

14. TAX EXPENDITURES

The Congressional Budget Act of 1974 (Public Law 93–344) requires that a list of “tax expenditures” be included in the budget. Tax expenditures are defined in the law as “revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability.” These exceptions may be viewed as alternatives to other policy instruments, such as spending or regulatory programs.

Identification and measurement of tax expenditures depends crucially on the baseline tax system against which the actual tax system is compared. The tax expenditure estimates presented in this chapter are patterned on a comprehensive income tax, which defines income as the sum of consumption and the change in net wealth in a given period of time.

An important assumption underlying each tax expenditure estimate reported below is that other parts of the

Tax Code remain unchanged. The estimates would be different if tax expenditures were changed simultaneously because of potential interactions among provisions. For that reason, this chapter does not present a grand total for the estimated tax expenditures.

Tax expenditures relating to the individual and corporate income taxes are estimated for fiscal years 2013–2019 using two methods of accounting: current revenue effects and present value effects. The present value approach provides estimates of the revenue effects for tax expenditures that generally involve deferrals of tax payments into the future.

A discussion of performance measures and economic effects related to the assessment of the effect of tax expenditures on the achievement of program performance goals is presented in Appendix A. This section is a complement to the Government-wide performance plan required by the Government Performance and Results Act of 1993.

TAX EXPENDITURES IN THE INCOME TAX

Tax Expenditure Estimates

All tax expenditure estimates presented here are based upon current tax law enacted as of December 31, 2013. In most cases, expired or repealed provisions are not listed if their revenue effects result only from taxpayer activity occurring before fiscal year 2013. The estimates are based on the economic assumptions from the Mid-Session Review of the 2014 Budget (except for health tax expenditures which are updated using assumptions in the February FY15 Budget.) The estimates reflect the “American Taxpayer Relief Act of 2012” (ATRA), enacted into law on January 2, 2013, which extended many tax expenditures, changed income tax rates, and provided Alternative Minimum Tax relief.

The total revenue effects for tax expenditures for fiscal years 2013–2019 are displayed according to the Budget’s functional categories in Table 14–1. Descriptions of the specific tax expenditure provisions follow the tables of estimates and the discussion of general features of the tax expenditure concept.

Two baseline concepts—the normal tax baseline and the reference tax law baseline—are used to identify and estimate tax expenditures.¹ For the most part, the two concepts coincide. However, items treated as tax expendi-

tures under the normal tax baseline, but not the reference tax law baseline, are indicated by the designation “normal tax method” in the tables. The revenue effects for these items are zero using the reference tax rules. The alternative baseline concepts are discussed in detail following the tables.

Table 14–2 reports separately the respective portions of the total revenue effects that arise under the individual and corporate income taxes separately. The location of the estimates under the individual and corporate headings does not imply that these categories of filers benefit from the special tax provisions in proportion to the respective tax expenditure amounts shown. Rather, these breakdowns show the form of tax liability that the various provisions affect. The ultimate beneficiaries of corporate tax expenditures could be shareholders, employees, customers, or other providers of capital, depending on economic forces.

Table 14–3 ranks the major tax expenditures by the size of their 2015–2019 revenue effect. The first column provides the number of the provision in order to cross reference this table to Tables 14–1 through 14–3, as well as to the descriptions below.

Interpreting Tax Expenditure Estimates

The estimates shown for individual tax expenditures in Tables 14–1, 14–2, and 14–3 do not necessarily equal the increase in Federal revenues (or the change in the budget

¹ These baseline concepts are thoroughly discussed in Special Analysis G of the 1985 Budget, where the former is referred to as the pre-1983 method and the latter the post-1982 method.

balance) that would result from repealing these special provisions, for the following reasons.

First, eliminating a tax expenditure may have incentive effects that alter economic behavior. These incentives can affect the resulting magnitudes of the activity or of other tax provisions or Government programs. For example, if capital gains were taxed at ordinary rates, capital gain realizations would be expected to decline, resulting in lower tax receipts. Such behavioral effects are not reflected in the estimates.

Second, tax expenditures are interdependent even without incentive effects. Repeal of a tax expenditure provision can increase or decrease the tax revenues associated with other provisions. For example, even if behavior does not change, repeal of an itemized deduction could increase the revenue costs from other deductions because some taxpayers would be moved into higher tax brackets. Alternatively, repeal of an itemized deduction could lower the revenue cost from other deductions if taxpayers are led to claim the standard deduction instead of itemizing. Similarly, if two provisions were repealed simultaneously, the increase in tax liability could be greater or less than the sum of the two separate tax expenditures, because each is estimated assuming that the other remains in force. In addition, the estimates reported in Table 14–1 are the totals of individual and corporate income tax revenue effects reported in Table 14–2 and do not reflect any possible interactions between individual and corporate income tax receipts. For this reason, the estimates in Table 14–1 should be regarded as approximations.

Present-Value Estimates

The annual value of tax expenditures for tax deferrals is reported on a cash basis in all tables except Table 14–4. Cash-based estimates reflect the difference between taxes deferred in the current year and incoming revenues that are received due to deferrals of taxes from prior years. Although such estimates are useful as a measure of cash flows into the Government, they do not accurately reflect the true economic cost of these provisions. For example, for a provision where activity levels have changed, so that incoming tax receipts from past deferrals are greater than deferred receipts from new activity, the cash-basis tax expenditure estimate can be negative, despite the fact that in present-value terms current deferrals have a real cost to the Government. Alternatively, in the case of a newly enacted deferral provision, a cash-based estimate can overstate the real effect on receipts to the Government because the newly deferred taxes will ultimately be received.

Discounted present-value estimates of revenue effects are presented in Table 14–4 for certain provisions that involve tax deferrals or other long-term revenue effects. These estimates complement the cash-based tax expenditure estimates presented in the other tables.

The present-value estimates represent the revenue effects, net of future tax payments, that follow from activities undertaken during calendar year 2013 which cause the deferrals or other long-term revenue effects. For instance, a pension contribution in 2013 would cause a de-

ferral of tax payments on wages in 2013 and on pension fund earnings on this contribution (e.g., interest) in later years. In some future year, however, the 2013 pension contribution and accrued earnings will be paid out and taxes will be due; these receipts are included in the present-value estimate. In general, this conceptual approach is similar to the one used for reporting the budgetary effects of credit programs, where direct loans and guarantees in a given year affect future cash flows.

