FEDERAL RECEIPTS AND COLLECTIONS

4. FEDERAL RECEIPTS

Receipts (budget and off-budget) are taxes and other collections from the public that result from the exercise of the Federal Government's sovereign or governmental powers. The difference between receipts and outlays determines the surplus or deficit.

The Federal Government also collects income from the public from market-oriented activities. Collections from these activities, which are subtracted from gross outlays, rather than added to taxes and other governmental receipts, are discussed in the following chapter.

Growth in receipts.—Total receipts in 2003 are estimated to be $2,048.1 billion, an increase of $101.9 billion or 5.2 percent relative to 2002. Receipts are projected to grow at an average annual rate of 5.9 percent between 2003 and 2007, rising to $2,571.7 billion. This growth in receipts is largely due to assumed increases in incomes resulting from both real economic growth and inflation.

As a share of GDP, receipts are projected to decline from 19.6 percent in 2001 to 18.8 percent in 2002 and 2003. The receipts share of GDP is projected to increase to 19.1 percent in 2007, despite the phasein of legislated tax reductions and the President's proposed tax plan.

Table 4–1. RECEIPTS BY SOURCE—SUMMARY

(In billions of dollars)

Source	2001 actual	Estimate					
		2002	2003	2004	2005	2006	2007
Individual income taxes	994.3	949.2	1,006.4	1,058.6	1,112.0	1,157.3	1,221.7
Corporation income taxes	151.1	201.4	205.5	212.0	237.1	241.4	250.6
Social insurance and retirement receipts	694.0	708.0	749.2	789.8	835.2	868.7	908.3
(On-budget)	(186.4)	(190.8)	(203.9)	(216.3)	(227.0)	(235.1)	(243.0)
(Off-budget)	(507.5)	(517.2)	(545.3)	(573.5)	(608.2)	(633.7)	(665.3)
Excise taxes	66.1	66.9	69.0	71.2	73.6	75.3	77.5
Estate and gift taxes	28.4	27.5	23.0	26.6	23.4	26.4	23.2
Customs duties	19.4	18.7	19.8	21.9	23.0	24.7	26.2
Miscellaneous receipts	37.8	36.4	40.2	42.8	43.2	44.4	46.2
Bipartisan economic security plan	....	–62.0	–65.0	–47.5	–9.5	17.0	18.0
Total receipts	**1,991.0**	**1,946.1**	**2,048.1**	**2,175.4**	**2,338.0**	**2,455.3**	**2,571.7**
(On-budget)	*(1,483.5)*	*(1,428.9)*	*(1,502.7)*	*(1,601.9)*	*(1,729.8)*	*(1,821.6)*	*(1,906.4)*
(Off-budget)	*(507.5)*	*(517.2)*	*(545.3)*	*(573.5)*	*(608.2)*	*(633.7)*	*(665.3)*

Table 4–2. EFFECT ON RECEIPTS OF CHANGES IN THE SOCIAL SECURITY TAXABLE EARNINGS BASE

(In billions of dollars)

	Estimate				
	2003	2004	2005	2006	2007
Social security (OASDI) taxable earnings base increases:.					
$84,900 to $89,700 on Jan. 1, 2003	2.2	5.8	6.4	7.0	7.7
$89,700 to $92,400 on Jan. 1, 2004	....	1.3	3.3	3.6	3.9
$92,400 to $96,000 on Jan. 1, 2005	....	....	1.7	4.5	4.9
$96,000 to $99,900 on Jan. 1, 2006	....	....	....	1.9	4.9
$99,900 to $103,800 on Jan. 1, 2007	....	....	....	....	1.9

ENACTED LEGISLATION

Several laws were enacted in 2001 that have an effect on governmental receipts. The major legislative changes affecting receipts are described below.

ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT OF 2001 (EGTRRA)

From the Administration's first day in office, President Bush worked to deliver on his campaign promise of meaningful tax relief. Congress moved with exceptional speed and on June 7, 2001, this Act was signed by President Bush. The major provisions of this Act, which are described in greater detail below, create a new 10-percent individual income tax rate bracket; reduce marginal income tax rates for individuals; eliminate the estate tax; reduce the marriage penalty; provide relief from the alternative minimum tax (AMT); modify the timing of estimated tax payments by corporations; and modify tax benefits for children, education, and pension and retirement savings. Almost all of the provisions phase in over a number of years and sunset on December 31, 2010.

Individual Income Tax Relief

Create a new 10-percent individual income tax rate bracket.—Effective for taxable years beginning after December 31, 2000 and before January 1, 2011, the prior law 15-percent individual income tax rate bracket is split into two tax rate brackets of 10 and 15 percent. The new 10-percent tax rate bracket applies to the first $6,000 of taxable income for single taxpayers and married taxpayers filing separate returns (increasing to $7,000 for taxable years beginning after December 31, 2007), the first $10,000 of taxable income for heads of household, and the first $12,000 of taxable income for married taxpayers filing a joint return (increasing to $14,000 of taxable income for taxable years beginning after December 31, 2007). Taxable income above these thresholds that was taxed at the 15-percent rate under prior law will continue to be taxed at that rate. The income thresholds for the new tax rate bracket will be adjusted annually for inflation, effective for taxable years beginning after December 31, 2008 and before January 1, 2011.

For 2001, most taxpayers received the benefit of the new 10-percent tax rate bracket through an advanced credit, issued by the Department of Treasury in the form of a check. The amount of the advanced credit was equal to 5 percent of taxable income reported on tax returns filed for 2000, up to a maximum credit of $300 for single taxpayers and married taxpayers filing separate returns, $500 for heads of household, and $600 for married taxpayers filing a joint return. Taxpayers are entitled to a similar credit on tax returns filed for 2001 to the extent that it exceeds the advanced credit, if any, that they received on the basis of tax returns filed for 2000.

Reduce individual income tax rates.—In addition to splitting the 15-percent tax rate bracket of prior law into two tax rate brackets (see preceding discussion), this Act replaces the four remaining statutory individual income tax rate brackets of prior law (28, 31, 36, and 39.6 percent) with a rate structure of 25, 28, 33, and 35 percent. The reduced tax rate structure is phased in over a period of six years, effective for taxable years beginning after December 31, 2000, as follows: the 28-percent rate is reduced to 27.5 percent for 2001, 27 percent for 2002 and 2003, 26 percent for 2004 and 2005, and 25 percent for 2006 through 2010; the 31 percent rate is reduced to 30.5 for 2001, 30 percent for 2002 and 2003, 29 percent for 2004 and 2005, and 28 percent for 2006 through 2010; the 36 percent rate is reduced to 35.5 percent for 2001, 35 percent for 2002 and 2003, 34 percent for 2004 and 2005, and 33 percent for 2006 through 2010; and the 39.6 percent rate is reduced to 39.1 percent for 2001, 38.6 percent for 2002 and 2003, 37.6 percent for 2004 and 2005, and 35 percent for 2006 through 2010. The income thresholds for these tax rate brackets are adjusted annually for inflation as provided under prior law.

Repeal phaseout of personal exemptions.—Under prior law, the deduction for taxpayer and dependent personal exemptions ($2,900 for taxable year 2001), began to be phased out for taxpayers with adjusted gross income (AGI) over certain thresholds (for taxable year 2001, the thresholds were $132,950 for single taxpayers, $166,200 for heads of household, $99,725 for married taxpayers filing separate returns, and $199,450 for married taxpayers filing a joint return). For taxable year 2001, the deduction for personal exemptions was fully phased out above AGI of $255,450 for single taxpayers, $288,700 for heads of household, $160,975 for married taxpayers filing separate returns, and $321,950 for married taxpayers filing a joint return. This Act phases in the repeal of the phaseout of personal exemptions over a five-year period, effective for taxable years beginning after December 31, 2005. The otherwise applicable personal exemption phaseout is reduced by one-third for taxable years 2006 and 2007, is reduced by two-thirds for taxable years 2008 and 2009, and is repealed for taxable year 2010.

Repeal limitation on itemized deductions.—Under prior law, the amount of otherwise allowable itemized deductions (other than medical expenses, investment interest, theft and casualty losses, and wagering losses) was reduced by three percent of AGI in excess of certain thresholds (for taxable year 2001, the thresholds were $66,475 for married taxpayers filing separate returns and $132,950 for all other taxpayers). This Act phases in the repeal of the limitation on itemized deductions over a five-year period, effective for taxable years beginning after December 31, 2005. The otherwise applicable limitation on itemized deductions is reduced by one-third for taxable years 2006 and 2007, is reduced by two-thirds for taxable years 2008 and 2009, and is repealed for taxable year 2010.

Tax Benefits for Children

Increase and expand the child tax credit.—Under prior law, taxpayers were provided a tax credit of up to $500 for each qualifying child under the age of 17. This Act doubles the maximum amount of the credit to $1,000 over a 10-year period, effective for taxable years beginning after December 31, 2000. The credit increases to $600 for taxable years 2001 through 2004, $700 for taxable years 2005 through 2008, $800 for taxable year 2009, and $1,000 for taxable year 2010.

Generally, the credit was nonrefundable under prior law; however, taxpayers with three or more qualifying children could be eligible for an additional refundable child tax credit if they had little or no individual income tax liability. The additional credit could be offset against social security payroll tax liability, provided that liability exceeded the refundable portion of the earned income tax credit (EITC). Under this Act, the child credit is refundable to the extent of 10 percent of the taxpayer's earned income in excess of $10,000 for taxable years 2001 through 2004. The percentage increases to 15 percent for taxable years 2005 through 2010. The $10,000 earned income threshold is indexed annually for inflation beginning in 2002. Families with three or more children are allowed a refundable credit for the amount by which their social security payroll taxes exceed their earned income credit (the prior law rule), if that amount is greater than the refundable credit based on their earned income in excess of $10,000. This Act also provides that the refundable portion of the child credit does not constitute income and shall not be treated as resources for purposes of determining eligibility or the amount or nature of benefits or assistance under any Federal program or any State or local program financed with Federal funds.

Under prior law, beginning in taxable year 2002, the child tax credit would have been allowed only to the extent that an individual's regular individual income tax liability exceeded his or her tentative minimum tax. In addition, beginning in taxable year 2002, the refundable child tax credit would have been reduced by the amount of the individual's alternative minimum tax. Effective for taxable years beginning after December 31, 2001 and before January 1, 2011, this Act allows the child credit to offset both the regular tax and the alternative minimum tax; in addition, the refundable credit will not be reduced by the amount of the alternative minimum tax.

Extend and expand adoption tax benefits.—Prior law provided a permanent nonrefundable 100-percent tax credit for the first $6,000 of qualified expenses incurred in the adoption of a child with special needs. A nonrefundable 100-percent tax credit was provided for the first $5,000 of qualified expenses incurred before January 1, 2002 in the adoption of a child without special needs. The adoption credit (including the credit for the adoption of a child with special needs) phased out ratably for taxpayers with modified AGI between $75,000 and $115,000. In addition, for taxable years beginning after December 31, 2001, the otherwise allowable adoption credit was allowed only to the extent that the taxpayer's regular income tax liability exceeded the taxpayer's tentative minimum tax. This Act increases the credit for qualified expenses incurred in the adoption of a child, including a child with special needs, to $10,000, effective for qualified expenses incurred after December 31, 2001 and before January 1, 2011. The $10,000 amount is indexed annually for inflation, effective for taxable years beginning after December 31, 2002. For the adoption of a child with special needs finalized after December 31, 2002 and before January 1, 2011, the credit is provided regardless of whether qualified adoption expenses are incurred. Effective for taxable years beginning after December 31, 2001 and before January 1, 2011, the credit (including the credit for the adoption of a child with special needs) phases out ratably for taxpayers with modified AGI between $150,000 and $190,000. The start of the phase-out range is indexed annually for inflation effective for taxable years beginning after December 31, 2002, but the width of the phase-out range remains at $40,000. In addition, for taxable years beginning after December 31, 2001 and before January 1, 2011, the adoption tax credit is allowed against the alternative minimum tax.

Under prior law, up to $5,000 per child in qualified adoption expenses paid or reimbursed by an employer under an adoption assistance program could be excluded from the gross income of an employee. The maximum exclusion was $6,000 for the adoption of a child with special needs. The exclusion, which applied to amounts paid or expenses incurred before January 1, 2002, was phased out ratably for taxpayers with modified AGI (including the full amount of the employer adoption benefit) between $75,000 and $115,000. This Act increases the maximum exclusion to $10,000 per child, including the adoption of a child with special needs, effective for expenses incurred after December 31, 2001 and before January 1, 2011. The $10,000 amount is indexed annually for inflation, effective for taxable years beginning after December 31, 2002. For the adoption of a child with special needs finalized after December 31, 2002 and before January 1, 2011, the exclusion is provided regardless of whether qualified adoption expenses are incurred. Effective for taxable years beginning after December 31, 2001 and before January 1, 2011, the exclusion (including the exclusion for the adoption of a child with special needs) phases out ratably for taxpayers with modified AGI between $150,000 and $190,000. The start of the phase-out range is indexed annually for inflation effective for taxable years beginning after December 31, 2002, but the width of the phase-out range remains at $40,000.

Expand dependent care tax credit.—Under prior law, a taxpayer could receive a nonrefundable tax credit for a percentage of a limited amount of dependent care expenses ($2,400 for one qualifying dependent and $4,800 for two or more qualifying dependents) paid in order to work. The credit rate was phased down from 30 percent of expenses (for taxpayers with AGI of $10,000 or less) to 20 percent of expenses (for taxpayers with AGI above $28,000). Effective for taxable years beginning after December 31, 2002 and before January 1, 2011, this Act increases the maximum amount of eligible employment related expenses to $3,000 for one qualifying dependent and to $6,000 for two or more qualifying dependents. In addition, the maximum credit rate is increased to 35 percent for taxpayers with AGI of $15,000 or less, and the phase down is modified so that the 20 percent rate applies to taxpayers with AGI above $43,000.

Provide tax credit for employer-provided child care facilities.—A 25-percent tax credit is provided to employers for qualified expenses incurred to build, acquire, rehabilitate, expand, or operate a child care facility for employee use, or to provide child care services to children of employees directly or through a third party. A 10-percent credit is provided for qualified expenses incurred to provide employees with child care resource and referral services. The maximum total credit for an employer may not exceed $150,000 per taxable year, and is effective for taxable years beginning after December 31, 2001 and before January 1, 2011. Any deduction the employer would otherwise be entitled to take for the expenses is reduced by the amount of the credit. The taxpayer's basis in a facility is reduced to the extent that a credit is claimed for expenses of constructing, rehabilitating, expanding, or acquiring a facility; in addition, the credit is subject to recapture for the first ten years after the qualified child care facility is placed in service.

Marriage Penalty Relief

Increase standard deduction for married taxpayers filing a joint return.—The basic standard deduction amount for single taxpayers under prior law was equal to 60 percent of the basic standard deduction amount for married taxpayers filing a joint return. Therefore, two single taxpayers had a combined standard deduction that exceeded the standard deduction of a married couple filing a joint return. This Act increases the standard deduction for married couples filing a joint return to double the standard deduction for single taxpayers over a five-year period, beginning after December 31, 2004. Under the phasein, the standard deduction for married taxpayers filing a joint return increases to 174 percent of the standard deduction for single taxpayers in taxable year 2005, 184 percent in taxable year 2006, 187 percent in taxable year 2007, 190 percent in taxable year 2008, and 200 percent in taxable years 2009 and 2010.

