several provisions that were enacted as part of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and then modified by the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA). In addition, H.R. 1308 establishes a uniform definition of a qualifying child for determining taxpayers' filing status and eligibility for certain tax credits and exemptions. The act also extends numerous provisions of the Internal Revenue Code that are scheduled to expire or that have already expired, including the research and experimentation tax credit, parity in the application of certain mental health benefits, and the increased share of rum excise tax revenues that is paid to Puerto Rico and the Virgin Islands.

The Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT) estimate that enacting H.R. 1308 would decrease federal revenues by about $27 billion in 2005, $112 billion over the 2005-2009 period, and $122 billion over the 2005-2014 period. In addition, CBO and JCT estimate direct spending would increase by about $2 billion in 2005, $21 billion over the 2005-2009 period, and $24 billion over the 2005-2014 period as a result of the legislation.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 1308 is shown in the following table. The spending impact of the legislation falls within budget function 800 (general government).

	By Fiscal Year, in Millions of Dollars									
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
CHANGES IN REVENUES										
Extensions of Family Tax Provisions										
$1,000 Child Tax Credit[a]	-2,638	-13,193	-13,198	-13,227	-12,376	-6,942	0	0	0	0
Marriage Penalty Relief[a]	-5,415	-5,412	-3,050	-1,493	-323	0	0	0	0	0
10% Bracket[a]	-4,262	-6,423	-6,796	-4,330	-3,229	-3,315	-1,006	0	0	0
Subtotal[a]	-12,315	-25,028	-23,044	-19,050	-15,928	-10,257	-1,006	0	0	0
Less: Outlays from Refundable Tax Credits	0	4,784	4,468	4,472	4,464	2,842	133	0	0	0
Effect on Revenues	-12,315	-20,244	-18,576	-14,578	-11,464	-7,415	-873	0	0	0
Accelerated Refundability of Child Credit	-64	0	0	0	0	0	0	0	0	0
Extension of Individual AMT Relief	-9,031	-13,546	0	0	0	0	0	0	0	0
Modified Treatment of Combat Pay for Certain Tax Purposes	-3	-3	0	0	0	0	0	0	0	0
Uniform Definition of a Child	-84	-168	-170	-178	-182	-185	-138	-50	-49	-50
Extension of Certain Other Expiring Provisions[b]	-5,558	-3,358	-1,290	-868	-540	-255	-199	-216	-263	-248
Total Change in Revenues	-27,055	-37,319	-20,036	-15,624	-12,186	-7,855	-1,210	-266	-312	-298
On-budget	-27,054	-37,306	-20,033	-15,624	-12,186	-7,855	-1,210	-266	-312	-298
Off-budget[b]	-1	-13	-3	0	0	0	0	0	0	0
CHANGES IN DIRECT SPENDING										
Outlays from Refundable Tax Credits										
Extensions of Family Tax Provisions	0	4,784	4,468	4,472	4,464	2,842	133	0	0	0
Accelerated Refundability of Child Credit	1,929	0	0	0	0	0	0	0	0	0
Modified Treatment of Combat Pay for Certain Tax Purposes	46	47	24	21	18	19	17	0	0	0
Uniform Definition of a Child	0	38	39	40	43	44	45	25	26	26
Outlays from Increased Limit on Cover Over (Payment) of Rum Excise Taxes	151	18	0	0	0	0	0	0	0	0
Total Change in Outlays[c]	2,126	4,887	4,531	4,533	4,525	2,905	195	25	26	26
Total Effect on the Budget Deficit[d]	-29,181	-42,206	-24,567	-20,157	-16,711	-10,760	-1,405	-291	-338	-324
On-budget	-29,180	-42,193	-24,564	-20,157	-16,711	-10,760	-1,405	-291	-338	-324
Off-budget[b]	-1	-13	-3	0	0	0	0	0	0	0

a. Estimate includes effects on outlays from refundable tax credits. A breakdown of the separate outlay effects for this provision is not available.

b. The provision that provides parity in the application of certain limits to mental health benefits, which is included in the estimate for extension of certain other expiring provisions, contains both on- and off-budget effects on revenues.

c. All estimated changes in outlays are on-budget.

d. Negative amounts indicate an increase in the deficit.