Tax Expenditure Baselines

A tax expenditure is an exception to baseline provisions of the tax structure that usually results in a reduction in the amount of tax owed. The 1974 Congressional Budget Act, which mandated the tax expenditure budget, did not specify the baseline provisions of the tax law. As noted previously, deciding whether provisions are exceptions, therefore, is a matter of judgment. As in prior years, most of this year's tax expenditure estimates are presented using two baselines: the normal tax baseline and the reference tax law baseline. Tax expenditures may take the form of credits, deductions, special exceptions and allowances, and reduce tax liability below the level implied by the baseline tax system.

The normal tax baseline is patterned on a practical variant of a comprehensive income tax, which defines income as the sum of consumption and the change in net wealth in a given period of time. The normal tax baseline allows personal exemptions, a standard deduction, and deduction of expenses incurred in earning income. It is not limited to a particular structure of tax rates, or by a specific definition of the taxpaying unit.

The reference tax law baseline is also patterned on a comprehensive income tax, but it is closer to existing law. Reference law tax expenditures are limited to special exceptions from a generally provided tax rule that serve programmatic functions in a way that is analogous to spending programs. Provisions under the reference law baseline are generally tax expenditures under the normal tax baseline, but the reverse is not always true.

Both the normal and reference tax baselines allow several major departures from a pure comprehensive income tax. For example, under the normal and reference tax baselines:

- Income is taxable only when it is realized in exchange. Thus, the deferral of tax on unrealized capital gains is not regarded as a tax expenditure. Accrued income would be taxed under a comprehensive income tax.
- There is a separate corporate income tax.
- Noncorporate tax rates vary by level of income.
- Individual tax rates, including brackets, standard deduction, and personal exemptions, are allowed to vary with marital status.
- Values of assets and debt are not generally adjusted for inflation. A comprehensive income tax would

Table 14–1. ESTIMATES OF TOTAL INCOME TAX EXPENDITURES FOR FISCAL YEARS 2013–2019

(In millions of dollars)

	Total from corporations and individuals							
	2013	2014	2015	2016	2017	2018	2019	2015–19
National Defense								
1 Exclusion of benefits and allowances to armed forces personnel	11,620	12,620	13,230	12,200	12,310	12,730	13,240	63,710
International affairs:								
2 Exclusion of income earned abroad by U.S. citizens	4,410	4,310	4,350	4,470	4,730	4,990	5,200	23,740
3 Exclusion of certain allowances for Federal employees abroad	1,100	1,160	1,220	1,280	1,340	1,410	1,480	6,730
4 Inventory property sales source rules exception	3,320	3,600	3,890	4,220	4,560	4,940	5,352	22,962
5 Deferral of income from controlled foreign corporations (normal tax method)	63,440	72,740	75,540	76,380	76,260	73,970	71,060	373,210
6 Deferred taxes for financial firms on certain income earned overseas	6,660	2,700	0	0	0	0	0	0
General science, space, and technology:								
7 Expensing of research and experimentation expenditures (normal tax method)	5,840	5,160	4,800	5,450	6,230	6,930	7,270	30,680
8 Credit for increasing research activities	8,430	5,420	3,170	2,860	2,570	2,300	2,030	12,930
Energy:								
9 Expensing of exploration and development costs, fuels	550	510	510	590	600	550	520	2,770
10 Excess of percentage over cost depletion, fuels	530	670	780	920	1,070	1,230	1,390	5,390
11 Alternative fuel production credit	10	0	0	0	0	0	0	0
12 Exception from passive loss limitation for working interests in oil and gas properties	20	20	20	20	20	20	20	100
13 Capital gains treatment of royalties on coal	90	80	90	110	120	120	130	570
14 Exclusion of interest on energy facility bonds	20	30	30	30	30	30	30	150
15 Energy production credit ¹	1,670	2,370	3,000	3,330	3,370	3,210	3,130	16,040
16 Energy investment credit ¹	1,950	1,840	1,470	1,380	850	220	–20	3,900
17 Alcohol fuel credits ²	40	10	10	0	0	0	0	10
18 Bio-Diesel and small agri-biodiesel producer tax credits ³	20	20	0	0	0	0	0	0
19 Tax credits for clean-fuel burning vehicles	270	440	670	680	650	400	150	2,550
20 Exclusion of utility conservation subsidies	340	340	340	340	320	320	320	1,640
21 Credit for holding clean renewable energy bonds ⁴	70	70	70	70	70	70	70	350
22 Deferral of gain from dispositions of transmission property to implement FERC restructuring policy	0	–60	–220	–220	–200	–170	–140	–950
23 Credit for investment in clean coal facilities	180	200	140	40	20	–10	–10	180
24 Temporary 50% expensing for equipment used in the refining of liquid fuels	600	–100	–700	–830	–870	–800	–660	–3,860
25 Natural gas distribution pipelines treated as 15-year property	100	100	100	110	110	120	120	560
26 Amortize all geological and geophysical expenditures over 2 years	100	110	130	130	120	100	100	580
27 Allowance of deduction for certain energy efficient commercial building property	70	40	20	0	0	–20	–20	–20
28 Credit for construction of new energy efficient homes	150	120	60	20	0	0	0	80
29 Credit for energy efficiency improvements to existing homes	610	0	0	0	0	0	0	0
30 Credit for energy efficient appliances	150	130	120	100	0	0	0	220
31 Credit for residential energy efficient property	960	1,060	1,170	1,300	540	0	0	3,010
32 Qualified energy conservation bonds ⁵	20	30	30	30	30	30	30	150
33 Advanced energy property credit	210	110	90	0	0	–10	–10	70
34 Advanced nuclear power production credit	0	0	0	0	210	470	590	1,270
Natural resources and environment:								
35 Expensing of exploration and development costs, nonfuel minerals	50	50	50	60	60	60	60	290
36 Excess of percentage over cost depletion, nonfuel minerals	580	590	590	600	610	620	640	3,060
37 Exclusion of interest on bonds for water, sewage, and hazardous waste facilities	450	490	560	630	690	730	790	3,400
38 Capital gains treatment of certain timber income	90	80	90	110	120	120	130	570
39 Expensing of multiperiod timber growing costs	280	300	300	320	330	340	360	1,650
40 Tax incentives for preservation of historic structures	570	580	600	610	620	630	640	3,100
41 Industrial CO ₂ capture and sequestration tax credit	80	80	80	130	250	120	0	580
42 Deduction for endangered species recovery expenditures	20	20	20	30	30	30	30	140
Agriculture:								
43 Expensing of certain capital outlays	90	100	100	110	110	120	120	560
44 Expensing of certain multiperiod production costs	140	140	140	140	150	150	160	740
45 Treatment of loans forgiven for solvent farmers	40	40	40	40	40	40	40	200

