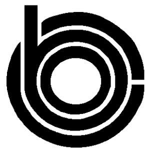

CONGRESSIONAL BUDGET OFFICE
PAY-AS-YOU-GO ESTIMATE

May 3, 2002

H.R. 3090
Job Creation and Worker Assistance Act of 2002

As signed by the President on March 9, 2002

SUMMARY

H.R. 3090, enacted as Public Law 107-147, reduces tax receipts from corporations by providing special depreciation allowances and increasing and extending certain deductions and exemptions. The act also provides certain tax benefits for areas of New York City damaged on September 11, 2001, and additional weeks of unemployment benefits to recipients who exhaust their eligibility for regular state benefits. In addition, the act extends numerous tax credits and makes other changes in tax law and spending programs.

CBO and the Joint Committee on Taxation (JCT) estimate that Public Law 107-147 will decrease governmental receipts by $42.5 billion in 2002, by $81.6 billion over the 2002-2007 period, and by $29.7 billion over the 2002-2012 period. In addition, the act will increase direct spending by $8.3 billion in 2002, $11.9 billion over the 2002-2007 period, and about the same amount over the 2002-2012 period. In total, Public Law 107-147 will reduce total surpluses by an estimated $41.6 billion over the 2002-2012 period.

Section 502 designates certain amounts of receipts and outlays as emergency requirements for purposes of enforcing pay-as-you-go procedures. CBO estimates that none of the revenue or outlay changes over the 2002-2006 period should be counted for pay-as-you-go purposes. The net changes in outlays and governmental receipts are shown in the following table.

TABLE 1. ESTIMATED IMPACT OF PUBLIC LAW 107-147 ON ON-BUDGET DIRECT SPENDING AND REVENUES

	By Fiscal Year, in Millions of Dollars										
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Total Effects on Direct Spending and Revenues (On-budget)[a]											
Changes in receipts	-42,526	-39,335	-29,048	-3,548	16,101	16,814	16,042	13,666	10,140	7,246	4,724
Changes in outlays	8,343	3,587	60	23	-14	-40	-36	-10	3	3	4
Effects Designated as Emergency Requirements											
Changes in receipts	-42,526	-39,335	-29,048	-3,548	16,101	16,814	16,042	13,666	10,140	7,246	4,724
Changes in outlays	8,343	3,587	60	23	-14	-40	-36	-10	3	3	4
Budgetary Effects Counted for Pay-As-You-Go Purposes											
Changes in receipts	0	0	0	0	0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Changes in outlays	0	0	0	0	0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Notes: n.a. = Not applicable. Pay-as-you-go enforcement procedures do not apply after 2006.

a. Social Security revenues and outlays are excluded from pay-as-you-go calculations. Social Security revenues will decline by $10 million in 2003, but be offset by a $10 million transfer (outlays) in 2004.

MAJOR PROVISIONS

Title I, entitled *Business Provisions*:

- Allows taxpayers to deduct an additional 30 percent of the value of certain qualifying capital assets and software in the first year if such property is placed in service between September 11, 2001, and September 11, 2004 (revenue loss of $35.3 billion in 2002, $59.5 billion over the 2002-2007 period, and $15.8 billion over the 2002-2012 period); and

- Temporarily expands the ability of unprofitable corporations to receive refunds of past taxes paid. The provision allows firms with current losses to receive refunds of taxes paid as many as five years earlier, compared to generally two years earlier under prior law. However, it only applies to losses in tax years 2001 or 2002 (revenue loss of $7.9 billion in 2002, $4.3 billion over the 2002-2007 period, and $2.1 billion over the 2002-2012 period).

Title II, entitled *Unemployment Assistance*:

- Provides up to 13 weeks of temporary extended unemployment benefits for those who exhaust their regular benefits in all states and an additional 13 weeks for those in any state with an insured unemployment rate of at least 4 percent (outlay increase of $11.6 billion during the 2002-2003 period); and

- Accelerates transfers from the federal unemployment accounts to the state accounts in the unemployment trust fund (for both provisions of title II, revenue loss of $1.2 billion over the 2002-2007 period and revenue gain of $8.8 billion over the 2002-2012 period).