SOURCES: CBO and the Joint Committee on Taxation.

BASIS OF ESTIMATE

Most of the budgetary effects of the legislation are reductions in revenues. However, the act also would increase outlays by making various changes to the income tax brackets and certain available exemptions and credits. By reducing the amount of taxes owed, those changes would result in a larger portion of tax credits being refundable—and thus recorded as outlays rather than reductions in revenues. In total, enacting H.R. 1308 would increase the budget deficit by $29 billion in 2005, $133 billion over the 2005-2009 period, and $146 billion over the 2005-2014 period.

Revenues

With the exception of the estimates for the provision extending increased limits for mental health parity, JCT provided all the revenue estimates. CBO and JCT estimate that enacting the provisions contained in H.R. 1308 would decrease federal revenues by about $27 billion in 2005, $112 billion over the 2005-2009 period, and $122 billion over the 2005-2014 period.

Extensions of Family Tax Provisions. Title I extends several individual income tax provisions that were enacted as part of EGTRRA and modified by JGTRRA. Most of the estimated effect on revenues over the 10-year period results from three provisions:

- *Increasing the Child Tax Credit.* Prior-law changes set the amount of the child credit at $1,000 for 2004, $700 for 2005-2008, $800 for 2009, and $1,000 for 2010. JCT estimates maintaining the child credit at $1,000 through 2009 would decrease revenues and increase refundable outlays by $61.6 billion over the 2005-2010 period, with no effect thereafter.

- *Extending Marriage Penalty Relief.* EGTRRA provided marriage penalty relief by increasing the dollar amounts that define the 15-percent tax bracket and the standard deduction for married taxpayers filing a joint return to twice those of single taxpayers. Those increases were scheduled to phase in over the 2003-2008 period. JGTRRA temporarily accelerated the phase-in, making those dollar amounts for married taxpayers twice those of single taxpayers for 2003 and 2004. JCT estimates that maintaining that marriage penalty relief through 2008 would decrease revenues and increase refundable outlays by $15.7 billion over the 2005-2009 period, with no effect thereafter.

- *Extending the 10-percent Rate Bracket.* Under EGTRRA, the 10-percent bracket amounts were initially set at $6,000 for single taxpayers and $12,000 for married taxpayers. In 2008, those amounts would increase to $7,000 and $14,000, respectively, and would be adjusted annually for inflation thereafter. JGTRRA temporarily accelerated the higher amounts to 2003 and 2004, with indexing. H.R. 1308 extends that increase through 2010, which JCT estimates would decrease revenues and increase refundable outlays by about $25 billion over the 2006-2009 period and $29.4 billion over the 2006-2011 period, with no effect beyond 2011.

In total, JCT estimates that those three provisions would result in reductions of revenues of about $12.3 billion in 2005, $77.2 billion over the 2005-2009 period, and $85.5 billion over the 2005-2011 period. Together, the three provisions also would increase outlays by about $18.2 billion over the 2005-2009 period and $21.2 billion over the 2005-2011 period; however, the effects on outlays cannot be separated out for each provision.

In addition, title I makes several other changes, including extending for one year the increased AMT exemption amounts that were set to expire at the end of 2004. JCT estimates doing so would decrease revenues by about $22.6 billion between 2005 and 2006. Title I also accelerates to 2004 the increase in refundability of the child tax credit scheduled for 2005, which would result in an estimated reduction in revenues of $64 million in 2005 and an increase in outlays of about $1.9 billion in the same year. Finally, it modifies the treatment of combat pay (which generally is excluded when calculating gross income) to include it as earned income for purposes of computing the refundable portion of the child credit. For 2004 and 2005, H.R. 1308 also provides taxpayers earning combat pay the option to include it as income when computing their earned income tax credit. JCT estimates that those changes in the treatment of combat pay would reduce revenues by $6 million over the 2005-2006 period and increase outlays by $193 million over the 2005-2014 period.