Table 14-1. ESTIMATES OF TOTAL INCOME TAX EXPENDITURES FOR FISCAL YEARS 2013–2019—Continued

(In millions of dollars)

		Total from corporations and individuals							
		2013	2014	2015	2016	2017	2018	2019	2015–19
46	Capital gains treatment of certain income	920	800	920	1,060	1,160	1,230	1,280	5,650
47	Income averaging for farmers	130	130	130	140	140	140	140	690
48	Deferral of gain on sale of farm refiners	20	20	20	20	20	20	20	100
49	Expensing of reforestation expenditures	70	70	70	80	80	90	100	420
Commerce and housing:									
Financial institutions and insurance:									
50	Exemption of credit union income	2,000	2,070	1,970	2,370	2,700	2,770	3,000	12,810
51	Exclusion of interest on life insurance savings	18,930	21,270	23,040	24,690	26,370	28,180	30,090	132,370
52	Special alternative tax on small property and casualty insurance companies	10	10	10	10	20	20	20	80
53	Tax exemption of certain insurance companies owned by tax-exempt organizations	600	660	690	730	760	790	830	3,800
54	Small life insurance company deduction	30	30	40	40	40	40	40	200
55	Exclusion of interest spread of financial institutions	210	1,260	1,840	1,940	2,030	2,130	2,230	10,170
Housing:									
56	Exclusion of interest on owner-occupied mortgage subsidy bonds	1,230	1,360	1,510	1,700	1,880	2,000	2,140	9,230
57	Exclusion of interest on rental housing bonds	1,000	1,090	1,230	1,390	1,520	1,640	1,750	7,530
58	Deductibility of mortgage interest on owner-occupied homes	69,020	70,370	73,910	79,830	89,150	100,600	112,840	456,330
59	Deductibility of State and local property tax on owner-occupied homes	29,290	31,740	33,880	36,570	39,600	42,730	45,770	198,550
60	Deferral of income from installment sales	1,140	1,330	1,470	1,630	1,760	1,860	1,950	8,670
61	Capital gains exclusion on home sales	34,270	52,250	56,510	61,110	66,090	71,480	77,300	332,490
62	Exclusion of net imputed rental income	72,440	76,220	79,810	83,470	87,900	92,570	97,488	441,238
63	Exception from passive loss rules for \$25,000 of rental loss	8,660	9,820	10,360	10,910	11,550	12,240	12,810	57,870
64	Credit for low-income housing investments	7,410	8,310	8,280	8,330	8,730	9,080	9,420	43,840
65	Accelerated depreciation on rental housing (normal tax method)	1,780	2,090	2,500	3,020	3,560	4,130	4,710	17,920
66	Discharge of mortgage indebtedness	3,360	870	0	0	0	0	0	0
Commerce:									
67	Discharge of business indebtedness	0	–60	–80	–80	–60	–20	20	–220
68	Exceptions from imputed interest rules	20	30	40	40	50	50	60	240
69	Treatment of qualified dividends	23,650	23,840	26,650	28,580	30,040	31,290	32,390	148,950
70	Capital gains (except agriculture, timber, iron ore, and coal)	68,860	60,030	68,850	79,300	86,950	91,550	95,620	422,270
71	Capital gains exclusion of small corporation stock	140	340	480	640	850	1,000	1,010	3,980
72	Step-up basis of capital gains at death	23,050	30,780	32,370	34,010	35,750	37,600	39,580	179,310
73	Carryover basis of capital gains on gifts	2,870	2,290	2,560	2,810	3,060	3,260	3,400	15,090
74	Ordinary income treatment of loss from small business corporation stock sale	60	60	60	60	60	60	60	300
75	Accelerated depreciation of buildings other than rental housing (normal tax method)	–7,650	–7,570	–7,540	–7,690	–7,970	–8,350	–8,990	–40,540
76	Accelerated depreciation of machinery and equipment (normal tax method)	48,460	15,300	15,470	35,640	52,860	69,300	84,420	257,690
77	Expensing of certain small investments (normal tax method)	3,950	–1,180	–2,040	–570	380	1,080	1,570	420
78	Graduated corporation income tax rate (normal tax method)	4,300	4,200	4,130	4,100	4,220	4,200	4,370	21,020
79	Exclusion of interest on small issue bonds	170	190	210	230	250	280	290	1,260
80	Deduction for US production activities	12,860	13,790	14,480	15,200	15,840	16,820	16,150	78,490
81	Special rules for certain film and TV production	290	207	120	80	40	10	0	250
Transportation:									
82	Tonnage tax	60	70	70	70	80	80	90	520
83	Deferral of tax on shipping companies	20	20	20	20	20	20	20	100
84	Exclusion of reimbursed employee parking expenses	2,580	2,670	2,780	2,900	3,010	3,110	3,220	15,020
85	Exclusion for employer-provided transit passes	710	710	710	770	810	860	920	4,070
86	Tax credit for certain expenditures for maintaining railroad tracks	120	60	0	0	0	0	0	0
87	Exclusion of interest on bonds for Highway Projects and rail-truck transfer facilities	240	230	220	210	200	190	170	990
Community and regional development:									
88	Investment credit for rehabilitation of structures (other than historic)	30	30	30	30	30	30	30	150
89	Exclusion of interest for airport, dock, and similar bonds	740	820	920	1,030	1,130	1,210	1,300	5,590
90	Exemption of certain mutuals' and cooperatives' income	110	120	120	120	130	130	130	630
91	Empowerment zones, the DC enterprise zone, and renewal communities	450	350	200	190	190	180	150	910

Table 14-1. ESTIMATES OF TOTAL INCOME TAX EXPENDITURES FOR FISCAL YEARS 2013–2019—Continued
(In millions of dollars)