Title III, entitled *Tax Incentives for New York City and Distressed Areas*:

- Expands the work opportunity tax credit to include a new targeted group of employees, which includes workers employed by businesses located in the New York Liberty Zone (Manhattan Island south of Canal or Grand Streets) or relocated from the New York Liberty Zone elsewhere in New York City as a result of the events of September 11, 2001 (revenue loss of $119 million in 2002 and $631 million over the 2002-2007 period);

- Allows taxpayers to deduct an additional 30 percent of the value of certain qualifying capital assets and software located in the New York Liberty Zone in the first year if such property is purchased after September 11, 2001, and placed in service generally on or before December 31, 2006 (revenue loss of $622 million in 2002, $2.9 billion over the 2002-2007 period, and $1.6 billion over the 2002-2012 period);

- Authorizes issuance of $8 billion in tax-exempt private-activity bonds in calendar years 2002, 2003, and 2004 to finance construction and rehabilitation of commercial and residential rental property in the New York Liberty Zone and makes interest from such bonds exempt from alternative minimum tax treatment as a preference item (revenue loss of $11 million in 2002, $544 million over the 2002-2007 period, and $1.2 billion over the 2002-2012 period);

- Allows $9 billion of certain bonds for facilities located in New York City to be used to redeem a prior bond issuance after 90 days for those bonds issued before January 1, 2005, generating more favorable tax treatment (revenue loss of $103 million in 2002, $698 million over the 2002-2007 period, and $937 billion over the 2002-2012 period);

- Increases the amount that taxpayers can deduct for investment in qualifying property in the New York Liberty Zone by $35,000 for property placed in service after September 11, 2001, and before January 1, 2007 (revenue loss of $36 million in 2002, $162 million over the 2002-2007 period, and $37 million over the 2002-2012 period);

- Reduces certain capital gains realizations by extending the replacement period from generally two years to five years for those taxpayers whose property was involuntarily converted within the New York Liberty Zone as a result of the attack of September 11, 2001, if substantially all the replacement property is in New York (revenue loss of $145 million in 2002, $355 million over the 2002-2007 period, and $318 million over the 2002-2012 period); and

- Allows lessors to treat qualified New York Liberty Zone leasehold improvement property as five-year property for depreciation purposes (revenue loss of $11 million in 2002, $368 million over the 2002-2007 period, and $595 million over the 2002-2012 period).

The provisions of title III interact with other provisions in Public Law 107-147, resulting in an additional revenue gain of $563 million in 2002, $1 billion over the 2002-2007 period, and $285 million over the 2002-2012 period.

Title IV, entitled *Miscellaneous and Technical Provisions*:

- Prohibits shareholders from increasing the basis of their stock in an S corporation as a result of excluding from taxable income the amount of the corporation's canceled debts (revenue gain of $34 million in 2002, $470 million over the 2002-2007 period, and $982 million over the 2002-2012 period);

- Limits the use of the non-accrual experience method of accounting to the amount to be received for the performance of qualified professional services (revenue gain $5 million in 2002, $161 million over the 2002-2007 period, and $228 million over the 2002-2012 period);

- Expands the exclusion from income for qualified foster care payments (revenue loss of $17 million in 2002, $240 million over the 2002-2007 period, and $692 million over the 2002-2012 period);

- Increases the interest rate used in determining additional qualified contributions to defined benefit pension plans and variable-rate premiums charged by the Pension Benefit Guaranty Corporation (PBGC) for plan years beginning after December 31,

2001, and before January 1, 2004 (revenue gain of $2 billion in 2002, revenue gain of $1 billion over the 2002-2007 period, and revenue loss of $2.9 billion over the 2002-2012 period; outlay reductions of $89 million over the 2002-2007 period and $139 million over the 2002-2012 period);

- Provides a deduction in calculating adjusted gross income for up to $250 annually for expenses incurred by eligible educators for taxable years beginning after December 31, 2001, and before January 1, 2004 (revenue loss of $152 million in 2002 and $409 million over the 2002-2004 period); and

- Makes several technical corrections to previously enacted legislation (revenue loss of $7 million over the 2002-2012 period).