Expand the 15-percent tax rate bracket for married taxpayers filing a joint return.—The size of the 15-percent tax rate bracket for married taxpayers filing a joint return is increased to twice the size of the corresponding tax rate bracket for single taxpayers. The increase, which is phased in over four years, beginning after December 31, 2004, is as follows: the 15-percent tax rate bracket for married taxpayers filing a joint return increases to 180 percent of the corresponding tax rate bracket for single taxpayers in taxable year 2005, 187 percent in taxable year 2006, 193 percent in taxable year 2007, and 200 percent in taxable years 2008, 2009 and 2010.

Modify the phaseout of the earned income credit (EITC) for married taxpayers filing a joint return and simplify the EITC.— The maximum earned income tax credit is phased in as an individual's earned income increases. The credit phases out for individuals with earned income (or, if greater, modified AGI) over certain levels. For married taxpayers filing a joint return, both the phasein and phaseout of the credit are calculated based on the couples' combined income. Under this Act, for married taxpayers filing a joint return, the income threshold at which the credit begins to phase out is increased, effective for taxable years beginning after December 31, 2001 and before January 1, 2011. For married taxpayers filing a joint return the phase-out threshold increases by $1,000 for taxable years 2002 through 2004, $2,000 for taxable years 2005 through 2007, and $3,000 for taxable years 2008 through 2010. The $3,000 amount is increased annually for inflation beginning in taxable year 2009.

This Act also simplifies EITC eligibility criteria and allows the Internal Revenue Service (IRS) to use more cost efficient procedures to deny certain questionable EITC claims. In addition, effective for taxable years beginning after December 31, 2001 and before January 1, 2011, the prior law rule that reduced the EITC by the amount of the alternative minimum tax is repealed.

Education Incentives

Increase and expand education savings accounts.—Under prior law, taxpayers were permitted to contribute up to $500 per year to an education savings account (an "education IRA") for beneficiaries under age 18. The contribution limit was phased out for taxpayers with modified AGI between $95,000 and $110,000 (between $150,000 and $160,000 for married couples filing a joint return). Contributions to an education IRA were not deductible, but earnings on contributions were allowed to accumulate tax-free. Distributions were excludable from gross income to the extent they did not exceed qualified higher education expenses incurred during the year the distribution was made. The earnings portion of a distribution not used to cover qualified higher education expenses was included in the gross income of the beneficiary and was generally subject to an additional 10-percent tax. If any portion of a distribution from an education savings account was excluded from gross income, an education tax credit could not be claimed with respect to the same student for the same taxable year. An excise tax of six percent was imposed on contributions to an education IRA in any year in which contributions were also made to a qualified State tuition program on behalf of the same beneficiary.

Effective for taxable years beginning after December 31, 2001 and before January 1, 2011, this Act increases the annual contribution limit to education IRAs to $2,000 and increases the contribution phase-out range for married couples filing a joint return to twice the range for single taxpayers ($190,000 to $220,000 of AGI). As under prior law, contributions to an education IRA are not deductible, but earnings on contributions are allowed to accumulate tax-free. In addition to allowing tax-free and penalty-free distributions for qualified higher education expenses, this Act expands education savings accounts to allow tax-free and penalty-free distributions for qualified elementary, secondary and after school expenses. Qualified expenses at public, private, and religious educational institutions providing elementary and secondary education generally include: tuition; fees; academic tutoring; special needs services; books; supplies; computer equipment; and certain expenses for room and board, uniforms, and transportation. Under this Act: (1) the rule prohibiting contributions after the beneficiary attains age 18 does not apply in the case of a special needs beneficiary, as defined by Treasury Department regulations, (2) both an education tax credit and a tax-free distribution from an education savings account are allowed with respect to the same student in the same taxable year, provided the credit and the distribution are not used for the same expenses, and (3) the excise tax on contributions made to an education IRA on behalf of a beneficiary during any taxable year in which contributions are made to a qualifying State tuition program on behalf of the same beneficiary is repealed.

Allow tax-free distributions from Qualified State Tuition Plans (QSTPs) for certain higher education expenses and allow private colleges to offer prepaid tuition plans.—QSTP programs generally take two forms - prepaid tuition plans and savings plans. Under a prepaid tuition plan, an individual may purchase tuition credits or certificates on behalf of a designated beneficiary, which entitle the beneficiary to the waiver or payment of qualified higher education expenses at participating educational institutions. Under a savings plan, an individual may make contributions to an account, which is established for the purpose of meeting the qualified higher education expenses of a designated beneficiary. Distributions from QSTPs for nonqualified expenses generally are subject to a more than de minimis penalty (typically 10 percent of the earnings portion of the distribution). There is no specific dollar cap on annual contributions to a QSTP; in addition, there is no limit on contributions to a QSTP based on the contributor's income. Contributions to a QSTP are permitted at any time during the beneficiary's lifetime and the account can remain open after the beneficiary reaches age 30. However, a QSTP must provide adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of amounts necessary to provide for qualified education expenses.

Two basic tax benefits were provided to contributions to, and beneficiaries of, QSTPs under prior law: (1) earnings on amounts invested in a QSTP were not subject to tax until a distribution was made (or educational benefits were provided), and (2) distributions made on behalf of a beneficiary were taxed at the beneficiary's (rather than the contributor's) individual income tax rate.

Effective for taxable years beginning after December 31, 2001 and before January 1, 2011, this Act provides for tax-free withdrawals from QSTPs for qualified higher education expenses, including tuition and fees; certain expenses for room and board; certain expenses for books, supplies, and equipment; and expenses of a special needs beneficiary that are necessary in connection with enrollment or attendance at an eligible education institution. An education tax credit, a tax-free distribution from an education savings account, and a tax-free distribution from a QSTP are allowed with respect to the same student in the same taxable year, provided the credit and the distributions are not used for the same expenses. Effective for taxable years beginning after December 31, 2003 and before January 1, 2011, this Act allows private educational institutions to establish qualified prepaid tuition plans (but not savings plans), provided the institution is eligible to participate in Federal financial aid programs under Title IV of the Higher Education Act of 1965. In addition, the prior law rule imposing a more than de minimis monetary penalty on any refund of earnings not used for qualified higher education expenses is repealed and replaced with an additional 10-percent tax on any payment includible in gross income; however, effective for taxable years beginning before January 1, 2004, the 10-percent tax does not apply to any distribution from a private prepaid tuition program that is includible in gross income but used for qualified higher education expenses.

Provide deduction for qualified higher education expenses.—An above-the-line deduction is provided for qualified higher education expenses, effective for expenses paid in taxable years beginning after December 31, 2001 and before January 1, 2006. Taxpayers with AGI less than or equal to $65,000 ($130,000 for married taxpayers filing a joint return) are provided a maximum deduction of $3,000 in taxable years 2002 and 2003, which increases to $4,000 in taxable years 2004 and 2005. Taxpayers with AGI greater than $65,000 and less than or equal to $80,000 (greater than $130,000 and less than or equal to $160,000 for married taxpayers filing a joint return) are provided a maximum deduction of $2,000 for taxable years 2004 and 2005. For a given taxable year, the deduction may not be claimed for the qualified education expenses of a student if an education tax credit is claimed for the same student. In addition, the deduction may not be claimed for amounts taken into account in determining the amount excludable from income due to a distribution from an education IRA or the amount of interest excludable from income with respect to education savings bonds. A taxpayer may not claim a deduction for the amount of a distribution from a qualified tuition plan that is excludable from income; however the deduction may be claimed for the amount of a distribution from a qualified tuition plan that is not attributable to earnings.

Extend and expand exclusion for employer-provided educational assistance.—Certain amounts paid or incurred by an employer for educational assistance provided to an employee are excluded from the employee's gross income for income and payroll tax purposes. The exclusion is limited to $5,250 of educational assistance with respect to an individual during a calendar year and applies whether or not the education is job-related. The exclusion, which applied to undergraduate courses beginning before January 1, 2002 under prior law, is extended to apply to courses beginning after December 31, 2001 and before January 1, 2011, and is expanded to apply to graduate courses.

Modify student loan interest deduction.—Prior law allowed certain individuals to claim an above-the-line deduction for up to $2,500 in annual interest paid on qualified education loans, during the first 60 months in which interest payments were required. The maximum annual interest deduction was phased out ratably for single taxpayers with AGI between $40,000 and $55,000 ($60,000 and $75,000 for married taxpayers filing a joint return). The deduction did not apply to voluntary payments, such as interest payments made during a period of loan forbearance. Effective for interest paid on qualified education loans after December 31, 2001 and before January 1, 2011, both the limit on the number of months during which interest paid is deductible and the restriction that voluntary payments of interest are not deductible are repealed. In addition, the income phase-out ranges for eligibility for the deduction are increased to between $50,000 and $65,000 of AGI for a single taxpayer ($100,000 and $130,000 for married taxpayers filing a joint return). The income phase-out ranges are adjusted annually for inflation after 2002.

Provide tax relief for awards under certain health education programs.—Current law provides tax-free treatment for certain scholarship and fellowship grants used to pay qualified tuition and related expenses, but not to the extent that any grant represents compensation for services. Under this Act, amounts received by an individual under the National Health Service Corps Scholarship Program or the Armed Forces Health Professions Scholarship and Financial Assistance Program may be "qualified scholarships" excludable from income, without regard to the recipient's future service obligation. This change is effective for awards received after December 31, 2001 and before January 1, 2011.

Modify arbitrage restrictions on tax-exempt bonds issued by small governmental units for public schools.—To prevent tax exempt entities from issuing more Federally subsidized tax-exempt bonds than is necessary for the activity being financed, current law includes arbitrage restrictions limiting the ability to profit from investment of tax-exempt bond proceeds. In general, arbitrage profits may be earned only during specified periods or on specified types of investments, and, subject to limited exceptions, must be rebated to the Federal Government. Under prior law, governmental bonds issued by small governmental units were not subject to the rebate. Small governmental units are defined as general purpose governmental units that issue no more than $5 million of tax-exempt governmental bonds in a calendar year ($10 million of governmental bonds if at least $5 million of the bonds are used to finance public schools). Effective for bonds issued after December 31, 2001 and before January 1, 2011, this Act increases to $15 million the maximum amount of governmental bonds that small governmental units may issue without being subject to the arbitrage rebate requirements, if at least $10 million of the bonds are used for public schools.

Allow States to issue tax-exempt private activity bonds for school construction.—Effective for taxable years beginning after December 31, 2001 and before January 1, 2011, the activities for which States may issue tax-exempt private activity bonds is expanded to include the construction and equipping of public school facilities owned by private, for-profit corporations pursuant to public-private partnership agreements with a State or local educational agency. Under such agreements the for-profit corporation constructs, rehabilitates, refurbishes or equips the school facility, which must be operated by a public educational agency as part of a system of public schools; ownership reverts to the public agency when the bonds are retired. Issuance of these bonds is subject to an annual per-State volume limit of $10 per resident (a minimum of $5 million is provided for small States); this is in addition to the present-law private activity bond per-State volume limit equal to the greater of $75 per resident or $225 million in 2002, and indexed annually thereafter.

Estate, Gift, and Generation-Skipping Transfer Tax Provisions

Phase out and repeal estate and generation-skipping transfer taxes, and reduce gift tax rates.—Under prior law, the unified estate and gift tax rates on taxable transfers began at 18 percent on the first $10,000 of cumulative taxable transfers and reached 55 percent on cumulative transfers in excess of $3 million. A five-percent surtax (which phased out the benefit of the graduated rates and increased the top marginal tax rate to 60 percent) was imposed on cumulative transfers between $10 million and $17,184,000. A generation-skipping transfer tax was imposed on transfers made either directly or through a trust or similar arrangement to a beneficiary in a generation more than one generation below that of the transferor (a "skip person"). Cumulative generation-skipping transfers in excess of $1 million (adjusted annually for inflation after 1997) were taxed at the top estate and gift tax rate of 55 percent.

Under this Act, estate, gift, and generation-skipping transfer tax rates are reduced for decedents dying and gifts made after December 31, 2001 and before January 1, 2010. Estate and generation-skipping transfer taxes are repealed for decedents dying after December 31, 2009 and before January 1, 2011, while the maximum tax rate on gifts made after December 31, 2009 and before January 1, 2011 is reduced to 35 percent on gifts in excess of a lifetime exclusion of $1 million (see discussion of unified credit below). The reduction in tax rates begins in 2002 with the repeal of the five-percent surtax and the reduction of the 53 percent and 55 percent rates to 50 percent. The maximum tax rate on estates, gifts, and generation-skipping transfers is reduced from 50 percent in 2002 to 49 percent in 2003, 48 percent in 2004, 47 percent in 2005, 46 percent in 2006, and 45 percent in 2007 through 2009.

Increase unified credit exemption amount.—Under prior law, the unified credit applicable to cumulative taxable transfers by gift and at death effectively exempted from tax transfers totaling $675,000 in 2001, $700,000 in 2002 and 2003, $850,000 in 2004, $950,000 in 2005 and $1 million in 2006 and subsequent years. The tax on generation-skipping transfers applied only to cumulative transfers in excess of $1 million, adjusted annually for inflation after 1997 ($1,060,000 in 2001). This Act increases the unified credit effective exemption amount for estate and gift tax purposes to $1 million in 2002. The effective exemption amount for gift tax purposes will remain at $1 million; however, the effective exemption amount for estate and generation-skipping transfer tax purposes will increase to $1.5 million in 2004 and 2005, $2.0 million in 2006 through 2008, and $3.5 million in 2009.

Reduce and modify allowance for State death taxes paid.—A credit against the Federal estate tax for any estate, inheritance, legacy, or succession taxes actually paid to any State or the District of Columbia with respect to any property included in the decedent's gross estate, was provided under prior law. The allowable credit was limited to the lesser of the tax paid or a percentage of the decedent's adjusted taxable estate (ranging from 0.8 percent of adjusted taxable estate between $40,000 and $90,000, up to 16 percent of adjusted taxable estate in excess of $10,040,000). This Act reduces the credit rates by 25 percent in 2002, 50 percent in 2003, and 75 percent in 2004. For 2005 through 2009, the credit is replaced by a deduction for taxes paid.

Modify basis of property received.—Under prior law, the basis of property passing from a decedent's estate generally was the fair market value of the property on the date of the decedent's death. This step up (or step down) in basis eliminated the recognition of income on any appreciation of the property that occurred prior to the decedent's death, and had the effect of eliminating the tax benefit from any unrealized loss. Effective for decedent's dying after December 31, 2009 and before January 1, 2011, the basis of property passing from a decedent's estate will be the lesser of the adjusted basis of the decedent or the fair market value of the property on the date of the decedent's death. Each decedent's estate generally is permitted to increase the basis of assets transferred by up to a total of $1.3 million for assets passing to any heir plus an additional $3 million for property transferred to a surviving spouse. Nonresidents who are not U.S. citizens are allowed to increase the basis of property by up to $60,000. Each estate is also allowed additional basis equal to the decedent's unused capital loss and net operating loss carryforwards and built-in capital losses.

Modify other provisions affecting estate, gift, and generation-skipping transfer taxes.—Other modifications provided in this Act: (1) expand the estate tax exclusion for qualified conservation easements, (2) change the generation-skipping transfer tax rules to ensure that a taxpayer does not inadvertently lose the benefit of the generation-skipping transfer tax exemption, and (3) expand eligibility for the payment of estate and gift taxes in installments.