		Total from corporations and individuals							
		2013	2014	2015	2016	2017	2018	2019	2015–19
92	New markets tax credit	950	1,010	1,040	1,050	960	750	560	4,360
93	Expensing of environmental remediation costs	–180	–180	–170	–160	–160	–160	–160	–810
94	Credit to holders of Gulf Tax Credit Bonds	220	240	280	310	340	360	390	1,680
95	Recovery Zone Bonds ⁶	120	130	150	160	180	190	210	890
96	Tribal Economic Development Bonds	20	40	40	60	60	60	60	280
Education, training, employment, and social services:									
Education:									
97	Exclusion of scholarship and fellowship income (normal tax method)	2,890	2,980	3,090	3,200	3,310	3,420	3,550	16,570
98	HOPE tax credit	0	0	0	0	0	720	7,230	7,950
99	Lifetime Learning tax credit	1,810	1,680	1,720	1,740	1,740	1,880	3,100	10,180
100	American Opportunity Tax Credit ⁷	12,540	15,530	15,240	15,310	15,370	13,760	0	59,680
101	Education Individual Retirement Accounts	70	80	100	110	120	130	150	610
102	Deductibility of student-loan interest	1,720	1,720	1,780	1,780	1,790	1,790	1,840	8,980
103	Deduction for higher education expenses	600	560	0	0	0	0	0	0
104	Qualified tuition programs	1,680	1,770	1,900	2,050	2,200	2,350	2,520	11,020
105	Exclusion of interest on student-loan bonds	510	560	620	700	760	820	880	3,780
106	Exclusion of interest on bonds for private nonprofit educational facilities	2,240	2,480	2,760	3,120	3,430	3,660	3,930	16,900
107	Credit for holders of zone academy bonds ⁸	200	180	160	130	120	110	100	620
108	Exclusion of interest on savings bonds redeemed to finance educational expenses ..	10	10	10	20	20	20	20	90
109	Parental personal exemption for students age 19 or over	5,200	5,320	5,400	5,490	5,570	5,660	5,760	27,880
110	Deductibility of charitable contributions (education)	4,550	5,040	5,370	5,810	6,290	6,780	7,290	31,540
111	Exclusion of employer-provided educational assistance	710	750	800	850	900	950	1,000	4,500
112	Special deduction for teacher expenses	190	170	0	0	0	0	0	0
113	Discharge of student loan indebtedness	90	90	90	90	100	100	100	480
114	Qualified school construction bonds ⁹	580	650	650	650	650	650	650	3,250
Training, employment, and social services:									
115	Work opportunity tax credit	900	880	460	250	200	170	130	1,210
116	Employer provided child care exclusion	880	920	970	1,040	1,110	1,170	1,240	5,530
117	Employer-provided child care credit	10	10	10	10	10	10	10	50
118	Assistance for adopted foster children	530	530	560	590	620	660	700	3,130
119	Adoption credit and exclusion ¹⁰	450	540	580	600	640	730	660	3,210
120	Exclusion of employee meals and lodging (other than military)	2,185	3,700	3,797	3,910	4,032	4,155	4,278	20,172
121	Child credit ¹¹	23,480	23,350	23,500	23,620	23,480	23,450	23,480	117,530
122	Credit for child and dependent care expenses	4,160	4,200	4,310	4,460	4,590	4,690	4,760	22,810
123	Credit for disabled access expenditures	30	30	30	30	30	40	40	170
124	Deductibility of charitable contributions, other than education and health	39,260	43,600	46,630	50,600	54,940	59,390	64,250	275,810
125	Exclusion of certain foster care payments	380	380	390	380	370	370	360	1,870
126	Exclusion of parsonage allowances	737	720	758	798	840	885	931	4,212
127	Indian employment credit	50	40	20	20	20	10	10	80
Health:									
128	Exclusion of employer contributions for medical insurance premiums and medical care ¹² ...	185,330	196,010	207,200	217,140	229,000	241,070	256,290	1,150,700
129	Self-employed medical insurance premiums	6,140	6,670	6,970	7,240	7,550	7,870	8,170	37,800
130	Medical Savings Accounts / Health Savings Accounts	3,110	3,900	4,890	6,110	7,630	9,440	11,720	39,790
131	Deductibility of medical expenses	8,010	8,090	8,560	8,910	8,840	9,370	10,510	46,190
132	Exclusion of interest on hospital construction bonds	3,430	3,790	4,210	4,740	5,220	5,570	5,970	25,710
133	Refundable Premium Assistance Tax Credit ¹³	0	0	–3,940	–4,060	–5,740	–6,290	–6,540	–26,570
134	Credit for employee health insurance expenses of small business ¹⁴	630	870	1,050	1,040	760	470	330	3,650
135	Deductibility of charitable contributions (health)	4,470	4,980	5,350	5,820	6,340	6,880	7,460	31,850
136	Tax credit for orphan drug research	1,040	1,260	1,520	1,830	2,210	2,660	3,210	11,430
137	Special Blue Cross/Blue Shield deduction	190	230	360	430	480	440	370	2,080
138	Tax credit for health insurance purchased by certain displaced and retired individuals ¹⁵	10	0	0	0	0	0	0	0
139	Distributions from retirement plans for premiums for health and long-term care insurance	320	360	400	440	460	480	500	2,280

Table 14-1. ESTIMATES OF TOTAL INCOME TAX EXPENDITURES FOR FISCAL YEARS 2013–2019—Continued

(In millions of dollars)