Title V, entitled *Social Security Held Harmless; Budgetary Treatment of Act*, specifies that any effects on the balances of Social Security trust funds shall be offset by transfers from the general fund. Also, certain amounts of receipts and outlays are designated as emergency requirements for purposes of enforcing pay-as-you-go procedures, based on revenue levels specified in H. Con. Res. 83, the concurrent resolution on the budget for fiscal year 2002, and on the spending allocations to the Senate Finance Committee.

Title VI, entitled *Extensions of Certain Expiring Provisions*:

- Extends for five years the provision allowing an exemption from taxable income for certain financing income earned abroad (revenue loss of $315 million in 2002 and $9 billion over the 2002-2007 period);

- Allows an individual to offset all regular tax liability and alternative minimum tax liability by personal nonrefundable credits in 2002 and 2003 (revenue loss of $85 million in 2002 and $1 billion over the 2002-2004 period);

- Extends the work opportunity tax credit and the welfare-to-work tax credit (revenue loss of $126 million in 2002 and more than $800 million over the 2002-2007 period);

- Increases certain payments to Puerto Rico and the Virgin Islands relating to excise taxes on rum manufactured in those territories and rum imported from other countries (outlays of $65 million in 2002 and $140 million over the 2002-2004 period);

- Extends the Mental Health Parity Act of 1996 for an additional year (revenue loss of $30 million over the 2003-2004 period);

- Extends other tax provisions, including deductions for mutual life insurance companies, accelerated depreciation for property on Indian reservations, and credits and deductions for energy-related production and purchases (revenue loss of $118 million in 2002, $1.8 billion over the 2002-2007 period, and $2.0 billion over the 2002-2012 period);

- Reauthorizes, for 2002, supplemental grants for population increases under the Temporary Assistance for Needy Families (TANF) program (outlay increase of $63 million in 2002 and $315 million over the 2002-2007 period); and

- Extends the contingency fund under TANF through September 30, 2002 (outlay increase of $23 million over the 2002-2012 period).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of Public Law 107-147 is shown in the following table. Most of the budgetary effects of the legislation are reductions in revenues.

CBO estimates that all of the on-budget effects of the act are to be designated as emergencies under the language of section 502 and are thus excluded from pay-as-you-go calculations. Under that section, the amount of the revenue losses that fall below the recommended levels of federal revenue in the 2002 budget resolution (H. Con. Res. 83) is designated as an emergency request. Under CBO's March 2002 baseline, revenues are already well below the levels specified in the concurrent resolution on the budget for 2002 and will remain so under the legislation. Section 502 also specifies that additional spending under Public Law 107-147 shall be designated an emergency request to the extent that it exceeds the allocations to the Senate Committee on Finance under section 302(a) of the Congressional Budget Act. CBO estimates that spending for programs under the jurisdiction of the Senate Committee on Finance is sufficiently above its allocations under the budget resolution that all spending effects fall under the emergency designation.