Pension and Retirement Provisions

Increase contributions to Individual Retirement Accounts (IRAs).—There are two types of IRAs under present law - Roth IRAs and traditional IRAs. Individuals with AGI below certain thresholds may make nondeductible contributions to a Roth IRA (deductible contributions are not allowed). The maximum allowable annual contribution to a Roth IRA is phased out for single taxpayers with AGI between $95,000 and $110,000 (between $150,000 and $160,000 for married taxpayers filing a joint return). Account earnings are not includible in income, and qualified distributions from a Roth IRA are tax-free. Both deductible and nondeductible contributions may be made to a traditional IRA. Contributions to a traditional IRA are deductible if neither the individual nor the individual's spouse is an active participant in an employer-sponsored retirement plan. If the individual is an active participant in an employer-sponsored retirement plan, the deduction limit is phased out between $34,000 and $44,000 of AGI for single taxpayers (between $54,000 and $64,000 of AGI for married taxpayers filing a joint return). If the individual is not an active participant in an employer-sponsored retirement plan but the individual's spouse is an active participant, the deduction limit is phased out between $150,000 and $160,000 of AGI. All taxpayers may make nondeductible contributions to a traditional IRA, regardless of income. Account earnings from IRAs are not includible in income when earned. However, distributions from traditional IRAs are includible in income, except to the extent they are a return of nondeductible contributions.

Under prior law, the maximum annual contribution to an IRA was the lesser of $2,000 or the individual's compensation. In the case of married taxpayers filing a joint return, annual contributions of up to $2,000 were allowed for each spouse, provided the combined compensation of the spouses was at least equal to the contributed amount. This Act increases the maximum annual contribution to an IRA to $3,000 for taxable years 2002 through 2004, $4,000 for taxable years 2005 through 2007, and $5,000 for taxable year 2008. For taxable years 2009 and 2010, the limit is adjusted annually for inflation in $500 increments. Effective for taxable years beginning after December 31, 2001, individuals who attain age 50 before the end of the year may make additional catch-up contributions to an IRA. For these individuals, the otherwise maximum contribution limit (before application of the AGI phase-out limits) is increased by $500 for taxable years 2002 through 2005 and by $1,000 for taxable years 2006 through 2010.

Increase contribution and benefit limits under qualified pension plans.—Limits on contributions and benefits under qualified pension plans are based on the type of plan. Under prior law, annual additions to a defined contribution plan with respect to each plan participant were limited to the lesser of (1) 25 percent of compensation or (2) $35,000 (for 2001), adjusted for inflation in $5,000 increments. Under prior law, the maximum annual benefit payable at an individual's social security retirement age under a defined benefit plan was generally the lesser of (1) 100 percent of average compensation, or (2) $140,000 (for 2001), adjusted for inflation in $5,000 increments. The annual compensation of each participant that could be taken into account for purposes of determining contributions and benefits under a plan generally was limited to $170,000 (for 2001), adjusted for inflation in $10,000 increments. Maximum annual elective deferrals that an individual was allowed to make to a qualified cash or deferred arrangement (401(k) plan), a tax-sheltered annuity (section 403(b) annuity), or a salary reduction simplified employee pension plan (SEP) under prior law were limited to $10,500 (for 2001), adjusted for inflation in increments of $500. The maximum amount of annual elective deferrals that an individual was allowed to make to a savings incentive match plan (SIMPLE plan) under prior law was $6,500 (for 2001), adjusted for inflation in increments of $500. Under prior law the maximum annual deferral under an eligible deferred compensation plan of a State or local government or a tax-exempt organization (a section 457 plan) was the lesser of (1) $8,500 (for 2001), adjusted for inflation in increments of $500, or (2) 33 1/3 percent of compensation. In the three years prior to retirement, the limit on contributions to an eligible section 457 plan is generally increased to twice the otherwise applicable dollar limit.

Effective for taxable years beginning after December 31, 2001, the contribution limit to a defined contribution plan is increased to the lesser of 100 percent of compensation or $40,000 (adjusted annually for inflation in $1,000 increments after 2002). Effective for taxable years ending after December 31, 2001, the benefit limit for defined benefit plans is increased to $160,000 (adjusted annually for inflation for plans ending after December 31, 2002, in increments of $1,000) and calculated as a benefit payable at age 62. The compensation that may be taken into account under a plan is increased to $200,000 in 2002 (indexed annually thereafter in $5,000 increments). The dollar limit on annual elective deferrals under section 401(k) plans, section 403(b) annuities and salary reduction SEPs is increased to $11,000 in 2002, and increased annually thereafter in $1,000 increments, reaching $15,000 in 2006 (adjusted annually for inflation in increments of $500 after 2006). The dollar limit on annual elective deferrals to a SIMPLE plan is increased to $7,000 in 2002, and increased annually thereafter in $1,000 increments, reaching $10,000 in 2005 (adjusted for inflation in increments of $500 after 2006). The dollar limit on contributions to an eligible section 457 plan is increased to the lesser of (1) 100 percent of includable compensation or (2) $11,000 in 2002, $12,000 in 2003, $13,000 in 2004, $14,000 in 2005, and $15,000 in 2006 (adjusted for inflation in increments of $500 after 2006).

Permit catch-up contributions to certain salary reduction arrangements.—Effective for taxable years beginning after December 31, 2001, the otherwise applicable dollar limit on elective deferrals under a section 401(k) plan, section 403(b) annuity, SEP or SIMPLE plan, or deferrals under a section 457 plan is increased for individuals who attain age 50 by the end of the year. The additional amount of elective contributions that is permitted to be made by an eligible individual participating in such a plan is the lesser of: (1) the applicable dollar amount or (2) the participant's compensation for the year after reduction by any other elective deferrals of the participant for the year. The applicable dollar amount under a 401(k) plan, section 403(b) plan, SEP, or section 457 plan is $1,000 for 2002, $2,000 for 2003, $3,000 for 2004, $4,000 for 2005, and $5,000 for 2006 through 2010 (adjusted annually for inflation in $500 increments beginning in 2007). The applicable dollar amount under a SIMPLE plan is $500 for 2002, $1,000 for 2003, $1,500 for 2004, $2,000 for 2005, and $2,500 for 2006 through 2010 (adjusted annually for inflation in $500 increments beginning in 2007).

Provide a nonrefundable tax credit to certain individuals for elective deferrals and IRA contributions.—For taxable years beginning after December 31, 2001 and before January 1, 2007, a nonrefundable tax credit is provided for up to $2,000 in contributions made by eligible taxpayers to a qualified plan or to a traditional or Roth IRA. The credit, which is in addition to any deduction or exclusion that would otherwise apply with respect to the contribution, is available to single taxpayers with AGI less than or equal to $25,000 ($37,500 for heads of household and $50,000 for married taxpayers filing a joint return). The credit is available to individuals who are 18 years of age or older (other than individuals who are full-time students or claimed as a dependent on another taxpayer's return) and is offset against both the regular and alternative minimum tax. The credit rate is 50 percent for single taxpayers with AGI less than or equal to $15,000 ($30,000 for married taxpayers filing a joint return and $22,500 for heads of household), 20 percent for single taxpayers with AGI between $15,000 and $16,250 (between $30,000 and $32,500 for married taxpayers filing a joint return and between $22,500 and $24,375 for heads of household), and 10 percent for single taxpayers with AGI between $16,250 and $25,000 (between $32,500 and $50,000 for married taxpayers filing a joint return and between $24,375 and $37,500 for heads of household).

Provide tax credit for new retirement plan expenses of small businesses.—Effective for taxable years beginning after December 31, 2001, a nonrefundable tax credit is provided for qualified administrative and retirement-education expenses incurred by a small business (an employer that did not employ, in the preceding year, more than 100 employees with compensation in excess of $5,000) that adopts a new qualified defined benefit or defined contribution plan (including a section 401(k) plan), SIMPLE plan, or SEP. The credit applies to 50 percent of the first $1,000 in qualifying expenses for the plan for each of the first three years of the plan. The 50 percent of qualifying expenses offset by the credit are not deductible; the other 50 percent of qualifying expenses (and other expenses) are deductible as under prior law.

Modify other pension and retirement provisions.—In addition to the provisions described above, this Act expands coverage in pension and retirement plans through provisions that: (1) require accelerated vesting for matching employer contributions, (2) modify the definition of key employee, (3) eliminate IRS user fees for certain determination letter requests regarding employer plans, (4) modify the application of the deduction limitation with regard to elective deferral contributions, (5) repeal the rules coordinating contributions to eligible section 457 plans with contributions under other types of plans, (6) increase the annual limitation on the amount of deductible contributions made by an employer to a profit-sharing or stock bonus plan, (7) modify the definition of compensation for purposes of the deduction rules, (8) provide the option to treat elective deferrals as after-tax contributions, (9) improve notice to employees for pension amendments reducing future accruals, (10) increase portability, (11) strengthen pension security and enforcement, and (12) reduce regulatory burdens.

Other Provisions

Provide minimum tax relief to individuals.—An alternative minimum tax is imposed on individuals to the extent that the tentative minimum tax exceeds the regular tax. An individual's tentative minimum tax generally is equal to the sum of: (1) 26 percent of the first $175,000 ($87,500 in the case of a married individual filing a separate return) of alternative minimum taxable income (taxable income modified to take account of specified preferences and adjustments) in excess of an exemption amount and (2) 28 percent of the remaining alternative minimum taxable income. The AMT exemption amounts under prior law were: (1) $45,000 for married taxpayers filing a joint return and surviving spouses; (2) $33,750 for single taxpayers, and (3) $22,500 for married taxpayers filing a separate return, estates and trusts. The exemption amounts are phased out by an amount equal to 25 percent of the amount by which the individual's alternative minimum taxable income exceeds: (1) $150,000 for married taxpayers filing a joint return and surviving spouses, (2) $112,500 for single taxpayers, and (3) $75,000 for married taxpayers filing a separate return, estates and trusts. The exemption amounts, the threshold phase-out amounts, and the rate brackets are not indexed for inflation. Effective for taxable years beginning after December 31, 2001 and before January 1, 2005, the exemption amount is increased to $49,000 for married taxpayers filing a joint return and surviving spouses, $35,750 for single taxpayers, and $24,500 for married taxpayers filing a separate return, estates and trusts.

Modify the timing of estimated tax payments by corporations.—Corporations generally are required to pay their income tax liability in quarterly estimated payments. For corporations that keep their accounts on a calendar year basis, these payments are due on or before April 15, June 15, September 15 and December 15 (if these dates fall on a holiday or weekend, payment is due on the next business day). This Act allowed corporations to delay the estimated payment otherwise due on September 17, 2001 until October 1, 2001; 20 percent of the estimated tax payment otherwise due on September 15, 2004 may be delayed until October 1, 2004.

VICTIMS OF TERRORISM TAX RELIEF ACT OF 2001

This Act provides income and estate tax relief to the survivors of victims of (1) the September 11, 2001 terrorist attacks on the United States, (2) the April 19, 1995 Oklahoma City bombing, and (3) exposure to anthrax on or after September 11, 2001 and before January 1, 2002. General relief is also provided for victims of disasters and terrorist actions. The tax relief provided in this Act does not apply to any individual identified by the Attorney General to have been a participant or conspirator in the terrorist attack or attacks to which a specific provision applies, or a representative of such individual. The major provisions of this Act are described below.

Provide individual income tax relief to victims of terrorist attacks.—Under current law an individual in active service as a member of the Armed Forces who dies while serving in a combat zone is not subject to income tax for the year of death (as well as for any prior taxable year ending on or after the first day the individual served in the combat zone). In addition, military and civilian employees of the United States are exempt from income taxes if they die as a result of wounds or injury incurred outside the United States in terrorist or military action. This exemption is available for the year of death and for prior taxable years beginning with the taxable year prior to the taxable year in which the wounds or injury were incurred. This Act extends relief similar to the present-law treatment of military or civilian employees of the United States who die as a result of terrorist or military activity outside the United States to individuals who die from wounds or injury incurred as a result of: (1) the terrorist attacks on September 11, 2001 or April 19, 1995, or (2) exposure to anthrax on or after September 11, 2001 and before January 1, 2002. These individuals (whether killed as a result of an attack or in rescue or recovery operations) generally are exempt from income tax for the year of death and for prior taxable years beginning with the taxable year prior to the taxable year in which the wounds or injury occurred. A minimum tax relief benefit of $10,000 will be provided to each eligible individual regardless of the income tax liability incurred during the eligible tax years.

Exclude certain death benefits from gross income.—In general, gross income includes income from whatever source derived, including payments made as a result of the death of an individual. Under this Act, amounts paid by an employer by reason of the death of an employee attributable to wounds or injury incurred as a result of the terrorist attacks on September 11, 2001 or April 19, 1995, or exposure to anthrax on or after September 11, 2001 and before January 1, 2002, are excluded from gross income. Subject to rules prescribed by the Secretary of the Treasury, the exclusion does not apply to amounts that would have been payable if the individual had died for a reason other than the specified attacks.

Provide a reduction in Federal estate taxes.—Under current law a reduction in Federal estate taxes is provided for taxable estates of U.S. citizens or residents who are active members of the U.S. Armed Forces and who are killed in action while serving in a combat zone. This estate tax reduction also applies to active service members who die as a result of wounds, disease, or injury suffered while serving in a combat zone by reason of a hazard to which the service member was subjected as an incident of such service. This Act simplifies the estate tax relief provided for combat-related deaths and generally treats individuals who die from wounds or injury incurred as a result of the terrorist attacks that occurred on September 11, 2001 and April 19, 1995, or as a result of exposure to anthrax on or after September 11, 2001 and before January 1, 2002, in the same manner as if they were active members of the U.S. Armed Forces killed in action while serving in a combat zone or dying as a result of wounds or injury suffered while serving in a combat zone. The executor of an estate eligible for the reduction may elect not to have the reduction apply if more favorable tax treatment would be available under generally applicable rules. The reduction effectively shields the first $8.8 million of a victim's estate from Federal estate taxes and reduces estate tax rates.

Treat payments by charitable organizations as exempt payments.—Under current law, charitable organizations generally are exempt from taxation. Such organizations must be organized and operated exclusively for exempt purposes and no part of the net earnings of such organizations may inure to the benefit of any private shareholder or individual. Such organizations must serve a public rather than a private interest and generally must serve a charitable class of persons that is indefinite or of sufficient size. Under this Act, charitable organizations that make payments on or after September 11, 2001 by reason of the death, injury, wounding, or illness of an individual incurred as a result of the September 11, 2001 attacks, or as a result of exposure to anthrax occurring on or after September 11, 2001 and before January 1, 2002, are not required to make a specific assessment of need for the payments to be related to the purpose or function constituting the basis for the organization's exemption. This rule applies provided that the organization makes the payments in good faith using a reasonable and objective formula that is consistently applied. Such payments must be for public and not private benefit and must serve a charitable class. Similarly, if a tax-exempt private foundation makes payments under the conditions described above, the payment will not be subject to excise taxes on self-dealing, even if made to a person who is otherwise disqualified under current law.

Provide exclusion for certain cancellations of indebtedness.—Gross income generally includes income that is realized by a debtor from the discharge of indebtedness, subject to certain exceptions for debtors in Title 11 bankruptcy cases, insolvent debtors, certain farm indebtedness, and certain real property business indebtedness. Under this Act, an exclusion from gross income is provided for any amount realized from the discharge (in whole or in part) of indebtedness if the indebtedness is discharged by reason of the death of an individual incurred as a result of the September 11, 2001 terrorist attacks, or as a result of anthrax exposure occurring on or after September 11, 2001 and before January 1, 2002. This exclusion applies to discharges made on or after September 11, 2001 and before January 1, 2002.