		Total from corporations and individuals							
		2013	2014	2015	2016	2017	2018	2019	2015–19
Income security:									
140	Exclusion of railroad retirement system benefits	380	370	360	350	320	300	270	1,600
141	Exclusion of workers' compensation benefits	10,090	10,310	10,500	10,640	10,790	10,950	11,100	53,980
142	Exclusion of public assistance benefits (normal tax method)	770	790	820	860	900	940	980	4,500
143	Exclusion of special benefits for disabled coal miners	30	30	30	20	20	20	20	110
144	Exclusion of military disability pensions	110	110	110	110	110	110	110	550
Net exclusion of pension contributions and earnings:									
145	Defined benefit employer plans	37,860	40,090	42,340	44,750	47,270	49,160	51,440	234,960
146	Defined contribution employer plans	50,670	59,380	61,050	77,020	88,740	92,770	94,820	414,400
147	Individual Retirement Accounts	19,310	17,450	17,480	18,540	19,630	20,650	21,720	98,020
148	Low and moderate income savers credit	1,190	1,200	1,210	1,260	1,300	1,280	1,300	6,350
149	Self-Employed plans	19,400	23,300	25,530	28,100	30,890	33,860	37,150	155,530
Exclusion of other employee benefits:									
150	Premiums on group term life insurance	1,910	1,940	1,980	2,030	2,080	2,130	2,180	10,400
151	Premiums on accident and disability insurance	310	310	310	320	320	330	330	1,610
152	Income of trusts to finance supplementary unemployment benefits	20	20	30	40	40	50	60	220
153	Special ESOP rules	1,650	1,730	1,810	1,910	2,000	2,090	2,200	10,010
154	Additional deduction for the blind	30	30	30	30	40	40	40	180
155	Additional deduction for the elderly	2,380	2,560	2,800	3,040	3,310	3,610	3,850	16,610
156	Tax credit for the elderly and disabled	10	10	10	10	10	10	10	50
157	Deductibility of casualty losses	310	340	360	380	400	420	430	1,990
158	Earned income tax credit ¹⁶	4,070	4,330	4,330	4,400	4,520	4,640	4,550	22,440
Social Security:									
Exclusion of social security benefits:									
159	Social Security benefits for retired workers	26,440	28,730	29,840	30,900	31,920	33,010	34,260	159,930
160	Social Security benefits for disabled workers	8,200	8,560	8,740	8,930	9,100	9,250	9,420	45,440
161	Social Security benefits for spouses, dependents and survivors	3,760	3,970	4,100	4,300	4,470	4,540	4,740	22,150
Veterans benefits and services:									
162	Exclusion of veterans death benefits and disability compensation	4,620	5,080	5,490	5,980	6,500	7,080	7,700	32,750
163	Exclusion of veterans pensions	410	430	450	470	480	490	510	2,400
164	Exclusion of GI bill benefits	980	1,110	1,160	1,240	1,320	1,410	1,500	6,630
165	Exclusion of interest on veterans housing bonds	10	10	20	20	30	30	30	130
General purpose fiscal assistance:									
166	Exclusion of interest on public purpose State and local bonds	28,440	31,450	35,010	39,420	43,400	46,340	49,660	213,830
167	Build America Bonds ¹⁷	0	0	0	0	0	0	0	0
168	Deductibility of nonbusiness State and local taxes other than on owner-occupied homes	44,020	46,710	49,290	53,450	58,120	62,800	67,140	290,800
Interest:									
169	Deferral of interest on U.S. savings bonds	1,020	1,080	1,090	1,100	1,120	1,130	1,140	5,580
Addendum: Aid to State and local governments:									
Deductibility of:									
	Property taxes on owner-occupied homes	29,290	31,740	33,880	36,570	39,600	42,730	45,770	198,550
	Nonbusiness State and local taxes other than on owner-occupied homes	44,020	46,710	49,290	53,450	58,120	62,800	67,140	290,800
Exclusion of interest on State and local bonds for:									
	Public purposes	28,440	31,450	35,010	39,420	43,400	46,340	49,660	213,830
	Energy facilities	20	30	30	30	30	30	30	150
	Water, sewage, and hazardous waste disposal facilities	450	490	560	630	690	730	790	3,400
	Small-issues	170	190	210	230	250	280	290	1,260
	Owner-occupied mortgage subsidies	1,230	1,360	1,510	1,700	1,880	2,000	2,140	9,230
	Rental housing	1,000	1,090	1,230	1,390	1,520	1,640	1,750	7,530
	Airports, docks, and similar facilities	740	820	920	1,030	1,130	1,210	1,300	5,590

(In millions of dollars)

		Total from corporations and individuals							
		2013	2014	2015	2016	2017	2018	2019	2015–19
	Student loans	510	560	620	700	760	820	880	3,780
	Private nonprofit educational facilities	2,240	2,480	2,760	3,120	3,430	3,660	3,930	16,900
	Hospital construction	3,430	3,790	4,210	4,740	5,220	5,570	5,970	25,710
	Veterans' housing	10	10	20	20	30	30	30	130

² In addition, the alcohol fuel mixture credit results in a reduction in excise tax receipts (in millions of dollars) as follows: 2013 \$0; 2014 \$0; 2015 \$0; 2016 \$0; 2017 \$0; 2018 \$0; 2019 \$0.

⁴ In addition, the provision has outlay effects of (in millions of dollars): 2013 \$40; 2014 \$50; 2015 \$50; 2016 \$50; 2017 \$50; 2018 \$50; 2019 \$50.

⁶In addition, recovery zone bonds have outlay effects (in millions of dollars) as follows: 2013 \$160, 2014 \$160, 2015 \$160, 2016 \$160, and 2017 \$160; 2018 \$160; 2019 \$160.

⁸ In addition, the credit for holders of zone academy bonds has outlay effects of (in millions of dollars): 2013 \$20; 2014 \$30; 2015 \$30; 2016 \$30; 2017 \$30; 2018 \$30; and 2019 \$30.

¹⁰The figures in the table indicate the effect of the adoption tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2013 \$0.

¹² The figures in the table indicate the effect on income taxes of the employer contributions for health. In addition, the effect on payroll tax receipts (in millions of dollars) is as follows: 2013 \$117,920; 2014 \$122,990; 2015 \$127,980; 2016 \$132,400; 2017 \$138,330; 2018 \$145,270; 2019 \$153,870.

¹⁴ In addition, the small business credit provision has outlay effects (in millions of dollars) as follows: 2013 \$80; 2014 \$100; 2015 \$110; 2016 \$120; 2017 \$110; 2018 \$70; 2019 \$50.

¹⁶The figures in the table indicate the effect of the earned income tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2013 \$56.760; 2014

The figures in the table indicate the effect of the earned income tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2010 \$50,700; 2014 \$58,430; 2015 \$58,070; 2016 \$58,360; 2017 \$59,500; 2018 \$60,900; and 2019 59,330.

¹⁷ In addition, Build America Bonds have outlay effects of (in millions of dollars): 2013 \$3,190; 2014 \$3,190; 2015 \$3,190; 2016 \$3,190; 2017 \$3,190; 2018 \$3,190; and 2019 \$3,190.

Note: Provisions with estimates denoted normal tax method have no revenue loss under the reference tax law method.