TABLE 2. ESTIMATED BUDGETARY IMPACT OF PUBLIC LAW 107-147

	By Fiscal Year, in Millions of Dollars										
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
CHANGES IN REVENUES											
Title I: Business Provisions	-43,256	-39,001	-24,981	3,001	20,842	19,521	16,194	12,206	8,411	5,597	3,563
Title II: Unemployment Assistance	0	-950	-1,030	-540	265	1,035	1,715	2,750	2,445	1,880	1,260
Title III: Tax Incentives for New York City and Distressed Areas	-484	-789	-629	-1,041	-1,262	-561	-156	-154	-16	36	27
Title IV: Miscellaneous and Technical Provisions	1,858	3,943	422	-2,406	-1,262	-1,584	-1,728	-1,174	-689	-190	-16
Title VI: Extensions of Expiring Provisions	-644	-2,548	-2,830	-2,562	-2,482	-1,597	17	38	-11	-77	-110
Total Changes in Revenues	-42,526	-39,345	-29,048	-3,548	16,101	16,814	16,042	13,666	10,140	7,246	4,724
On-Budget	-42,526	-39,335	-29,048	-3,548	16,101	16,814	16,042	13,666	10,140	7,246	4,724
Off-Budget	0	-10	0	0	0	0	0	0	0	0	0
CHANGES IN DIRECT SPENDING											
Unemployment Assistance	8,215	3,360	0	0	0	0	0	0	0	0	0
Pension Benefit Guaranty Corporation	0	102	-28	-42	-48	-73	-38	-12	0	0	0
Payments to Puerto Rico and Virgin Islands	65	61	14	0	0	0	0	0	0	0	0
Temporary Assistance for Needy Families and Food Stamps	63	64	64	65	34	33	2	2	3	3	4
Transfer to Social Security Trust Funds											
On-Budget	0	0	10	0	0	0	0	0	0	0	0
Off-Budget	0	0	-10	0	0	0	0	0	0	0	0
Total Changes in Outlays	8,343	3,587	50	23	-14	-40	-36	-10	3	3	4
On-Budget	8,343	3,587	60	23	-14	-40	-36	-10	3	3	4
Off-Budget	0	0	-10	0	0	0	0	0	0	0	0
Net Increase or Decrease (-) in the Budget Surplus	-50,869	-42,932	-29,098	-3,571	16,115	16,854	16,078	13,676	10,137	7,243	4,720

SOURCES: Joint Committee on Taxation and Congressional Budget Office

BASIS OF ESTIMATE

Revenues

All the estimates for the revenue provisions, with the exception of the provision relating to unemployment trust fund revenues (detailed in the direct-spending section) and the provision relating to the extension of the Mental Health Parity Act of 1996, were provided by the JCT. Of the provisions estimated by the JCT, four provisions comprise most of the changes in revenues. The provisions that allow taxpayers to deduct an additional 30 percent of the value of certain assets, allow a carryback of net operating losses, provide tax benefits for areas of New York City damaged on September 11, 2001, and extend exceptions from active financing income reduce revenues by an estimated $44 billion in 2002, $78 billion over the 2002-2007 period, and $32 billion over the 2002-2012 period.

Unemployment Assistance. CBO projects revenue effects from both the provision of temporary, emergency benefits to unemployed persons and from the transfer of additional funds to state accounts required by section 204. Taken together, those changes will increase balances in state trust funds for unemployment in the first few years of the projection period. CBO expects that the increase will allow states to reduce trust fund income by reducing unemployment insurance tax rates or postponing increases in those tax rates. Because those taxes are recorded as revenues in the federal budget, such actions reduce federal revenues. In later years, the changes in Public Law 107-147 will reduce balances in state trust funds, and states are assumed to respond by raising revenue. As a result of those changes, CBO projects revenues to decline by $2.5 billion from 2003 to 2005. CBO projects revenues to rise, however, by $8.8 billion over the 2003-2012 period. (Further details about this provision are provided in the discussion of the impact on direct spending.)

Mental Health Parity. Section 610 extends the provisions of the Mental Health Parity Act of 1996, which is scheduled to expire at the end of calendar year 2002, through the end of calendar year 2003. That act prohibits group health plans that provide both medical and surgical benefits and mental health benefits from imposing aggregate lifetime limits or annual limits for coverage of mental health benefits that are different from those used for medical and surgical benefits. CBO estimates that this provision will increase premiums for group health insurance by an average of 0.1 percent, before accounting for the responses of health plans, employers, and workers to the higher premiums under the act. CBO assumes that 60 percent of that increase will be offset by purchasers switching to less expensive plans, cutting back on benefits, or dropping coverage. The remaining costs will be passed through to employees of private firms, reducing both their taxable compensation and other fringe benefits. Reductions in taxable compensation will lead to lower federal tax revenues. CBO estimates that, as a result of the mental health parity provisions, federal tax revenues will fall by $30 million in fiscal year 2003 and by $10 million in 2004, with no effect in subsequent

years. (These amounts are included in the totals for Title VI in Table 2.) Of that decline, $10 million is a reduction in receipts from Social Security taxes in 2003.