Provide general tax relief for victims of terrorist/military actions, Presidentially-declared disasters, and certain other disasters.—This Act also: (1) clarifies that payments of compensation made under the Air Transportation Safety and System Stabilization Act are excludable from gross income, (2) provides a specific exclusion from gross income for "qualified disaster relief payments," (3) expands the authority of the Secretary of the Treasury to prescribe regulations concerning deadlines for performing various acts under the Internal Revenue Code and the waiver of interest on underpayments of tax liability, (4) expands the present-law exclusion from gross income for disability income of U.S. civilian employees attributable to a terrorist attack outside the United States to apply to disability income received by any individual attributable to a terrorist or military action, (5) extends the income tax relief provided under current law to U.S. military and civilian personnel who die as a result of terrorist or military activity outside the United States to such personnel regardless of where the terrorist or military action occurs, (6) modifies the tax treatment of structured settlement arrangements, (7) modifies the personal exemption deduction for certain disability trusts, and (8) expands the availability of returns and return information for purposes of investigating terrorist incidents, threats, or activities, and for analyzing intelligence concerning terrorist incidents, threats, or activities.

RAILROAD RETIREMENT AND SURVIVORS' IMPROVEMENT ACT OF 2001

The Federally administered railroad retirement system is a two-tier system consisting of social security equivalent benefits (frequently referred to as Tier I benefits) and a rail industry pension plan (frequently referred to as Tier II benefits). This Act modernizes the financing of the railroad retirement system and provides enhanced benefits to retirees and survivors. Under prior law, the Tier II payroll tax levied on the annual taxable wage base of rail industry employees was 16.1 percent for employers and 4.9 percent for employees. This Act reduces the rate for employers to 15.6 percent in 2002 and to 14.2 percent in 2003. Starting in 2004, the rates are adjusted annually and linked to the level of Tier II reserves. Under current estimates, those rates are expected to be 13.1 percent for employers and 4.9 percent for employees; the rates necessary to maintain reserves at a level sufficient to fund benefits for four years. If the reserve fund falls below the level sufficient to fund four years of benefits or increases to a level sufficient to fund more than six years of benefits, then payroll tax rates would change according to a schedule set in the Act. The rate on employers can vary between 8.2 percent and 22.1 percent, while the rate on employees can vary between zero and 4.9 percent.

INVESTOR AND CAPITAL MARKETS FEE RELIEF ACT

The Securities and Exchange Commission (SEC) collects fees for registrations, mergers, and transactions of securities. Under prior law, some of these fees were classified as receipts and others were classified as offsetting collections (outlays). The specific fees collected included the following: (1) Transaction fees equal to 1/300th of a percent (1/800th of a percent beginning in 2008) of the aggregate dollars traded through national securities exchanges, national securities associations, brokers, and dealers. (2) Registration fees equal to $200 per $1 million ($67 per $1 million beginning in 2007) of the maximum aggregate price for securities that are proposed to be offered. Additional registration fees (subject to appropriation) equal to $39 per $1 million for 2002 ($28 for 2003, $9 for 2004, $5 for 2005 and zero for 2006 and subsequent years) of the aggregate price for securities proposed to be offered. (3) Merger fees equal to $200 per $1 million of the value of securities proposed to be purchased as part of a merger. (4) Assessments on transactions of single stock futures equal to $.02 per transaction ($.0075 per transaction beginning in 2007).

This Act reclassifies all of these fees as offsetting collections (outlays) and adjusts the fee rates as follows: (1) Transaction fees are reduced to $15 per $1 million of the aggregate dollars traded. For 2003 and each subsequent year, the SEC is required to establish a rate that would generate transaction fee collections equal to a target amount for that year. (2) Registration fees are reduced to $92 per $1 million of the maximum aggregate price for securities that are proposed to be offered. For 2003 and each subsequent year, the SEC is required to establish a fee rate that would generate collections equal to a target amount. (3) Merger fees are reduced to $92 per $1 million of the value of securities proposed to be purchased as part of a merger. For 2003 and each subsequent year, these fees would be equal to the rate for registration fees. (4) Assessments on transactions of single stock futures would be reduced to $0.009 per transaction for 2002 through 2006 and then fall to $0.0042 per transaction for 2007 and subsequent years.

ADMINISTRATION PROPOSALS

The President's plan provides tax incentives for charitable giving, education, the disabled, health care, farmers, and the environment. It also provides tax incentives designed to increase domestic production of oil and gas and promote energy conservation, extends for two years provisions that expired in 2001, permanently extends the research and experimentation (R&E) tax credit, and permanently extends the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 that sunset on December 31, 2010. In addition, the President intends to work with the Congress in a bipartisan manner to enact an economic security plan that will provide an immediate and effective stimulus to the Nation's economy. In addition, the Treasury Department will be conducting a thorough review of means of simplifying the tax code. The Administration intends to work with Congress, tax practitioners, tax administrators, and taxpayers to produce meaningful simplification. An introduction to these efforts is contained at the end of this Chapter.

BIPARTISAN ECONOMIC SECURITY PLAN

The President believes that it is crucial for Congress to quickly pass an economic security bill that will reinvigorate economic growth and assist workers affected by the economic downturn that has followed the terrorist attacks of September 11, 2001. To prevent further job losses and help displaced workers get back to work quickly, the Administration will continue to work with Congress in a bipartisan manner to enact an economic stimulus package and a worker assistance package to provide additional temporary, quick, and effective help for those who have lost their jobs

TAX INCENTIVES

Provide Incentives for Charitable Giving

Provide charitable contribution deduction for nonitemizers.—Under current law, individual taxpayers who do not itemize their deductions (nonitemizers) are not able to deduct contributions to qualified charitable organizations. The Administration proposes to allow nonitemizers to deduct charitable contributions in addition to claiming the standard deduction, effective for taxable years beginning after December 31, 2001. The deduction would be phased in between 2002 and 2012, as follows: (1) Single taxpayers would be allowed a maximum deduction of $100 in 2002 through 2004, $300 in 2005 through 2011, and $500 in 2012 and subsequent years. (2) Married taxpayers filing a joint return would be allowed a maximum deduction of $200 in 2002 through 2004, $600 in 2005 through 2011, and $1,000 in 2012 and subsequent years. Deductible contributions would be subject to existing rules governing itemized charitable contributions, such as the substantiation requirements and the percentage-of-AGI limitations.

Permit tax-free withdrawals from IRAs for charitable contributions.—Under current law, eligible individuals may make deductible or non-deductible contributions to a traditional IRA. Pre-tax contributions and earnings in a traditional IRA are included in income when withdrawn. Effective for distributions after December 31, 2001, the Administration proposes to allow individuals who have attained age 59½ to exclude from gross income IRA distributions made directly to a charitable organization. The exclusion would apply without regard to the percentage-of-AGI limitations that apply to deductible charitable contributions. The exclusion would apply only to the extent the individual receives no return benefit in exchange for the transfer, and no charitable deduction would be allowed with respect to any amount that is excludable from income under this provision.

Raise the cap on corporate charitable contributions.—Current law limits deductible charitable contributions by corporations to 10 percent of net income (calculated before the deduction of the charitable contributions and certain other deductions). The Administration proposes to increase the limit on deductible charitable contributions by corporations from 10 percent to 15 percent of net income, effective for taxable years beginning after December 31, 2001.

Expand and increase the enhanced charitable deduction for contributions of food inventory.—A taxpayer's deduction for charitable contributions of inventory generally is limited to the taxpayer's basis (typically cost) in the inventory. However, for certain contributions of inventory, C corporations may claim an enhanced deduction equal to the lesser of: (1) basis plus one half of the fair market value in excess of basis, or (2) two times basis. To be eligible for the enhanced deduction, the contributed property generally must be inventory of the taxpayer, contributed to a charitable organization, and the donee must (1) use the property consistent with the donee's exempt purpose solely for the care of the ill, the needy, or infants, (2) not transfer the property in exchange for money, other property, or services, and (3) provide the taxpayer a written statement that the donee's use of the property will be consistent with such requirements. To use the enhanced deduction, the taxpayer must establish that the fair market value of the donated item exceeds basis.

Under the Administration's proposal, which is designed to encourage contributions of food inventory to charitable organizations, any taxpayer engaged in a trade or business would be eligible to claim an enhanced deduction for donations of food inventory. The enhanced deduction for donations of food inventory would be increased to the lesser of: (1) fair market value, or (2) two times basis. However, to ensure consistent treatment of all businesses claiming an enhanced deduction for donations of food inventory, the enhanced deduction for qualified food donations by S corporations and non-corporate taxpayers would be limited to 15 percent of net income from the trade or business. A special provision would allow taxpayers with a zero or low basis in the qualified food donation (e.g., taxpayers that use the cash method of accounting for purchases and sales, and taxpayers that are not required to capitalize indirect costs) to assume a basis equal to 25 percent of fair market value. The enhanced deduction would be available only for donations of "apparently wholesome food" (food intended for human consumption that meets all quality and labeling standards imposed by Federal, State, and local laws and regulations, even though the food may not be readily marketable due to appearance, age, freshness, grade, size, surplus, or other conditions). The fair market value of "apparently wholesome food" that cannot or will not be sold solely due to internal standards of the taxpayer or lack of market, would be determined by taking into account the price at which the same or substantially the same food items are sold by the taxpayer at the time of the contribution or, if not sold at such time, in the recent past. These proposed changes in the enhanced deduction for donations of food inventory would be effective for taxable years beginning after December 31, 2001.

Reform excise tax based on investment income of private foundations.—Under current law, private foundations that are exempt from Federal income tax are subject to a two-percent excise tax on their net investment income (one-percent if certain requirements are met). The tax on private foundations that are not exempt from Federal income tax, such as certain charitable trusts, is equal to the excess of the sum of the excise tax that would have been imposed if the foundation were tax exempt and the amount of the unrelated business income tax that would have been imposed if the foundation were tax exempt, over the income tax imposed on the foundation. To encourage increased charitable activity and simplify the tax laws, the Administration proposes to replace the two rates of tax on the net investment income of private foundations that are exempt from Federal income tax with a single tax rate of one percent. The tax on private foundations not exempt from Federal income tax would be equal to the excess of the sum of the one-percent excise tax that would have been imposed if the foundation were tax exempt and the amount of the unrelated business income tax what would have been imposed if the foundation were tax exempt, over the income tax imposed on the foundation. The proposed change would be effective for taxable years beginning after December 31, 2001.

Modify tax on unrelated business taxable income of charitable remainder trusts.—A charitable remainder annuity trust is a trust that is required to pay, at least annually, a fixed dollar amount of at least five percent of the initial value of the trust to a non-charity for the life of an individual or for a period of 20 years or less, with the remainder passing to charity. A charitable remainder unitrust is a trust that generally is required to pay, at least annually, a fixed percentage of at least five percent of the fair market value of the trust's assets determined at least annually to a non-charity for the life of an individual or for a period of 20 years or less, with the remainder passing to charity. A trust does not qualify as a charitable remainder annuity if the annuity for a year is greater than 50 percent of the initial fair market value of the trust's assets. A trust does not qualify as a charitable remainder unitrust if the percentage of assets that are required to be distributed at least annually is greater than 50 percent. A trust does not qualify as a charitable remainder annuity trust or a charitable remainder unitrust unless the value of the remainder interest in the trust is at least 10 percent of the value of the assets contributed to the trust. Distributions from a charitable remainder annuity trust or charitable remainder unitrust, which are included in the income of the beneficiary for the year that the amount is required to be distributed, are treated in the following order as: (1) ordinary income to the extent of the trust's current and previously undistributed ordinary income for the trust's year in which the distribution occurred, (2) capital gains to the extent of the trust's current capital gain and previously undistributed capital gain for the trust's year in which the distribution occurred, (3) other income to the extent of the trust's current and previously undistributed other income for the trust's year in which the distribution occurred, and (4) corpus (trust principal).

Charitable remainder annuity trusts and charitable remainder unitrusts are exempt from Federal income tax; however, such trusts lose their income tax exemption for any year in which they have unrelated business taxable income. Any taxes imposed on the trust are required to be allocated to trust corpus. The Administration proposes to levy a 100-percent excise tax on the unrelated business taxable income of charitable remainder trusts, in lieu of removing the Federal income tax exemption for any year in which unrelated business taxable income is incurred. This change, which is a more appropriate remedy than loss of tax exemption, is proposed to become effective for taxable years beginning after December 31, 2001, regardless of when the trust was created.

Modify basis adjustment to stock of S corporations contributing appreciated property.—Under current law, each shareholder in an S corporation separately accounts for his/her pro rata share of the S corporation's charitable contributions in determining his/her income tax liability. A shareholder's basis in the stock of the S corporation must be reduced by the amount of his/her pro-rata share of the S corporation's charitable contribution. In order to preserve the benefit of providing a charitable contribution deduction for contributions of appreciated property and to prevent the recognition of gain on the contributed property on the disposition of the S corporation stock, the Administration proposes to allow a shareholder in an S corporation to increase his/her basis in the stock of an S corporation by an amount equal to the excess of the shareholder's pro rata share of the S corporation's charitable contribution over the stockholder's pro rata share of the adjusted basis of the contributed property. The proposal would be effective for taxable years beginning after December 31, 2001.

Allow expedited consideration of applications for exempt status.—The Administration proposes to allow expedited consideration of applications for exempt status by organizations formed for the primary purpose of providing social services to the poor and the needy. To be eligible, the organization must have applied for a grant under a Federal, State, or local program that provides funding for social service programs on or before the day that the organization applies to the Secretary of the Treasury for determination of its exempt status. Organizations that demonstrate that under the terms of the grant program exempt status is required before the organization is eligible to apply for a grant would also qualify for expedited consideration. Each organization would be required to include with its application for exempt status a copy of its completed grant application. The proposal would be effective for taxable years beginning after December 31, 2001.

Strengthen and Reform Education

Provide refundable tax credit for certain costs of attending a different school for pupils assigned to failing public schools.—Under the Administration's proposal, a refundable tax credit would be allowed for 50 percent of the first $5,000 of qualifying elementary and secondary education expenses incurred during the taxable year with respect to enrollment of a qualifying student in a qualifying school. Qualifying students would be those who, for a given school year, would normally attend a public school determined by the State as not having made "adequate yearly progress" under the terms of the Elementary and Secondary Education Act as amended by the No Child Left Behind Act of 2001. A qualifying student in one school year generally would qualify for an additional school year even if the school normally attended made adequate yearly progress by the beginning of the second school year. A qualifying school would be any public school making adequate yearly progress or private elementary or secondary school. Qualifying expenses generally would be tuition, required fees, and transportation costs incurred by the taxpayer in connection with the attendance at a qualifying school. The proposal would be effective with respect to expenses incurred beginning with the 2002–2003 school year through the 2006–2007 school year.

Allow teachers to deduct out-of-pocket classroom expenses.—Under current law, teachers who incur unreimbursed, job-related expenses may deduct those expenses to the extent that when combined with other miscellaneous itemized deductions they exceed 2 percent of AGI, but only if the teacher itemizes deductions (i.e., does not use the standard deduction). Effective for expenses incurred in taxable years beginning after December 31, 2003, the Administration proposes to allow certain teachers and other elementary and secondary school professionals to treat up to $400 in qualified out-of-pocket classroom expenses as a non-itemized deduction (above-the-line deduction). Unreimbursed expenditures for certain books, supplies and equipment related to classroom instruction and for certain professional training programs would qualify for the deduction.

Invest in Health Care

Provide refundable tax credit for the purchase of health insurance.—Current law provides a tax preference for employer-provided group health insurance plans, but not for individually purchased health insurance coverage except to the extent that deductible medical expenses exceed 7.5 percent of AGI or the individual has self-employment income. The Administration proposes to make health insurance more affordable for individuals not covered by an employer plan or a public program. Effective for taxable years beginning after December 31, 2002, a new refundable tax credit would be provided for the cost of health insurance purchased by individuals under age 65. The credit would provide a subsidy for a percentage of the health insurance premium, up to a maximum includable premium. The maximum subsidy percentage would be 90 percent for low-income taxpayers and would phase down with income. The maximum credit would be $1,000 for an adult and $500 for a child. The credit would be phased out at $30,000 for single taxpayers and $60,000 for families purchasing a family policy.