All estimates have been rounded to the nearest \$10 million. Provisions with estimates that rounded to zero in each year are not included in the table.

Table 14–2. ESTIMATES OF TAX EXPENDITURES FOR THE CORPORATE AND INDIVIDUAL INCOME TAXES FOR FISCAL YEARS 2013-2019

(In millions of dollars)

	Corporations								Individuals							
	2013	2014	2015	2016	2017	2018	2019	2015-19	2013	2014	2015	2016	2017	2018	2019	2015-19
National Defense																
1 Exclusion of benefits and allowances to armed forces personnel									11,620	12,620	13,230	12,200	12,310	12,730	13,240	63,710
International affairs:																
2 Exclusion of income earned abroad by U.S. citizens									4,410	4,310	4,350	4,470	4,730	4,990	5,200	23,740
3 Exclusion of certain allowances for Federal employees abroad									1,100	1,160	1,220	1,280	1,340	1,410	1,480	6,730
4 Inventory property sales source rules exception	3,320	3,600	3,890	4,220	4,560	4,940	5,352	22,962								
5 Deferral of income from controlled foreign corporations (normal tax method)	63,440	72,740	75,540	76,380	76,260	73,970	71,060	373,210								
6 Deferred taxes for financial firms on certain income earned overseas	6,660	2,700	0	0	0	0	0	0								
General science, space, and technology:																
7 Expensing of research and experimentation expenditures (normal tax method)	5,340	4,730	4,480	5,080	5,800	6,450	6,760	28,570	500	430	320	370	430	480	510	2,110
8 Credit for increasing research activities	7,910	5,150	3,040	2,740	2,460	2,200	1,940	12,380	520	270	130	120	110	100	90	550
Energy:																
9 Expensing of exploration and development costs, fuels	460	430	430	490	500	460	430	2,310	90	80	80	100	100	90	90	460
10 Excess of percentage over cost depletion, fuels	450	560	650	760	880	1,010	1,140	4,440	80	110	130	160	190	220	250	950
11 Alternative fuel production credit	10	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
12 Exception from passive loss limitation for working interests in oil and gas properties									20	20	20	20	20	20	20	100
13 Capital gains treatment of royalties on coal									90	80	90	110	120	120	130	570
14 Exclusion of interest on energy facility bonds	10	10	10	10	10	10	10	50	10	20	20	20	20	20	20	100
15 Energy production credit ¹	1,250	1,780	2,250	2,500	2,530	2,410	2,350	12,040	420	590	750	830	840	800	780	4,000
16 Energy investment credit ¹	1,560	1,470	1,180	1,100	680	180	-20	3,120	390	370	290	280	170	40	0	780
17 Alcohol fuel credits ²	10	0	0	0	0	0	0	0	30	10	10	0	0	0	0	10
18 Bio-Diesel and small agri-biodiesel producer tax credits ³	10	10	0	0	0	0	0	0	10	10	0	0	0	0	0	0
19 Tax credits for clean-fuel burning vehicles	60	100	120	130	100	50	20	420	210	340	550	550	550	350	130	2,130
20 Exclusion of utility conservation subsidies ...	20	20	20	20	10	10	10	70	320	320	320	320	310	310	310	1,570
21 Credit for holding clean renewable energy bonds ⁴	20	20	20	20	20	20	20	100	50	50	50	50	50	50	50	250
22 Deferral of gain from dispositions of transmission property to implement FERC restructuring policy		-60	-220	-220	-200	-170	-140	-950	0	0	0	0	0	0	0	0
23 Credit for investment in clean coal facilities	170	190	130	40	20	-10	-10	170	10	10	10	0	0	0	0	10
24 Temporary 50% expensing for equipment used in the refining of liquid fuels	600	-100	-700	-830	-870	-800	-660	-3,860	0	0	0	0	0	0	0	0
25 Natural gas distribution pipelines treated as 15-year property	100	100	100	110	110	120	120	560	0	0	0	0	0	0	0	0
26 Amortize all geological and geophysical expenditures over 2 years	80	80	100	100	90	80	80	450	20	30	30	30	30	20	20	130
27 Allowance of deduction for certain energy efficient commercial building property ...	30	20	10	0	0	-10	-10	-10	40	20	10	0	0	-10	-10	-10
28 Credit for construction of new energy efficient homes	50	40	20	10	0	0	0	30	100	80	40	10	0	0	0	50
29 Credit for energy efficiency improvements to existing homes									610	0	0	0	0	0	0	0
30 Credit for energy efficient appliances	150	130	120	100	0	0	0	220	0	0	0	0	0	0	0	0
31 Credit for residential energy efficient property	0	0	0	0	0	0	0	0	960	1,060	1,170	1,300	540	0	0	3,010
32 Qualified energy conservation bonds ⁵	10	10	10	10	10	10	10	50	10	20	20	20	20	20	20	100
33 Advanced Energy Property Credit	210	110	90	0	0	-10	-10	70	0	0	0	0	0	0	0	0
34 Advanced nuclear power production credit		0	0	0	160	350	440	950	0	0	0	0	50	120	150	320

**Table 14-2. ESTIMATES OF TAX EXPENDITURES FOR THE CORPORATE AND
INDIVIDUAL INCOME TAXES FOR FISCAL YEARS 2013-2019—Continued**
(In millions of dollars)