Uniform Definition of a Qualifying Child. Title II establishes a uniform definition of a qualifying child, simplifying the various sets of criteria that taxpayers with children must meet in order to qualify for the exemption for dependents, child tax credit, earned income tax credit, dependent care credit, and head-of-household filing status. That definition applies to taxable years beginning after December 31, 2004, and would reduce revenues over the 2005-2014 period by about $1.3 billion and increase outlays over the same period by $325 million.

Extensions of Certain Expiring Provisions. Title III extends 23 provisions scheduled to expire or that have already expired. Roughly 60 percent of the revenue effects for the 2005-2014 period (a revenue decrease of about $7.6 billion) results from the extension of the research and experimentation credit, which expired on June 30, 2004, and would be extended under H.R. 1308 through December 31, 2005. Among the other provisions is the one-year extension of parity when applying certain limits to mental health benefits. CBO estimates this extension would decrease revenues by $57 million between 2005 and 2007. (Of this reduction, $17 million would apply to off-budget receipts.) In total, the extension of expiring provisions would result in revenue decreases of about $5.6 billion in 2005, $11.6 billion over the 2005-2009 period, and $12.8 billion over the 2005-2014 period.

Direct Spending

Outlays from Refundable Tax Credits. JCT provided the outlay effects resulting from the refundable tax credits contained in titles I and II. In total, JCT estimates that the provisions in title I would increase outlays by about $23.3 billion over the 2005-2014 period. Nearly all of that increase ($21.2 billion between 2006 and 2011) is due to extending the increased child tax credit, marriage penalty relief, and the 10-percent bracket. As described earlier, these provisions also affect revenues, and separate estimates of the effects on outlays for each of these three provisions are not available.

JCT estimates that accelerating the increase in the refundability of the child tax credit would increase outlays by about $1.9 billion in 2005, with no effect thereafter. Modifying the treatment of combat pay for computing the refundable child tax credit and the earned income tax credit would result in an estimated $193 million in additional outlays over the 2005-2011 period.

Title II establishes a uniform definition of a qualifying child for purposes of determining whether or not taxpayers with children are eligible for the exemption for dependents, child credit, earned income tax credit, dependent care credit, and head-of-household filing status. JCT estimates that doing so would increase outlays by $325 million over the 2005-2014 period.

Cover Over (Payment) of Tax on Distilled Spirits. Under current law, an excise tax of $13.50 per proof gallon is assessed on distilled spirits produced or brought into the United States. The treasuries of Puerto Rico and the Virgin Islands had received $13.25 per proof gallon of the excise tax on rum imported into the U.S. from any country or those possessions (that amount is known as the tax cover over) through December 31, 2003. Since then, the treasuries have received a lower payment of $10.50 per proof gallon. Under H.R. 1308, the payments would revert back to $13.25 per proof gallon of tax assessments made between January 1, 2004, and December 31, 2005. Those payments are recorded as outlays in the budget. Based on recent tax and payment data, CBO estimates that increasing the possessions' share of the excise tax would increase direct spending by $169 million over fiscal years 2005-2006.

SUMMARY OF THE EFFECTS ON REVENUES AND DIRECT SPENDING

The effects of H.R. 1308 on on-budget revenues and direct spending over the 2005-2014 period are shown in the following table.

	By Fiscal Year, in Millions of Dollars									
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Changes in receipts	-27,054	-37,306	-20,033	-15,624	-12,186	-7,855	-1,210	-266	-312	-298
Changes in outlays	2,126	4,887	4,531	4,533	4,525	2,905	195	25	26	26

SOURCES: CBO and the Joint Committee on Taxation.

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