Individuals could claim the tax credit for health insurance premiums paid as part of the normal tax-filing process. Alternatively, beginning July 1, 2003, the tax credit would be available in advance at the time the individual purchases health insurance. The advance credit would reduce the premium paid by the individual to the health insurer, and the health insurer would be reimbursed directly by the Department of Treasury for the amount of the advance credit. Eligibility for an advance credit would be based on an individual's prior year tax return. To qualify for the credit, a health insurance policy would have to include coverage for catastrophic medical expenses. Qualifying insurance could be purchased in the individual market. Qualifying health insurance could also be purchased through private purchasing groups, State-sponsored insurance purchasing pools, and high-risk pools. Such groups may help reduce health insurance costs and increase coverage options for individuals, including older and higher-risk individuals. Individuals would not be allowed to claim the credit and make a contribution to an Archer Medical Savings Account (MSA) for the same taxable year.

Provide an above-the-line deduction for long-term care insurance premiums.—Current law provides a tax preference for employer-paid long-term care insurance. However, the vast majority of the long-term care insurance market consists of individually purchased policies, for which no tax preference is provided except to the extent that deductible medical expenses exceed 7.5 percent of AGI or the individual has self-employment income. Premiums on qualified long-term care insurance are deductible as a medical expense, subject to annual dollar limitations that increase with age. The Administration proposes to make individually-purchased long-term care insurance (the vast majority of the long-term care insurance market) more affordable by creating an above-the-line deduction for qualified long-term care insurance premiums. To qualify for the deduction, the long-term care insurance would be required to meet certain standards providing consumer protections. The deduction would be available to taxpayers who individually purchase qualified long-term care insurance and to those who pay at least 50 percent of the cost of employer-provided coverage. The deduction would be effective for taxable years beginning after December 31, 2003 but would be phased in over five years. The deduction would be subject to current law annual dollar limitations on qualified long-term care insurance premiums.

Allow up to $500 in unused benefits in a health flexible spending arrangement to be carried forward to the next year.—Under current law, unused benefits in a health flexible spending arrangement under a cafeteria plan for a particular year revert to the employer at the end of the year. Effective for plan years beginning after December 31, 2003, the Administration proposes to allow up to $500 in unused benefits in a health flexible spending arrangement at the end of a particular year to be carried forward to the next plan year.

Provide additional choice with regard to unused benefits in a health flexible spending arrangement.—In addition to the proposed carryforward of unused benefits (see preceding discussion), the Administration proposes to allow up to $500 in unused benefits in a health flexible spending arrangement at the end of a particular year to be distributed to the participant as taxable income, contributed to an Archer MSA, or contributed to the employer's 401(k), 403(b), or governmental 457(b) retirement plan. Amounts distributed to the participant would be subject to income tax withholding and employment taxes. Amounts contributed to an Archer MSA or retirement plan would be subject to the normal rules applicable to elective contributions to the receiving plan or account. The proposal would be effective for plan years beginning after December 31, 2003.

Permanently extend and reform Archer Medical Savings Accounts.—Current law allows only self-employed individuals and employees of small firms to establish Archer MSAs, and caps the number of accounts at 750,000. In addition to other requirements, (1) individuals who establish MSAs must be covered by a high-deductible health plan (and no other plan) with a deductible of at least $1,650 but not greater than $2,500 for policies covering a single person and a deductible of at least $3,300 but not greater than $4,950 in all other cases, (2) tax-preferred contributions are limited to 65 percent of the deductible for single policies and 75 percent of the deductible for other policies, and (3) either an individual or an employer, but not both, may make a tax-preferred contribution to an MSA for a particular year. The Administration proposes to permanently extend the MSA program, which is scheduled to expire on December 31, 2002, and to modify the program to make it more consistent with currently available health plans. Effective after December 31, 2002, the Administration proposes to remove the 750,000 cap on the number of accounts. In addition, the program would be reformed by (1) expanding eligibility to include all individuals and employees of firms of all sizes covered by a high-deductible health plan, (2) modifying the definition of high deductible to permit a deductible as low as $1,000 for policies covering a single person and $2,000 in all other cases, (3) increasing allowable tax-preferred contributions to 100 percent of the deductible, (4) allowing tax-preferred contributions by both employers and employees for a particular year, up to the applicable maximum, (5) allowing contributions to MSAs under cafeteria plans, and (6) permitting qualified plans to provide, without counting against the deductible, up to $100 of coverage for allowable preventive services per covered individual each year. Individuals would not be allowed to make a contribution to an MSA and claim the proposed refundable tax credit for health insurance premiums for the same taxable year.

Provide an additional personal exemption to home caretakers of family members.—Current law provides a tax deduction for certain long-term care expenses. In addition, taxpayers are allowed to claim exemptions for themselves (and their spouses, if married) and dependents who they support. However, neither provision may meet the needs of taxpayers who provide long-term care in their own home for close family members. Effective for taxable years beginning after December 31, 2003, the Administration proposes to provide an additional personal exemption to taxpayers who care for certain qualified family members who reside with the taxpayer in the household maintained by the taxpayer. A taxpayer is considered to maintain a household only if he/she furnishes over half of the annual cost of maintaining the household. Qualified family members would include any individual with long-term care needs who (1) is the spouse of the taxpayer or an ancestor of the taxpayer or the spouse of such an ancestor and (2) is a member of the taxpayer's household for the entire year. An individual would be considered to have long-term care needs if he or she were certified by a licensed physician (prior to the filing of a return claiming the exemption) as being unable for at least 180 consecutive days to perform at least two activities of daily living without substantial assistance from another individual due to a loss of functional capacity. Alternatively, an individual would be considered to have long-term care needs if he or she were certified by a licensed physician as, for at least 180 consecutive days, (1) requiring substantial supervision to be protected from threats to his or her own health and safety due to severe cognitive impairment and (2) being unable to perform at least one activity of daily living or being unable to engage in age appropriate activities.

Assist Americans With Disabilities

Exclude from income the value of employer-provided computers, software and peripherals.—The Administration proposes to allow individuals with disabilities to exclude from income the value of employer-provided computers, software or other office equipment that are necessary for the individual to perform work for the employer at home. To qualify for the exclusion, the employee would be required to make substantial use of the equipment (relative to overall use) performing work for his or her employer. However, unlike current law, which limits the exclusion to the extent that the equipment is used to perform work for the employer, the proposed exclusion would apply to all use of such equipment, including use by the employee for personal or non-employer-related trade or business purposes. Employees would be required to provide their employer with a certification from a licensed physician that they meet eligibility criteria. The proposal would be effective for taxable years beginning after December 31, 2003.

Help Farmers and Fishermen Manage Economic Downturns

Establish Farm, Fish and Ranch Risk Management (FFARRM) savings accounts.—Current law does not provide for the elective deferral of farm or fishing income. However, farmers can elect to average their farming income over a three-year period, and farmers may carry back net operating losses over the five previous years. In addition, taxes can be deferred on certain forms of income, including disaster payments, crop insurance and proceeds from emergency livestock sales. The Administration proposes to allow up to 20 percent of taxable income attributable to an eligible farming or fishing business to be contributed to a FFARRM savings account each year and deducted from income. Earnings on contributions would be taxable as earned and distributions from the account (except those attributable to earnings on contributions) would be included in gross income. Any amount not distributed within five years of deposit would be deemed to have been distributed and included in gross income; in addition, such distributions would be subject to a 10-percent surtax. The proposal would be effective for taxable years beginning after December 31, 2003.

Increase Housing Opportunities

Provide tax credit for developers of affordable single-family housing.—The Administration proposes to provide annual tax credit authority to States (including U.S. possessions) designed to promote the development of affordable single-family housing in low-income urban and rural neighborhoods. Beginning in calendar year 2003, first-year credit authority of $1.75 per capita (indexed annually for inflation thereafter) would be made available to each State. State housing agencies would award first-year credits to single-family housing units comprising a project located in a census tract with median income equal to 80 percent or less of area median income. Units in condominiums and cooperatives could qualify as single-family housing. Credits would be awarded as a fixed amount for individual units comprising a project. The present value of the credits, determined on the date of a qualifying sale, could not exceed 50 percent of the cost of constructing a new home or rehabilitating an existing property. The taxpayer (developer or investor partnership) owning the housing unit immediately prior to the sale to a qualified buyer would be eligible to claim credits over a 5-year period beginning on the date of sale. Eligible homebuyers would be required to have incomes equal to 80 percent or less of area median income. Technical features of the provision would follow similar features of current law with respect to the low-income housing tax credit and mortgage revenue bonds.

Encourage Saving

Establish Individual Development Accounts (IDAs).—The Administration proposes to allow eligible individuals to make contributions to a new savings vehicle, the Individual Development Account, which would be set up and administered by qualified financial institutions, nonprofit organizations, or Indian tribes (qualified entities). Citizens or legal residents of the United States between the ages of 18 and 60 who cannot be claimed as a dependent on another taxpayer's return, are not students, and who meet certain income limitations would be eligible to establish and contribute to an IDA. A single taxpayer would be eligible to establish and contribute to an IDA if his/her modified AGI in the preceding taxable year did not exceed $20,000 ($30,000 for heads of household, and $40,000 for married taxpayers filing a joint return). These thresholds would be indexed annually for inflation beginning in 2004. Qualified entities that set up and administer IDAs would be required to match, dollar-for-dollar, the first $500 contributed by an eligible individual to an IDA in a taxable year. Qualified entities would be allowed a 100 percent tax credit for up to $500 in annual matching contributions to each IDA, and a $50 tax credit for each IDA maintained at the end of a taxable year with a balance of not less that $100 (excluding the taxable year in which the account was established). Matching contributions and the earnings on those contributions would be deposited in a separate "parallel account." Contributions to an IDA by an eligible individual would not be deductible, and earnings on those contributions would be included in income. Matching contributions by qualified entities and the earnings on those contributions would be tax-free. Withdrawals from the parallel account may be made only for qualified purposes (higher education, the first-time purchase of a home, business start-up, and qualified rollovers). Withdrawals from the IDA for other than qualified purposes may result in the forfeiture of some or all matching contributions and the earnings on those contributions. The proposal would be effective for contributions made after December 31, 2002 and before January 1, 2010, to the first 900,000 IDA accounts opened before January 1, 2008.

Protect the Environment

Permanently extend expensing of brownfields remediation costs.—Taxpayers may elect to treat certain environmental remediation expenditures that would otherwise be chargeable to capital account as deductible in the year paid or incurred. Under current law, the ability to deduct such expenditures expires with respect to expenditures paid or incurred after December 31, 2003. The Administration proposes to permanently extend this provision, facilitating its use by businesses to undertake projects that may extend beyond the current expiration date and be uncertain in overall duration.

Exclude 50 percent of gains from the sale of property for conservation purposes.—The Administration proposes to create a new incentive for private, voluntary land protection. This incentive is a cost-effective, non-regulatory approach to conservation. Under the proposal, when land (or an interest in land or water) is sold for conservation purposes, only 50 percent of any gain would be included in the seller's income. To be eligible for the exclusion, the sale may be either to a government agency or to a qualified conservation organization, and the buyer must supply a letter of intent that the acquisition will serve conservation purposes. In addition, the taxpayer or a member of the taxpayer's family must have owned the property for the three years immediately preceding the sale. The provision would be effective for sales taking place after December 31, 2003.

Increase Energy Production and Promote Energy Conservation

Extend and modify the tax credit for producing electricity from certain sources.—Taxpayers are provided a 1.5-cent-per-kilowatt-hour tax credit, adjusted for inflation after 1992, for electricity produced from wind, closed-loop biomass (organic material from a plant grown exclusively for use at a qualified facility to produce electricity), and poultry waste. To qualify for the credit, the electricity must be sold to an unrelated third party and must be produced during the first 10 years of production at a facility placed in service before January 1, 2002. The Administration proposes to extend the credit for electricity produced from wind and biomass to facilities placed in service before January 1, 2005. In addition, eligible biomass sources would be expanded to include certain biomass from forest-related resources, agricultural sources, and other specified sources. Special rules would apply to biomass facilities placed in service before January 1, 2002. Electricity produced at such facilities from newly eligible sources would be eligible for the credit only from January 1, 2002 through December 31, 2004, and at a rate equal to 60 percent of the generally applicable rate. Electricity produced from newly eligible biomass co-fired in coal plants would also be eligible for the credit only from January 1, 2002 through December 31, 2004, and at a rate equal to 30 percent of the generally applicable rate. The Administration also proposes to modify the rules relating to governmental financing of qualified facilities. There would be no percentage reduction in the credit for governmental financing attributable to tax-exempt bonds. Instead, such financing would reduce the credit only to the extent necessary to offset the value of the tax exemption. The rules relating to leased facilities would also be modified to permit the lessee, rather than the owner, to claim the credit.

Provide tax credit for residential solar energy systems.—Current law provides a 10-percent investment tax credit to businesses for qualifying equipment that uses solar energy to generate electricity; to heat, cool or provide hot water for use in a structure; or to provide solar process heat. A credit currently is not provided for nonbusiness purchases of solar energy equipment. The Administration proposes a new tax credit for individuals who purchase solar energy equipment to generate electricity (photovoltaic equipment) or heat water (solar water heating equipment) for use in a dwelling unit that the individual uses as a residence, provided the equipment is used exclusively for purposes other than heating swimming pools. The proposed nonrefundable credit would be equal to 15 percent of the cost of the equipment and its installation; each individual taxpayer would be allowed a maximum credit of $2,000 for photovoltaic equipment and $2,000 for solar water heating equipment. The credit would apply to photovoltaic equipment placed in service after December 31, 2001 and before January 1, 2008 and to solar water heating equipment placed in service after December 31, 2001 and before January 1, 2006.

Modify treatment of nuclear decommissioning funds.—Under current law, deductible contributions to nuclear decommissioning funds are limited to the amount included in the taxpayer's cost of service for ratemaking purposes. For deregulated utilities, this limitation may result in the denial of any deduction for contributions to a nuclear decommissioning fund. The Administration proposes to repeal this limitation.

Also under current law, deductible contributions are not permitted to exceed the amount the IRS determines to be necessary to provide for level funding of an amount equal to the taxpayer's post-1983 decommissioning costs. The Administration proposes to permit funding of all decommissioning costs through deductible contributions. Any portion of these additional contributions relating to pre-1983 costs that exceeds the amount previously deducted (other than under the nuclear decommissioning fund rules) or excluded from the taxpayer's gross income on account of the taxpayer's liability for decommissioning costs, would be allowed as a deduction ratably over the remaining useful life of the nuclear power plant.

The Administration's proposal would also permit taxpayers to make deductible contributions to a qualified fund after the end of the nuclear power plant's estimated useful life and would provide that nuclear decommissioning costs are deductible when paid. These changes in the treatment of nuclear decommissioning funds are proposed to be effective for taxable years beginning after December 31, 2001.