	Corporations								Individuals							
	2013	2014	2015	2016	2017	2018	2019	2015-19	2013	2014	2015	2016	2017	2018	2019	2015-19
Natural resources and environment:																
35 Expensing of exploration and development costs, nonfuel minerals	50	50	50	60	60	60	60	290	0	0	0	0	0	0	0	0
36 Excess of percentage over cost depletion, nonfuel minerals	540	540	550	560	570	580	590	2,850	40	50	40	40	40	40	50	210
37 Exclusion of interest on bonds for water, sewage, and hazardous waste facilities	140	120	160	200	230	230	240	1,060	310	370	400	430	460	500	550	2,340
38 Capital gains treatment of certain timber income									90	80	90	110	120	120	130	570
39 Expensing of multiperiod timber growing costs	170	180	180	190	200	210	230	1,010	110	120	120	130	130	130	130	640
40 Tax incentives for preservation of historic structures	490	500	510	520	530	540	550	2,650	80	80	90	90	90	90	90	450
41 Industrial CO2 capture and sequestration tax credit	80	80	80	130	250	120	0	580	0	0	0	0	0	0	0	0
42 Deduction for endangered species recovery expenditures	10	10	10	10	10	10	10	50	10	10	10	20	20	20	20	90
Agriculture:																
43 Expensing of certain capital outlays	10	10	10	10	10	10	10	50	80	90	90	100	100	110	110	510
44 Expensing of certain multiperiod production costs	10	10	10	10	10	10	10	50	130	130	130	130	140	140	150	690
45 Treatment of loans forgiven for solvent farmers									40	40	40	40	40	40	40	200
46 Capital gains treatment of certain income									920	800	920	1,060	1,160	1,230	1,280	5,650
47 Income averaging for farmers									130	130	130	140	140	140	140	690
48 Deferral of gain on sale of farm refiners	20	20	20	20	20	20	20	100	0	0	0	0	0	0	0	0
49 Expensing of reforestation expenditures	20	20	20	20	20	30	30	120	50	50	50	60	60	60	70	300
Commerce and housing:																
Financial institutions and insurance:																
50 Exemption of credit union income	2,000	2,070	1,970	2,370	2,700	2,770	3,000	12,810								
51 Exclusion of interest on life insurance savings	3,210	3,710	4,100	4,270	4,520	4,820	5,010	22,720	15,720	17,560	18,940	20,420	21,850	23,360	25,080	109,650
52 Special alternative tax on small property and casualty insurance companies ...	10	10	10	10	20	20	20	80								
53 Tax exemption of certain insurance companies owned by tax-exempt organizations	600	660	690	730	760	790	830	3,800								
54 Small life insurance company deduction	30	30	40	40	40	40	40	200								
55 Exclusion of interest spread of financial institutions	0	0	0	0	0	0	0	0	210	1,260	1,840	1,940	2,030	2,130	2,230	10,170
Housing:																
56 Exclusion of interest on owner-occupied mortgage subsidy bonds	380	340	430	540	620	630	650	2,870	850	1,020	1,080	1,160	1,260	1,370	1,490	6,360
57 Exclusion of interest on rental housing bonds	310	270	350	440	500	520	530	2,340	690	820	880	950	1,020	1,120	1,220	5,190
58 Deductibility of mortgage interest on owner-occupied homes									69,020	70,370	73,910	79,830	89,150	100,600	112,840	456,330
59 Deductibility of State and local property tax on owner-occupied homes									29,290	31,740	33,880	36,570	39,600	42,730	45,770	198,550
60 Deferral of income from installment sales									1,140	1,330	1,470	1,630	1,760	1,860	1,950	8,670
61 Capital gains exclusion on home sales ..									34,270	52,250	56,510	61,110	66,090	71,480	77,300	332,490
62 Exclusion of net imputed rental income ..									72,440	76,220	79,810	83,470	87,900	92,570	97,488	441,238
63 Exception from passive loss rules for \$25,000 of rental loss									8,660	9,820	10,360	10,910	11,550	12,240	12,810	57,870
64 Credit for low-income housing investments	7,040	7,890	7,870	7,910	8,290	8,630	8,950	41,650	370	420	410	420	440	450	470	2,190
65 Accelerated depreciation on rental housing (normal tax method)	300	340	410	500	600	710	830	3,050	1,480	1,750	2,090	2,520	2,960	3,420	3,880	14,870
66 Discharge of mortgage indebtedness									3,360	870	0	0	0	0	0	0

**Table 14-2. ESTIMATES OF TAX EXPENDITURES FOR THE CORPORATE AND
INDIVIDUAL INCOME TAXES FOR FISCAL YEARS 2013-2019—Continued**
(In millions of dollars)

		Corporations								Individuals							
		2013	2014	2015	2016	2017	2018	2019	2015-19	2013	2014	2015	2016	2017	2018	2019	2015-19
Commerce:																	
67	Discharge of business indebtedness									0	-60	-80	-80	-60	-20	20	-220
68	Exceptions from imputed interest rules									20	30	40	40	50	50	60	240
69	Treatment of qualified dividends									23,650	23,840	26,650	28,580	30,040	31,290	32,390	148,950
70	Capital gains (except agriculture, timber, iron ore, and coal)									68,860	60,030	68,850	79,300	86,950	91,550	95,620	422,270
71	Capital gains exclusion of small corporation stock									140	340	480	640	850	1,000	1,010	3,980
72	Step-up basis of capital gains at death ...									23,050	30,780	32,370	34,010	35,750	37,600	39,580	179,310
73	Carryover basis of capital gains on gifts ...									2,870	2,290	2,560	2,810	3,060	3,260	3,400	15,090
74	Ordinary income treatment of loss from small business corporation stock sale									60	60	60	60	60	60	60	300
75	Accelerated depreciation of buildings other than rental housing (normal tax method)	-3,450	-3,340	-3,340	-3,440	-3,610	-3,840	-4,230	-18,460	-4,200	-4,230	-4,200	-4,250	-4,360	-4,510	-4,760	-22,080
76	Accelerated depreciation of machinery and equipment (normal tax method) ..	32,680	8,330	8,090	22,270	34,580	46,660	58,110	169,710	15,780	6,970	7,380	13,370	18,280	22,640	26,310	87,980
77	Expensing of certain small investments (normal tax method)	570	-260	-390	-160	-10	110	200	-250	3,380	-920	-1,650	-410	390	970	1,370	670
78	Graduated corporation income tax rate (normal tax method)	4,300	4,200	4,130	4,100	4,220	4,200	4,370	21,020								
79	Exclusion of interest on small issue bonds	50	50	60	70	80	90	90	390	120	140	150	160	170	190	200	870
80	Deduction for US production activities	9,730	10,430	10,950	11,500	11,980	12,720	12,220	59,370	3,130	3,360	3,530	3,700	3,860	4,100	3,930	19,120
81	Special rules for certain film and TV production	230	167	100	60	30	10	0	200	60	40	20	20	10	0	0	50
Transportation:																	
82	Tonnage tax	60	70	70	70	80	80	90	520								
83	Deferral of tax on shipping companies	20	20	20	20	20	20	20	100								
84	Exclusion of reimbursed employee parking expenses									2,580	2,670	2,780	2,900	3,010	3,110	3,220	15,020
85	Exclusion for employer-provided transit passes									710	710	710	770	810	860	920	4,070
86	Tax credit for certain expenditures for maintaining railroad tracks	100	50	0	0	0	0	0	0	20	10	0	0	0	0	0	0
87	Exclusion of interest on bonds for Highway Projects and rail-truck transfer facilities .	60	60	50	50	50	50	40	240	180	170	170	160	150	140	130	750
Community and regional development:																	
88	Investment credit for rehabilitation of structures (other than historic)	10	10	10	10	10	10	10	50	20	20	20	20	20	20	20	100
89	Exclusion of interest for airport, dock, and similar bonds	230	200	260	330	370	380	400	1,740	510	620	660	700	760	830	900	3,850
90	Exemption of certain mutuals' and cooperatives' income	110	120	120	120	130	130	130	630								
91	Empowerment zones, the DC enterprise zone, and renewal communities	180	100	50	50	50	50	40	240	270	250	150	140	140	130	110	670
92	New markets tax credit	930	990	1,020	1,030	940	730	550	4,270	20	20	20	20	20	20	10	90
93	Expensing of environmental remediation costs	-150	-150	-140	-130	-130	-130	-130	-660	-30	-30	-30	-30	-30	-30	-30	-150
94	Credit to holders of Gulf Tax Credit Bonds. ...	70	60	80	100	110	110	120	520	150	180	200	210	230	250	270	1,160
95	Recovery Zone Bonds ⁶	40	30	40	50	60	60	60	270	80	100	110	110	120	130	150	620
96	Tribal Economic Development Bonds	10	10	10	20	20	20	20	90	10	30	30	40	40	40	40	190
Education, training, employment, and social services:																	
Education:																	
97	Exclusion of scholarship and fellowship income (normal tax method)									2,890	2,980	3,090	3,200	3,310	3,420	3,550	16,570
98	HOPE tax credit									0	0	0	0	0	720	7,230	7,950
99	Lifetime Learning tax credit									1,810	1,680	1,720	1,740	1,740	1,880	3,100	10,180
100	American Opportunity Tax Credit ⁷									12,540	15,530	15,240	15,310	15,370	13,760	0	59,680