Direct Spending

Unemployment Compensation. Public Law 107-147 will provide temporary, emergency benefits to unemployed persons who exhaust their receipt of regular unemployment compensation. The long-term unemployed will receive up to 13 weeks of emergency compensation regardless of their state's unemployment rate. In states where the insured unemployment rate (IUR) exceeds 4 percent, beneficiaries can receive another 13 weeks of benefits. No benefits resulting from this legislation can be paid after January 1, 2003. CBO estimates these provisions will increase outlays for unemployment compensation by $8.2 billion in fiscal year 2002 and $3.4 billion in fiscal year 2003.

In estimating the benefits to be paid under this law, CBO assumes that roughly 80,000 recipients of unemployment compensation will exhaust their regular benefits each week, and will draw, on average, about 10 weeks of emergency benefits under the first tier of benefits. CBO estimates that about half of the beneficiaries who exhausted regular benefits between March 15, 2001, and the date of enactment will collect emergency benefits. CBO assumes that about one-third of all beneficiaries would be in states that would meet the 4 percent IUR trigger, making them eligible for an additional period of emergency benefits. The costs of emergency benefits will total about $10.3 billion over the 2002-2003 period, including costs of administering the benefits.

These costs will be offset by a reduction of about $0.7 billion in spending on the existing program for extended benefits. However, CBO estimates that the availability of additional benefits will increase slightly the average number of compensated weeks in the regular benefits program, raising outlays under that program by about $1.9 billion. CBO estimates the net increase in spending on unemployment benefits will total $11.6 billion.

In addition, Public Law 107-147 will require the transfer of $8 billion to the state accounts in the unemployment trust fund. CBO estimates that this is an acceleration of transfers that would have occurred in future years under prior law. CBO expects that this transfer will not affect outlays but will affect states' benefit accounts and how states set their unemployment tax rates.

Pension Benefit Guaranty Corporation. Section 405 makes two changes to the way funding levels are calculated for defined-benefit pension plans under the Internal Revenue Code and the Employee Retirement Income Security Act (ERISA).

Section 405 changes the formula used to determine premiums paid by single-employer pension plans to the Pension Benefit Guaranty Corporation (PBGC). All plans pay a flat, per-participant premium and, in addition, those plans that are not fully funded pay a variable-rate premium based on the degree of underfunding. Previous law required that the interest rate used to calculate a plan's liabilities be 85 percent of the interest rate on 30-year Treasury securities in the month preceding the month in which the plan year begins. Furthermore, previous law required that once the Department of the Treasury issues new mortality tables for pension beneficiaries, the liability calculation would be 100 percent of the 30-year Treasury bond rate for the preceding month. As part of its latest baseline projections, CBO anticipated that this change would become effective with plan year 2003.

Section 405 mandates that the interest rate used to determine a plan's liabilities be changed to 100 percent of the interest rate for 30-year Treasury securities, starting in plan-months after December 31, 2001. Increasing the interest rate used to determine benefits effectively lowers the amount of underfunding among plans because using higher interest rates reduces the discounted present value of projected liabilities. Because it reduces the calculated level of underfunding, CBO anticipates the act will lower variable-rate premiums collected by PBGC. Based on information provided by PBGC, CBO estimates that this provision of section 405 will reduce these collections by $102 million in 2003 relative to the CBO baseline.