Provide tax credit for purchase of certain hybrid and fuel cell vehicles.—Under current law, a 10-percent tax credit up to $4,000 is provided for the cost of a qualified electric vehicle. The full amount of the credit is available for purchases prior to 2002. The credit begins to phase down in 2002 and is not available after 2004. A qualified electric vehicle is a motor vehicle that is powered primarily by an electric motor drawing current from rechargeable batteries, fuel cells, or other portable sources of electric current, the original use of which commences with the taxpayer, and that is acquired for use by the taxpayer and not for resale. Electric vehicles and hybrid vehicles (those that have more than one source of power on board the vehicle) have the potential to reduce petroleum consumption, air pollution and greenhouse gas emissions. To encourage the purchase of such vehicles, the Administration is proposing the following tax credits: (1) A credit of up to $4,000 would be provided for the purchase of qualified hybrid vehicles after December 31, 2001 and before January 1, 2008. The amount of the credit would depend on the percentage of maximum available power provided by the rechargeable energy storage system and the amount by which the vehicle's fuel economy exceeds the 2000 model year city fuel economy. (2) A credit of up to $8,000 would be provided for the purchase of new qualified fuel cell vehicles after December 31, 2001 and before January 1, 2008. A minimum credit of $4,000 would be provided, which would increase as the vehicle's fuel efficiency exceeded the 2000 model year city fuel economy, reaching a maximum credit of $8,000 if the vehicle achieved at least 300 percent of the 2000 model year city fuel economy.

Provide tax credit for energy produced from landfill gas.—Taxpayers that produce gas from biomass (including landfill methane) are eligible for a tax credit equal to $3 per barrel-of-oil equivalent (the amount of gas that has a British thermal unit content of 5.8 million), adjusted by an inflation adjustment factor for the calendar year in which the sale occurs. To qualify for the credit, the gas must be produced domestically from a facility placed in service by the taxpayer before July 1, 1998, pursuant to a written binding contract in effect before January 1, 1997. In addition, the gas must be sold to an unrelated person before January 1, 2008. The Administration proposes to extend the credit to apply to landfill methane produced from a facility (or portion of a facility) placed in service after December 31, 2001 and before January 1, 2011, and sold (or used to produce electricity that is sold) before January 1, 2011. The credit for fuel produced at landfills subject to EPA's 1996 New Source Performance Standards/Emissions Guidelines would be limited to two-thirds of the otherwise applicable amount beginning on January 1, 2008, if any portion of the facility for producing fuel at the landfill was placed in service before July 1, 1998, and beginning on January 1, 2002, in all other cases.

Provide tax credit for combined heat and power property.—Combined heat and power (CHP) systems are used to produce electricity (and/or mechanical power) and usable thermal energy from a single primary energy source. Depreciation allowances for CHP property vary by asset use and capacity. No income tax credit is provided under current law for investment in CHP property. CHP systems utilize thermal energy that is otherwise wasted in producing electricity by more conventional methods and achieve a greater level of overall energy efficiency, thereby lessening the consumption of primary fossil fuels, lowering total energy costs, and reducing carbon emissions. To encourage increased energy efficiency by accelerating planned investments and inducing additional investments in such systems, the Administration is proposing a 10-percent investment credit for qualified CHP systems with an electrical capacity in excess of 50 kilowatts or with a capacity to produce mechanical power in excess of 67 horsepower (or an equivalent combination of electrical and mechanical energy capacities). A qualified CHP system would be required to produce at least 20 percent of its total useful energy in the form of thermal energy and at least 20 percent of its total useful energy in the form of electrical or mechanical power (or a combination thereof) and would also be required to satisfy an energy-efficiency standard. For CHP systems with an electrical capacity in excess of 50 megawatts (or a mechanical energy capacity in excess of 67,000 horsepower), the total energy efficiency would have to exceed 70 percent. For smaller systems, the total energy efficiency would have to exceed 60 percent. Investments in qualified CHP assets that are otherwise assigned cost recovery periods of less than 15 years would be eligible for the credit, provided that the taxpayer elected to treat such property as having a 22-year class life. The credit, which would be treated as an energy credit under the investment credit component of the general business credit, and could not be used in conjunction with any other credit for the same equipment, would apply to investments in CHP property placed in service after December 31, 2001 and before January 1, 2007.

Provide excise tax exemption (credit) for ethanol.—Under current law an income tax credit and an excise tax exemption are provided for ethanol and renewable source methanol used as a fuel. In general, the income tax credit for ethanol is 53 cents per gallon, but small ethanol producers (those producing less than 30 million gallons of ethanol per year) qualify for a credit of 63 cents per gallon on the first 15 million gallons of ethanol produced in a year. A credit of 60 cents per gallon is allowed for renewable source methanol. As an alternative to the income tax credit, gasohol blenders may claim a gasoline tax exemption of 53 cents for each gallon of ethanol and 60 cents for each gallon of renewable source methanol that is blended into qualifying gasohol. The rates for the ethanol credit and exemption are each reduced by 1 cent per gallon in 2003 and by an additional 1 cent per gallon in 2005. The income tax credit expires on December 31, 2007 and the excise tax exemption expires on September 30, 2007. Neither the credit nor the exemption apply during any period in which motor fuel taxes dedicated to the Highway Trust Fund are limited to 4.3 cents per gallon. The Administration proposes to extend both the income tax credit and the excise tax exemption through December 31, 2010. The current law rule providing that neither the credit nor the exemption apply during any period in which motor fuel taxes dedicated to the Highway Trust Fund are limited to 4.3 cents per gallon would be retained.

Promote Trade

Extend and expand Andean trade preferences.—The Administration proposes to renew and enhance the Andean Trade Preference Act (ATPA), which expired on December 4, 2001, through December 31, 2005. The ATPA, which was enacted in 1991, was designed to provide economic alternatives for Bolivia, Columbia, Ecuador, and Peru in their fight against narcotics production and trafficking.

Initiate a new trade preference program for Southeast Europe.—The Administration is proposing the Southeast Europe Trade Preference Act (SETPA), which would initiate a new five-year trade preference program for Southeast Europe, beginning October 1, 2002. The program is designed to rebuild the economies of Southeast Europe that were harmed by recent ethnic conflict in the area and will fulfill a commitment made by the United States, along with our European partners, when we signed the Stability Pact for Southeast Europe.

Implement free trade agreements with Chile and Singapore.—Free trade agreements are expected to be completed with Chile and Singapore in 2002, with ten-year implementation to begin in fiscal year 2003. These agreements will benefit U.S. producers and consumers, as well as strengthen the economies of Chile and Singapore. In addition, these agreements will establish precedents in our market opening efforts in two important and dynamic regions - Latin America and Southeast Asia.

Improve Tax Administration

Modify the IRS Restructuring and Reform Act of 1998 (RRA98).—The proposed modification to RRA98 is comprised of six parts. The first part modifies employee infractions subject to mandatory termination and permits a broader range of available penalties. It strengthens taxpayer privacy while reducing employee anxiety resulting from unduly harsh discipline or unfounded allegations. The second part adopts measures to curb frivolous submissions and filings that are intended to impede or delay tax administration. The third part allows IRS to terminate installment agreements when taxpayers fail to make timely tax deposits and file tax returns on current liabilities. The fourth part streamlines jurisdiction over collection due process cases in the Tax Court, thereby reducing the cycle time for certain collection due process cases. The fifth part permits taxpayers to enter into installment agreements that do not guarantee full payment of liability over the life of the agreement. It allows the IRS to enter into agreements with taxpayers that desire to resolve their tax obligations but cannot make payments large enough to satisfy their entire liability and for whom an offer in compromise is not a viable alternative. The sixth part eliminates the requirement that the IRS Chief Counsel provide an opinion for any accepted offer-in-compromise of unpaid tax (including interest and penalties) equal to or exceeding $50,000. This proposal requires that the Treasury Secretary establish standards to determine when an opinion is appropriate.

Initiate IRS cost savings measures.—The Administration has six proposals to improve IRS efficiency and performance from current resources. The first proposal permits the IRS to use certificates of mailing as an alternative to certified mail for notices and letters that currently require such mailing. The second proposal eliminates the requirement that notices of an intent to levy and right to a pre-levy hearing be sent with return receipt requested, but retains the requirement that such notices be sent by certified or registered mail or by first-class mail evidenced by a certificate of mailing. These two proposals reduce postal costs while retaining proof of first-class mailing. The third proposal eliminates the requirement that dual notices be sent to joint filers who reside at the same address. The fourth proposal treats as nullities certain tax returns that the Criminal Investigation Division determines contain insufficient information to compute tax, contain false information, or lack a valid signature. Under this proposal, such returns that have been filed to impede or delay tax administration are excluded from deficiency procedures. The fifth proposal modifies the way that Financial Management Services (FMS) recovers its transaction fees for processing IRS levies by permitting FMS to retain a portion of the amount collected before transmitting the balance to the IRS. The offset amount would be included as part of the 15-percent limit on levies against income and would also be credited against the taxpayer's liability, thereby reducing Government transactions costs. Finally, the sixth proposal extends the April filing date for electronically filed tax returns by at least ten days to help encourage the growth of electronic filing.

Reform Unemployment Insurance

Reform unemployment insurance administrative financing.—Current law funds the administrative costs of the unemployment insurance system and related programs out of the Federal Unemployment Tax (FUTA) paid by employers. FUTA is set at 0.8 percent of the first $7,000 in covered wages, which includes a 0.2 percent surtax scheduled to expire in 2007. State unemployment taxes are deposited into the Unemployment Trust Fund and used by States to pay unemployment benefits. Under current law, FUTA balances in excess of statutory ceilings are distributed to the States to pay unemployment benefits or the administrative costs of the system (these are known as Reed Act transfers). The Administration supports an immediate distribution of $9 billion in Reed Act funds as part of a bipartisan economic security plan. This would take the place of the smaller Reed Act transfer projected for October 1, 2002. In addition, the Administration has a comprehensive proposal to reform the administrative financing of this system. It proposes to eliminate the FUTA surtax in 2003, and make additional rate cuts to achieve a net FUTA tax rate of 0.2 percent in 2007. The proposal will transfer administrative funding control to the States in 2005 and allow them to use their benefit taxes to pay these costs. Federal administrative grants to the States will be significantly reduced. During the transition to State financing, special Reed Act distributions will be made to the States, and additional Federal funds for administrative expenses will be provided.

EXPIRING PROVISIONS

Extend Provisions that Expired in 2001 for Two Years

Extend the work opportunity tax credit.—The work opportunity tax credit provides an incentive for employers to expand the number of entry level positions for individuals from certain targeted groups. The credit generally applies to the first $6,000 of wages paid to several categories of economically disadvantaged or handicapped workers. The credit rate is 25 percent of qualified wages for employment of at least 120 hours but less than 400 hours and 40 percent for employment of 400 or more hours. The Administration proposes to extend the credit for two years, making the credit available for workers hired after December 31, 2001 and before January 1, 2004.

Extend the welfare-to-work tax credit.—The welfare-to-work tax credit entitles employers to claim a tax credit for hiring certain recipients of long-term family assistance. The purpose of the credit is to expand job opportunities for persons making the transition from welfare to work. The credit is 35 percent of the first $10,000 of eligible wages in the first year of employment and 50 percent of the first $10,000 of eligible wages in the second year of employment. Eligible wages include cash wages plus the cash value of certain employer-paid health, dependent care, and educational fringe benefits. The minimum employment period that employees must work before employers can claim the credit is 400 hours. The Administration proposes to extend the credit for two years, to apply to individuals who begin work after December 31, 2001 and before January 1, 2004.

Extend minimum tax relief for individuals.—A temporary provision of prior law permits nonrefundable personal tax credits to be offset against both the regular tax and the alternative minimum tax. The temporary provision expires after taxable year 2001. The Administration is concerned that the AMT may limit the benefit of personal tax credits and impose financial and compliance burdens on taxpayers who have few, if any, tax preference items and who were not the originally intended targets of the AMT. The Administration proposes to extend minimum tax relief for nonrefundable personal tax credits two years, to apply to taxable years 2002 and 2003. The proposed extension does not apply to the child credit, the earned income tax credit or the adoption credit, which were provided AMT relief through December 31, 2010 under the Economic Growth and Tax Relief Reconciliation Act of 2001, as explained above. The refundable portion of the child credit and the earned income tax credit are also allowed against the AMT through December 31, 2010.

Extend exceptions provided under subpart F for certain active financing income.—Under the Subpart F rules, certain U.S. shareholders of a controlled foreign corporation (CFC) are subject to U.S. tax currently on certain income earned by the CFC, whether or not such income is distributed to the shareholders. The income subject to current inclusion under the subpart F rules includes, among other things, “foreign personal holding company income” and insurance income. Foreign personal holding company income generally includes many types of income derived by a financial service company, such as dividends; interest; royalties; rents; annuities; net gains from the sale of certain property, including securities, commodities and foreign currency; and income from notional principal contracts and securities lending activities. For taxable years beginning before 2002, certain income derived in the active conduct of a banking, financing, insurance, or similar business is excepted from Subpart F. The Administration proposes to extend the exception for two years, to apply to taxable years beginning in 2002 and 2003.

Extend suspension of net income limitation on percentage depletion from marginal oil and gas wells.—Taxpayers are allowed to recover their investment in oil and gas wells through depletion deductions. For certain properties, deductions may be determined using the percentage depletion method; however, in any year, the amount deducted generally may not exceed 100 percent of the net income from the property. For taxable years beginning after December 31, 1997 and before January 1, 2002, domestic oil and gas production from "marginal" properties is exempt from the 100-percent of net income limitation. The Administration proposes to extend the exemption to apply to taxable years beginning after December 31, 2001 and before January 1, 2004.

Extend Generalized System of Preferences (GSP).—Under GSP, duty-free access is provided to over 4,000 items from eligible developing countries that meet certain worker rights, intellectual property protection, and other criteria. The Administration proposes to extend this program, which expired after September 30, 2001, through September 30, 2003.

Extend authority to issue Qualified Zone Academy Bonds.—Prior law allows State and local governments to issue "qualified zone academy bonds," the interest on which is effectively paid by the Federal government in the form of an annual income tax credit. The proceeds of the bonds must be used for teacher training, purchases of equipment, curriculum development, or rehabilitation and repairs at certain public school facilities. A nationwide total of $400 million of qualified zone academy bonds was authorized to be issued in each of calendar years 1998 through 2001. In addition, unused authority arising in 1998 and 1999 may be carried forward for up to three years and unused authority arising in 2000 and 2001 may be carried forward for up to two years. The Administration proposes to authorize the issuance of an additional $400 million of qualified zone academy bonds in each of calendar years 2002 and 2003.

Permanently Extend Expiring Provisions

Permanently extend provisions expiring in 2010.—As explained in the discussion of the Economic Growth and Tax Relief Reconciliation Act of 2001, most of the provisions of the Act sunset on December 31, 2010. The Administration proposes to permanently extend these provisions.

Permanently extend the research and experimentation (R&E) tax credit.—The Administration proposes to permanently extend the 20-percent tax credit for qualified research and experimentation expenditures above a base amount and the alternative incremental credit, which are scheduled to expire on June 30, 2004.

TAX SIMPLIFICATION

In addition to the proposals summarized above, the Administration is developing both short-term and longer-term tax simplification proposals. The project to develop short-term proposals, which is described below, focuses on immediately achievable reforms of the current tax system, while the longer-term project focuses on more fundamental reforms of the tax system.

As many recent studies and proposals have highlighted, the U.S. income tax system is extraordinarily complex. Many taxpayers and businesses face significant challenges in understanding the tax laws, keeping required records, and filling out numerous complicated and detailed tax forms, which often require working through lengthy abstruse instructions and cumbersome calculations. Fortunately, our tax system is not complicated for everyone. Millions of taxpayers who have relatively uncomplicated financial and family circumstances and are able to file form 1040EZ, for example, avoid most of the complexity of the tax system. But for many others, coping with the tax system is daunting. The need to deal with complexities in the tax system is not limited to multinational corporations or high-income investors with complex financial assets; many taxpayers facing overwhelmingly complicated tax situations are lower- and middle-income families, single mothers, elderly people, small business owners and entrepreneurs.

Tax complexity is costly to taxpayers and the economy. Credible estimates of the cost to taxpayers of complying with the income tax range from $70 billion to $125 billion per year. Additional costs may be imposed on the economy if taxpayers avoid certain investments, savings vehicles, business transactions, etc., because of the tax complexities they would involve or because of uncertainty about how the tax system would apply to them. Extensive tax planning engaged in by some taxpayers and businesses is a wasteful use of resources. Complexity makes it more costly for the IRS to administer the tax system. It makes it more difficult for the IRS to train its staff, to give correct answers to increased numbers of taxpayers seeking help in understanding the tax laws, and to check and audit tax returns. These costs are a significant burden on the economy. Tax simplification can cut these costs and contribute to greater economic efficiency.

Tax complexity also may have other undesirable effects. Complexity may undermine confidence in the tax system. If taxpayers conclude that the tax system is so complex that no one can really figure it out, it will destroy confidence that the tax system is accomplishing its objectives, that other taxpayers are paying their fair share of tax, and that the IRS can administer the system fairly. It may thereby undermine compliance with the tax system and confidence in the government in general. Reducing tax complexity is, therefore, an important policy objective.

But tax simplification is not simple. Complexity in the tax system has not arisen merely because the writers of the tax laws have been inattentive or because of a desire to provide jobs for tax accountants and lawyers. Many legitimate factors contribute to tax complexity. The modern, highly-productive U.S. economy is very complex, and many taxpayers and companies have complex financial and economic situations. Application of the tax system to these complex financial and economic arrangements is also unavoidably complex. Many taxpayers have complex family arrangements or have special circumstances that affect their needs or their ability to pay taxes. Many special provisions have been added to the tax system to recognize the special circumstances of certain groups of taxpayers and adjust their tax burdens accordingly. The tax system has also been used extensively to provide incentives or benefits for taxpayers engaging in certain kinds of activities ranging from saving for retirement to saving energy that are deemed to be socially beneficial. While all of these tax provisions are well intended and presumptively have beneficial effects, they also contribute to complexity in the tax system. At some point, the complexity itself detracts from the ability of the tax system to function effectively and to accomplish these other objectives.

Because of the multiple objectives involved in shaping any particular tax provision, the effort to simplify the tax system frequently involves tradeoffs. There may be a few places in the tax code where it is possible to draft less complex provisions that will accomplish all of the policy objectives equally well or even better. Such complexities may have arisen because of insufficient time to draft less complex provisions as a tax bill was being passed or because a series of provisions has been enacted, revised, and added to over time without an effort to consider the whole set of provisions and how they could be combined and simplified to better achieve their objectives. In many cases, however, simplification will result in some compromise in achieving other policy objectives, less precise targeting of a tax benefit, treatment of a type of income or expense in a way that is less consistent with its true economic nature, etc. In many areas, therefore, developing simplification proposals involves identifying areas of the tax system and specific simplification schemes for which the simplification that can be achieved is regarded as more valuable than the resulting decrease in achievement of other policy goals.

The purpose of tax simplification, therefore, may be stated succinctly as implementing changes that will reduce the compliance burden on taxpayers and/or administrative costs of the IRS while enhancing or resulting in acceptably small sacrifices in the achievement of other policy objectives such as efficiency, fairness, revenue, and enforceability.

The Administration has established the following objectives for the simplification project and principles for developing the simplification proposals.

Objectives of Simplification

- To reduce burdens on taxpayers and the IRS.
- Greater economic growth.
- Increased voluntary compliance, including use of the tax benefits provided by the law.
- Lower administrative and compliance costs.
- Fewer errors made by taxpayers and the IRS.
- Fewer inquiries taxpayers must make and the IRS must handle.
- Fewer disputes between the IRS and taxpayers.
- Increased predictability (i.e., transparency) of the tax law.
- Improvement of taxpayers' confidence in the system.
- Similar treatment of similarly situated taxpayers.
- Similar treatment of transactions with similar economic results.
- Fewer complex and expensive tax planning strategies.

Principles for Developing Tax Simplification Proposals

- Reduce or eliminate rules or requirements when the cost of compliance and/or enforcement outweighs the benefits of the rules or requirements.
- Improve the readability of the law.
- Reduce overly technical and overly vague language in the law.
- Avoid highly detailed conditions and requirements.
- Eliminate duplicative or overlapping provisions.
- Eliminate differing definitions of similar terms or concepts.
- Reduce the amount of subjectivity necessary to apply the tax law by providing clear rules and clear distinctions.
- Reduce structural complexity.
- Reduce the number of phase-out provisions or coordinate the amounts in different phase-out provisions.
- Reduce the number and/or complexity of computations.
- Reduce record keeping and information gathering requirements; coordinate record keeping and information gathering requirements with business practices.
- Reduce inconsistencies in the law so that similarly situated taxpayers are treated the same.
- Reduce distortions among economic activities.
- Eliminate provisions or rules no longer needed because other provisions or rules have changed or because the provisions or rules are outdated.
- Reduce the number of temporary or sunset provisions.

Highest priority will be given to simplification proposals that will yield the largest benefits, i.e., that will affect the most people and have the largest effects in reducing compliance burdens and administrative costs.

Examples of areas in the tax system where the Administration's tax simplification project is focusing include the following:

Individual AMT.—The AMT was enacted to ensure that taxpayers with substantial amounts of economic income do not avoid significant tax liability by using combinations of exclusions, deductions, and tax credits. Structural defects in the AMT, including lack of indexing for inflation or adjustment for family size, have resulted in the tax affecting millions of taxpayers to whom it was not intended to apply. Millions of additional taxpayers must complete AMT schedules or forms to determine that they are not subject to the AMT.

The number of taxpayers affected by the AMT and the amount of revenue raised by the AMT are rising rapidly, making simplification of the AMT an increasingly important objective of tax policy. This year, 2 million individual filers will be subject to the AMT and therefore required to file the 65-line AMT form. The temporary increase in the AMT exemption under EGTRRA will reduce the increase in the number of AMT taxpayers through 2004. Nevertheless, that number will increase to 5 million in 2004, and more than double, increasing to 12 million in 2005 when the temporary provision expires. In 2005, 47 percent of taxpayers with AGI between $100,000 and $200,000 (in 2002 dollars) and 75 percent of taxpayers with AGI between $200,000 and $500,000 (in 2002 dollars) will pay AMT. By 2010, these percentages will increase to 90 percent and 96 percent, respectively. By 2012, the number of AMT taxpayers will be 39 million (assuming EGTRRA is extended), which is 34 percent of all taxpayers with individual income tax liability.

Family-related provisions.— Taxpayers with family responsibilities face confusing and sometimes conflicting rules. Many taxpayers are entitled to both the EITC and the additional child tax credit. Both credits are based on earned income and the number of children in the family. But the two credits use different definitions of earned income, and different definitions of qualifying children. Further, many taxpayers with three or more children must compute the additional child tax credit twice to determine which formula yields the larger credit. Similarly, some taxpayers can offset the costs of child care assistance using either a child and dependent care tax credit or an exclusion from income, but they must make multiple computations to determine which of the two is most advantageous. Conforming eligibility criteria and reducing the number of computations taxpayers must make would help simplify family-related tax provisions, thus reducing burdens on families.

Uniform definition of a child.—The tax code provides assistance to families with children through the dependent exemption, head-of-household filing status, child tax credit, child and dependent care tax credit, and EITC. But to obtain these benefits, taxpayers must wade through pages of bewildering rules and instructions because each provision defines "qualifying child" differently. For example, to claim the dependent exemption and the child tax credit, a taxpayer must demonstrate that he or she provides most of the support of the child. To claim the EITC, the taxpayer must demonstrate that he or she resides with the child for a specified period of time. Replacing the support test, which is difficult to understand and to administer, with a uniform residency test would reduce both compliance and administrative costs.

Income based phaseouts.—Various tax provisions are phased out in order to target the effects of the provisions and to limit the associated revenue loss. The major provisions subject to income-based phaseouts are the EITC, the child tax credit, the child and dependent care tax credit, IRAs, the HOPE and Lifetime Learning tax credits, the deduction for higher-education expenses, the deduction for student loan interest, the exclusion for interest on education savings bonds, and the adoption credit and exclusion. Two additional phase-out provisions are scheduled to be reduced beginning in 2006 and eliminated completely in 2010: the overall limitation on itemized deductions; and the phaseout of personal exemptions. Phaseouts are complicated and increase marginal tax rates, sometimes significantly. Complexity is increased even more by the fact that different benefits are phased out differently. As a result, taxpayers must often consider multiple phase-out provisions.

Education incentives.—The various tax code provisions providing incentives for higher education use differing definitions of the various elements that make up qualifying higher education expenses. The definitional differences add to the complexity taxpayers face when they use the education incentives. The array of education incentives from which taxpayers may choose means further complexity.

Individual Retirement Accounts.—The current multiple sets of IRA income limits are complex and contain marriage penalties. The income limits complicate participation in IRAs by disallowing participation among certain workers depending on type of IRA, income level, filing status, and both spouses' coverage under an employer retirement plan. Taxpayers need to make year-end calculations to determine their eligibility for a deduction or contribution. Taxpayers in the income range over which eligibility for the benefits phases out need to make calculations to determine the deductible portion of contributions to a traditional IRA, or the allowable amount of contributions to a Roth IRA. Taxpayers face uncertainty at the start of the year, because they need to forecast their year-end income to estimate their eligibility.

Individual capital gains.—Under current law, long-term capital gains in excess of any short-term losses are taxed separately from other income, and may be taxed at 8, 10, 18, 20, 25 or 28 percent rates. Special rules apply to collectibles, recapture of certain depreciation deductions, certain small business stock, principal residences, certain investments in Enterprise Zones and similar qualified zones, and certain like-kind exchanges. These multiple capital gains rates and exclusions result in complicated tax forms and schedules, and the need for careful tax planning.

Excise taxes.—A number of excise taxes no longer have a policy rationale, and in several cases involve a significant number of taxpayers but generate relatively little revenue. Some excise taxes could be restructured to better accomplish policy objectives, reflect recent technological changes, and reduce compliance burdens for both taxpayers and the IRS. Other changes would both improve excise tax compliance and simplify their administration.

Tax-exempt bonds.—Two areas of the statutory tax-exempt bond rules are particularly complex: the definition of a private activity bond and the arbitrage-related provisions. The definition of a private activity bond could be simplified without undoing the policy objective of limiting the issuance of these bonds in tax-exempt form. Compliance with arbitrage rules can be burdensome for issuers even in cases in which bond proceeds are used for traditional governmental purposes. Simplifying changes could be made while still avoiding incentives for premature or over issuance of tax-exempt bonds.

Corporate AMT.—The corporate AMT is a separate tax regime within the Federal income tax system. Under present law, corporations with average gross receipts of at least $7.5 million for the prior three years are required to calculate their tax liability twice: once using the rules of the regular tax system and a second time using the corporate AMT rules. Under the corporate AMT rules, many of the advantageous deductions and credits allowed under the regular tax rules are not allowed, but income under the AMT is taxed at a lower rate than under the regular corporate tax (20 percent, rather than 35 percent). If tax liability calculated under the AMT rules exceeds regular tax liability, the corporation is required to pay AMT in addition to its regular tax. Because payment of AMT represents a prepayment of regular tax, the amount of AMT paid generates AMT credits that can be used to offset regular tax in subsequent years (subject to certain limitations).

The corporate AMT rules increase compliance burdens by causing corporations to devote additional resources to tax planning and record keeping. Because the AMT rules limit the use of tax preferences only for corporations that are AMT payers, corporations that engage in tax-preferred activities incur expenditures to develop strategies to minimize the effect of the AMT rules. In addition, the AMT requires corporations to keep extensive records of numerous adjustments and preferences. For example, depreciation allowances for newly invested property generally are calculated one way under the regular tax and a different way under the AMT. Although a corporation may not have AMT liability, it is required to calculate the AMT to determine whether it owes AMT. The AMT tax regime is difficult and burdensome for corporations to comply with and for IRS to administer.

Depreciation.—There are several sources of complexity in tax depreciation. One source is ambiguity in determining an asset's class life, which determines the asset's annual depreciation allowance. New types of assets, assets used in multiple activities, and building-related expenditures are sometimes difficult to classify and so lead to disputes between taxpayers and the IRS. New assets may be particularly difficult to fit within existing classification guidelines, which generally have not been updated since the mid-1980s.

Placed-in-service conventions also can add to complexity and create uncertainty. Generally, an asset does not receive a full year's depreciation during the tax year in which it is initially placed in service. Instead, the asset receives a fraction of the annual depreciation allowances, as determined by the date on which statutory convention deems the asset to have been placed in service. The placed-in-service conventions sometimes require taxpayers to wait until the end of the taxable year to determine the proper depreciation allowance for property that may have been placed in service at various dates throughout the year.

Capitalization.— Substantial ambiguity exists over whether many items of cost may be deducted currently or instead must be capitalized. Case law holds that the determination of whether an item of cost must be capitalized is based on each particular taxpayer's facts and circumstances. While no one factor has been held to be determinative, the current legal standard relies heavily on whether the item creates a significant future benefit, but the degree of future benefit required for capitalization is ambiguous. Thus, taxpayers and the IRS may end up in dispute over whether certain costs, which traditionally have been deducted, should instead be capitalized. The present uncertain legal environment has elevated capitalization to the top of the list of contested audit issues for businesses.

Tax accounting.—There are many sources of complexity in tax accounting. These include issues related to accrual and inventory accounting, uniform capitalization rules, and the percentage of completion method. Compliance problems generally are more severe for small companies.

Accrual accounting and inventory accounting can be complex and add to the burden of complying with the tax law, especially for small taxpayers. Some of this complexity arises from the additional record keeping required to measure taxes on an accrual basis when the taxpayer uses cash accounting for financial reporting. Additional complexity arises from legal ambiguities about whether certain taxpayers are required to keep inventory accounts. Recently implemented IRS Revenue Procedures provide substantial simplification and certainty by exempting many small taxpayers from the record-keeping burdens of accrual and inventory accounting. For small businesses that do not qualify for tax relief under these Procedures, however, accrual and inventory accounting may continue to impose complexity and record keeping costs.

The LIFO (Last In First Out, a method of accounting for inventories) conformity requirement, that requires firms to use the LIFO method for financial reporting when they use LIFO for tax accounting, also adds to complexity. Conformity violations are more a matter of how information is provided than of what information is provided, creating complications and traps for the unwary.

The uniform capitalization (UNICAP) rules require that both direct and indirect costs be added to basis or included in inventory. Measuring and accounting for all capitalizable costs can be difficult, especially for small taxpayers. Yet, for many taxpayers the UNICAP rules have only a small effect on tax liability, compared to simpler methods, and so add to complexity without substantially affecting tax results.

The percentage of completion method used for determining income from a long-term contract requires the taxpayer to estimate costs and receipts over the life of the contract, with timing errors corrected by a look-back adjustment once the contract is completed. The calculations and record keeping required can be burdensome, especially for small taxpayers. Moreover, in some cases simpler tax accounting methods would cause only a small reduction in tax liability.

International tax rules.—There is much that can be done to reduce the complexity of our international tax rules. This area of the tax law is singled out by businesses as one of the biggest sources of administrative complexity and compliance costs. Moreover, the global economy has changed dramatically since the U.S. international tax rules were developed. It is time to re-examine the rules with a view toward significant rationalization. The focus of efforts in this area will be to reduce the instances in which the international tax rules impose conditions or requirements on U.S. taxpayers that are not consistent with the way businesses operate in the global marketplace and that require efforts that otherwise are unnecessary or noneconomic.