Section 405 also makes changes to the funding requirements in 2002 and 2003 for defined-benefit pension plans sponsored by single employers. CBO anticipates that the new law will cause employers to reduce contributions to their pension plans during 2002 and 2003 and increase contributions in later years. As a result, CBO anticipates that the level of actual underfunding among covered plans will increase for several years and then return to baseline levels. Since underfunded liability is used to determine variable-rate premiums, CBO projects that this portion of section 405 will cause collections by PBGC to increase until 2009. Based on information from PBGC, CBO estimates that this provision will cause collections to increase by $241 million over the 2003-2009 period.

Overall, CBO projects that section 405 will decrease collections by PBGC by $102 million in 2003 but increase them by $139 million during the 2003-2012 period.

Cover Over of Tax on Distilled Spirits. A tax of $13.50 per proof gallon is currently assessed on distilled spirits produced in or brought into the United States. Under Public Law 107-147, the treasuries of Puerto Rico and the Virgin Islands will receive an increase from $10.50 to $13.25 of the tax assessed on rum manufactured in either territory between January 1, 2002, and December 31, 2003. (Beginning January 1, 2004, the amount of the federal excise tax the government shares with the territories will fall to $10.50.) In addition,

the territories receive payments, at a similar rate, on all rum imported into the United States from any foreign country.

Those payments to Puerto Rico and the Virgin Islands are recorded as outlays in the budget. Based on recent tax and payment data, CBO estimates that increasing the territories' share of the excise tax will increase direct spending by $65 million in 2002 and by $140 million over the 2002-2004 period.

Temporary Assistance for Needy Families. Public Law 107-147 extends two provisions of the Temporary Assistance for Needy Families program. The TANF program provides block grants to states for the operation of welfare programs.

Section 616 extends the Supplemental Grant for Population Increases in Certain States program for an additional year at its 2001 funding level of $319 million. Seventeen states qualified for grants in 2001 based on their poverty level and population growth. CBO expects that states will spend the grants slowly over the next six years, spending $64 million in 2002 and $319 million over the 2002-2012 period. Many states have accumulated significant unspent balances from their TANF grants in 1997-2001, and we expect that those states will not spend much of the new money until they draw down on past balances.

CBO expects that some of the additional funding provided will be used to increase benefits to families that also receive food stamps. The additional TANF income would reduce the Food Stamp benefit, so we expect small savings in the Food Stamp program, totaling $4 million over the 2002-2012 period.

Section 617 extends the Contingency Fund for State Welfare Programs. The contingency fund provides additional federal funds to states with high and increasing unemployment rates or significant growth in Food Stamp caseloads. Based on CBO’s projections of unemployment, Food Stamp participation, and state TANF spending, CBO estimates that states will draw $1 million from the contingency fund for fiscal year 2002 and $23 million over the 2002-2012 period.

While CBO estimates that as many as 16 states might meet the unemployment or Food Stamp trigger in a particular year, we expect that states will not draw down most of the contingency fund money for which they are potentially eligible and many eligible states will draw down nothing. In order to draw money from the contingency fund, eligible states must spend at least as much as they spent on welfare programs in 1994 and match federal payments at the rate used in the Medicaid program (pro-rated for the percentage of the year that they qualify), a requirement that CBO expects relatively few states will meet.

The act extends the supplemental grant and the contingency fund through 2002. Both are provisions of the TANF program, which also expires in 2002 . In accordance with the instructions governing baseline projections specified in section 257 of the Balanced Budget and Emergency Deficit Control Act of 1985, CBO assumes that the contingency fund will continue when it expires at the end of 2002. Public Law 107-147 directs CBO to assume that the supplemental grants program does not continue after 2002, notwithstanding section 257.

Transfer to Social Security Trust Funds. Section 610, which extends the Mental Health Parity Act of 1996, will reduce Social Security revenue in 2003 by an estimated $10 million. However, section 501 of the act requires the Secretary of the Treasury to hold the trust funds harmless for any effects of the legislation. CBO expects that the Secretary will transfer $10 million to the Social Security trust funds at the end of 2004 to fulfill this requirement.

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