Table 4–3. EFFECT OF PROPOSALS ON RECEIPTS

(In millions of dollars)

	Estimate							
	2002	2003	2004	2005	2006	2007	2003–2007	2003–2012
Bipartisan Economic Security Plan[1]	–62,000	–65,000	–47,500	–9,500	17,000	18,000	–87,000	–43,500
Tax Incentives:								
Provide incentives for charitable giving:								
Provide charitable contribution deduction for nonitemizers	–570	–1,429	–1,437	–2,288	–3,567	–3,591	–12,312	–32,636
Permit tax-free withdrawals from IRAs for charitable contributions	–93	–192	–205	–219	–230	–238	–1,084	–2,632
Raise the cap on corporate charitable contributions	–24	–169	–121	–127	–139	–156	–712	–1,730
Expand and increase the enhanced charitable deduction for contributions of food inventory	–10	–49	–54	–59	–66	–72	–300	–789
Reform excise tax based on investment income of private foundations	–122	–177	–181	–189	–198	–205	–950	–2,101
Modify tax on unrelated business taxable income of charitable remainder trusts	–1	–3	–3	–4	–4	–4	–18	–48
Modify basis adjustment to stock of S corporations contributing appreciated property	–8	–11	–13	–17	–21	–25	–87	–282
Allow expedited consideration of applications for exempt status[2]	....	....	....	....	....	....	....	....
Strengthen and reform education:								
Provide refundable tax credit for certain costs of attending a different school for pupils assigned to failing public schools[3]	....	–10	–24	–38	–52	–62	–186	–219
Allow teachers to deduct out-of-pocket classroom expenses	....	....	–16	–163	–191	–207	–577	–1,718
Invest in health care:								
Provide refundable tax credit for the purchase of health insurance[4]	....	–245	–1,689	–2,811	–2,774	–2,951	–10,470	–29,116
Provide an above-the-line deduction for long-term care insurance premiums	....	–328	–406	–605	–1,222	–2,158	–4,719	–20,730
Allow up to $500 in unused benefits in a health flexible spending arrangement to be carried forward to the next year	....	....	–441	–723	–782	–830	–2,776	–7,819
Provide additional choice with regard to unused benefits in a health flexible spending arrangement	....	....	–23	–39	–45	–52	–159	–566
Permanently extend and reform Archer MSAs	....	....	–43	–468	–530	–607	–1,648	–5,691
Provide an additional personal exemption to home caretakers of family members	....	–314	–383	–362	–345	–348	–1,752	–3,957
Assist Americans with disabilities:								
Exclude from income the value of employer-provided computers, software and peripherals	....	....	–2	–6	–6	–6	–20	–52
Help farmers and fishermen manage economic downturns:								
Establish FFARRM savings accounts	....	....	–133	–350	–244	–171	–898	–1,233
Increase housing opportunities:								
Provide tax credit for developers of affordable single-family housing	....	–7	–76	–302	–715	–1,252	–2,352	–15,257
Encourage saving:								
Establish Individual Development Accounts (IDAs)	....	–124	–267	–319	–300	–255	–1,265	–1,722

Table 4–3. EFFECT OF PROPOSALS ON RECEIPTS—Continued

(In millions of dollars)

	Estimate							
	2002	2003	2004	2005	2006	2007	2003–2007	2003–2012
Protect the environment:								
Permanently extend expensing of brownfields remediation costs	....	....	–193	–306	–299	–289	–1,087	–2,390
Exclude 50 percent of gains from the sale of property for conservation purposes	....	–2	–44	–90	–94	–98	–328	–918
Increase energy production and promote energy conservation:								
Extend and modify tax credit for producing electricity from certain sources	–92	–227	–303	–212	–143	–146	–1,031	–1,779
Provide tax credit for residential solar energy systems	–3	–6	–7	–8	–17	–24	–62	–72
Modify treatment of nuclear decommissioning funds	–89	–156	–168	–178	–188	–199	–889	–2,042
Provide tax credit for purchase of certain hybrid and fuel cell vehicles	–21	–80	–181	–349	–530	–763	–1,903	–3,027
Provide tax credit for energy produced from landfill gas	–12	–34	–59	–86	–120	–140	–439	–1,130
Provide tax credit for combined heat and power property	–97	–208	–235	–238	–296	–139	–1,116	–1,091
Provide excise tax exemption (credit) for ethanol [2]	....	....	....	....	....	....	....	....
Promote trade:								
Extend and expand Andean trade preferences [5]	–130	–192	–213	–226	–58	....	–689	–689
Initiate a new trade preference program for Southeast Europe [5]	....	–19	–23	–25	–7	....	–74	–74
Implement free trade agreements with Chile and Singapore [5]	....	–21	–86	–109	–131	–155	–502	–1,560
Improve tax administration:								
Implement IRS administrative reforms	....	60	49	50	52	54	265	559
Reform unemployment insurance:								
Reform unemployment insurance administrative financing [5]	....	–1,002	–1,451	–2,902	–2,982	–4,429	–12,766	–6,924
Expiring Provisions:								
Extend provisions that expired in 2001 for two years:								
Work opportunity tax credit	–43	–153	–200	–127	–60	–29	–569	–576
Welfare-to-work tax credit	–9	–37	–57	–48	–32	–22	–196	–209
Minimum tax relief for individuals	–122	–353	–256	....	....	....	–609	–609
Exceptions provided under Subpart F for certain active financing income	–864	–1,502	–630	....	....	....	–2,132	–2,132
Suspension of net income limitation on percentage depletion from marginal oil and gas wells	–25	–44	–18	....	....	....	–62	–62
Generalized System of Preferences (GSP) [5]	–370	–415	....	....	....	....	–415	–415
Authority to issue qualified zone academy bonds	–4	–13	–25	–35	–37	–37	–147	–332
Permanently extend expiring provisions:								
Provisions expiring in 2010:								
Marginal individual income tax rate reductions	....	....	....	....	....	....	....	–183,769
Child tax credit [6]	....	....	....	....	....	....	....	–31,697
Marriage penalty relief [7]	....	....	....	....	....	....	....	–12,976
Education incentives	–1	–5	–10	–15	–20	–26	–76	–2,810
Repeal of estate and generation-skipping transfer taxes, and modification of gift taxes	178	–550	–1,097	–1,485	–1,987	–2,178	–7,297	–103,659
Modifications of IRAs and pension plans	....	....	....	....	....	....	....	–6,490
Other incentives for families and children	....	....	....	....	....	....	....	–1,298
Research and experimentation (R&E) tax credit	....	....	–906	–2,949	–4,654	–5,623	–14,132	–51,051
Total effect of proposals	**–64,532**	**–73,017**	**–59,130**	**–27,927**	**–6,034**	**–9,433**	**–175,541**	**–591,020**

[1] Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is $27,000 million for 2002, $8,000 for 2003, $1,500 million for 2004, $9,500 million for 2003–2007, and $9,500 million for 2003–2012.

[2] Policy proposal with a receipt effect of zero.

[3] Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is $165 million for 2003, $449 million for 2004, $699 million for 2005, $975 million for 2006, $1,213 million for 2007, $3,501 million for 2003–2007, and $4,155 million for 2003–2012.

[4] Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is $667 million for 2003, $5,185 million for 2004, $6,292 million for 2005, $6,560 million for 2006, $6,441 million for 2007, $25,145 million for 2003–2007, and $59,873 million for 2003–2012.

[5] Net of income offsets.

[6] Affects both receipts and outlays. Only the receipt effect is shown here. The outlays effect is $8,745 million for 2003–2012.

[7] Affects both receipts and outlays. Only the receipt effect is shown here. The outlays effect is $1,527 million for 2003–2012,

Table 4–4. RECEIPTS BY SOURCE

(In millions of dollars)

Source	2001 Actual	Estimate 2002	2003	2004	2005	2006	2007
Individual income taxes (federal funds):							
Existing law	994,339	949,885	1,009,047	1,063,560	1,119,913	1,167,409	1,233,065
Proposed Legislation (PAYGO)	....	–646	–2,693	–4,966	–7,904	–10,133	–11,378
Total individual income taxes	**994,339**	**949,239**	**1,006,354**	**1,058,594**	**1,112,009**	**1,157,276**	**1,221,687**
Corporation income taxes:							
Federal funds:							
Existing law	151,071	202,547	207,960	215,170	241,952	248,397	258,890
Proposed Legislation (PAYGO)	....	–1,102	–2,471	–3,182	–4,865	–6,949	–8,275
Total Federal funds corporation income taxes	151,071	201,445	205,489	211,988	237,087	241,448	250,615
Trust funds:							
Hazardous substance superfund	4	....	....	....	....	....	....
Total corporation income taxes	**151,075**	**201,445**	**205,489**	**211,988**	**237,087**	**241,448**	**250,615**
Social insurance and retirement receipts (trust funds):							
Employment and general retirement:							
Old-age and survivors insurance (Off-budget)	434,057	442,131	466,185	490,228	519,907	541,680	568,723
Disability insurance (Off-budget)	73,462	75,067	79,158	83,244	88,286	91,984	96,576
Hospital insurance	149,651	151,677	159,310	167,667	178,255	185,997	195,448
Railroad retirement:							
Social Security equivalent account	1,614	1,704	1,721	1,749	1,771	1,795	1,818
Rail pension and supplemental annuity	2,658	2,556	2,412	2,307	2,299	2,332	2,366
Total employment and general retirement	661,442	673,135	708,786	745,195	790,518	823,788	864,931
On-budget	153,923	155,937	163,443	171,723	182,325	190,124	199,632
Off-budget	507,519	517,198	545,343	573,472	608,193	633,664	665,299
Unemployment insurance:							
Deposits by States [1]	20,824	23,254	29,887	34,564	36,363	36,744	36,914
Proposed Legislation (PAYGO)	....	....	–1	–5	–462	63	–289
Federal unemployment receipts [1]	6,937	6,934	7,065	7,237	7,410	7,580	7,749
Proposed Legislation (PAYGO)	....	....	–1,252	–1,809	–3,165	–3,790	–5,247
Railroad unemployment receipts [1]	51	100	150	156	120	94	103
Total unemployment insurance	27,812	30,288	35,849	40,143	40,266	40,691	39,230
Other retirement:							
Federal employees' retirement—employee share	4,647	4,550	4,527	4,424	4,337	4,221	4,068
Non-Federal employees retirement [2]	66	62	50	46	42	39	36
Total other retirement	4,713	4,612	4,577	4,470	4,379	4,260	4,104
Total social insurance and retirement receipts	**693,967**	**708,035**	**749,212**	**789,808**	**835,163**	**868,739**	**908,265**
On-budget	186,448	190,837	203,869	216,336	226,970	235,075	242,966
Off-budget	507,519	517,198	545,343	573,472	608,193	633,664	665,299
Excise taxes:							
Federal funds:							
Alcohol taxes	7,624	7,627	7,664	7,748	7,831	7,877	7,923
Tobacco taxes	7,396	8,045	8,115	7,974	7,875	7,782	7,692
Transportation fuels tax	1,150	1,138	1,180	1,216	1,266	304	312
Telephone and teletype services	5,769	5,984	6,345	6,753	7,179	7,612	8,050
Ozone depleting chemicals and products	32	22	13	7	....	....	....
Other Federal fund excise taxes	2,151	1,963	1,867	1,854	1,911	1,976	2,030
Proposed Legislation (PAYGO)	....	–122	–177	–181	–189	–198	–205
Total Federal fund excise taxes	24,122	24,657	25,007	25,371	25,873	25,353	25,802
Trust funds:							
Highway	31,469	31,926	32,952	34,121	35,414	36,919	38,038
Proposed Legislation (PAYGO)	....	....	....	–7	–17	–29	–38

Table 4–4. RECEIPTS BY SOURCE—Continued

(In millions of dollars)

Source	2001 Actual	Estimate					
		2002	2003	2004	2005	2006	2007
Airport and airway	9,191	8,939	9,680	10,269	10,878	11,518	12,178
Aquatic resources	358	385	393	414	424	435	443
Black lung disability insurance	522	554	573	597	616	628	638
Inland waterway	113	97	98	98	99	100	101
Hazardous substance superfund	2	....	....	....	....	....	....
Vaccine injury compensation	112	123	125	125	127	128	129
Leaking underground storage tank	179	190	193	199	204	214	218
Total trust funds excise taxes	41,946	42,214	44,014	45,816	47,745	49,913	51,707
Total excise taxes	**66,068**	**66,871**	**69,021**	**71,187**	**73,618**	**75,266**	**77,509**
Estate and gift taxes:							
Federal funds	28,400	27,484	23,559	27,638	24,769	28,121	24,992
Proposed Legislation (PAYGO)	....	6	–560	–1,050	–1,343	–1,736	–1,794
Total estate and gift taxes	**28,400**	**27,490**	**22,999**	**26,588**	**23,426**	**26,385**	**23,198**
Customs duties:							
Federal funds	18,583	18,538	19,781	21,424	22,549	23,964	25,283
Proposed Legislation (PAYGO)	....	–668	–863	–430	–482	–262	–207
Trust funds	786	796	887	905	977	1,041	1,075
Total customs duties	**19,369**	**18,666**	**19,805**	**21,899**	**23,044**	**24,743**	**26,151**
MISCELLANEOUS RECEIPTS: [3]							
Miscellaneous taxes	94	109	111	113	115	117	119
United Mine Workers of America combined benefit fund	150	143	138	132	127	123	117
Deposit of earnings, Federal Reserve System	26,124	25,596	29,025	31,512	32,084	33,214	34,832
Defense cooperation	7	6	6	6	6	6	6
Fees for permits and regulatory and judicial services	8,483	7,905	8,463	8,650	8,478	8,607	8,794
Fines, penalties, and forfeitures	2,724	2,685	2,523	2,509	2,517	2,525	2,534
Gifts and contributions	284	244	219	185	186	179	180
Refunds and recoveries	–54	–298	–305	–317	–325	–327	–335
Total miscellaneous receipts	**37,812**	**36,390**	**40,180**	**42,790**	**43,188**	**44,444**	**46,247**
Proposed bipartisan economic security plan (PAYGO)	....	–62,000	–65,000	–47,500	–9,500	17,000	18,000
Total budget receipts	**1,991,030**	**1,946,136**	**2,048,060**	**2,175,354**	**2,338,035**	**2,455,301**	**2,571,672**
On-budget	1,483,511	1,428,938	1,502,717	1,601,882	1,729,842	1,821,637	1,906,373
Off-budget	507,519	517,198	545,343	573,472	608,193	633,664	665,299
MEMORANDUM							
Federal funds	1,255,504	1,195,158	1,255,629	1,338,515	1,453,879	1,535,377	1,610,437
Trust funds	445,470	465,179	497,771	518,623	542,161	564,491	587,613
Interfund transactions	–217,463	–231,399	–250,683	–255,256	–266,198	–278,231	–291,677
Total on-budget	**1,483,511**	**1,428,938**	**1,502,717**	**1,601,882**	**1,729,842**	**1,821,637**	**1,906,373**
Off-budget (trust funds)	**507,519**	**517,198**	**545,343**	**573,472**	**608,193**	**633,664**	**665,299**
Total	**1,991,030**	**1,946,136**	**2,048,060**	**2,175,354**	**2,338,035**	**2,455,301**	**2,571,672**

[1] Deposits by States cover the benefit part of the program. Federal unemployment receipts cover administrative costs at both the Federal and State levels. Railroad unemployment receipts cover both the benefits and adminstrative costs of the program for the railroads.

[2] Represents employer and employee contributions to the civil service retirement and disability fund for covered employees of Government-sponsored, privately owned enterprises and the District of Columbia municipal government.

[3] Includes both Federal and trust funds.