**Table 14-2. ESTIMATES OF TAX EXPENDITURES FOR THE CORPORATE AND
INDIVIDUAL INCOME TAXES FOR FISCAL YEARS 2013-2019—Continued**
(In millions of dollars)

		Corporations								Individuals							
		2013	2014	2015	2016	2017	2018	2019	2015-19	2013	2014	2015	2016	2017	2018	2019	2015-19
101	Education Individual Retirement Accounts									70	80	100	110	120	130	150	610
102	Deductibility of student-loan interest									1,720	1,720	1,780	1,780	1,790	1,790	1,840	8,980
103	Deduction for higher education expenses									600	560	0	0	0	0	0	0
104	Qualified tuition programs									1,680	1,770	1,900	2,050	2,200	2,350	2,520	11,020
105	Exclusion of interest on student-loan bonds	160	140	180	220	250	260	270	1,180	350	420	440	480	510	560	610	2,600
106	Exclusion of interest on bonds for private nonprofit educational facilities	690	610	780	990	1,130	1,160	1,200	5,260	1,550	1,870	1,980	2,130	2,300	2,500	2,730	11,640
107	Credit for holders of zone academy bonds ⁸	200	180	160	130	120	110	100	620								
108	Exclusion of interest on savings bonds redeemed to finance educational expenses									10	10	10	20	20	20	20	90
109	Parental personal exemption for students age 19 or over									5,200	5,320	5,400	5,490	5,570	5,660	5,760	27,880
110	Deductibility of charitable contributions (education)	730	780	830	870	920	960	990	4,570	3,820	4,260	4,540	4,940	5,370	5,820	6,300	26,970
111	Exclusion of employer-provided educational assistance									710	750	800	850	900	950	1,000	4,500
112	Special deduction for teacher expenses ...									190	170	0	0	0	0	0	0
113	Discharge of student loan indebtedness									90	90	90	90	100	100	100	480
114	Qualified school construction bonds ⁹	150	160	160	160	160	160	160	800	430	490	490	490	490	490	490	2,450
Training, employment, and social services:																	
115	Work opportunity tax credit	670	610	300	160	130	110	80	780	230	270	160	90	70	60	50	430
116	Employer provided child care exclusion ...									880	920	970	1,040	1,110	1,170	1,240	5,530
117	Employer-provided child care credit	10	10	10	10	10	10	10	50								
118	Assistance for adopted foster children									530	530	560	590	620	660	700	3,130
119	Adoption credit and exclusion ¹⁰									450	540	580	600	640	730	660	3,210
120	Exclusion of employee meals and lodging (other than military)									2,185	3,700	3,797	3,910	4,032	4,155	4,278	20,172
121	Child credit ¹¹									23,480	23,350	23,500	23,620	23,480	23,450	23,480	117,530
122	Credit for child and dependent care expenses									4,160	4,200	4,310	4,460	4,590	4,690	4,760	22,810
123	Credit for disabled access expenditures ...	10	10	10	10	10	20	20	70	20	20	20	20	20	20	20	100
124	Deductibility of charitable contributions, other than education and health	1,590	1,670	1,740	1,830	1,900	1,970	2,050	9,490	37,670	41,930	44,890	48,770	53,040	57,420	62,200	266,320
125	Exclusion of certain foster care payments									380	380	390	380	370	370	360	1,870
126	Exclusion of parsonage allowances									737	720	758	798	840	885	931	4,212
127	Indian employment credit	30	20	10	10	10	0	0	30	20	20	10	10	10	10	10	50
Health:																	
128	Exclusion of employer contributions for medical insurance premiums and medical care ¹²									185,330	196,010	207,200	217,140	229,000	241,070	256,290	1,150,700
129	Self-employed medical insurance premiums									6,140	6,670	6,970	7,240	7,550	7,870	8,170	37,800
130	Medical Savings Accounts / Health Savings Accounts									3,110	3,900	4,890	6,110	7,630	9,440	11,720	39,790
131	Deductibility of medical expenses									8,010	8,090	8,560	8,910	8,840	9,370	10,510	46,190
132	Exclusion of interest on hospital construction bonds	1,060	940	1,190	1,500	1,720	1,760	1,820	7,990	2,370	2,850	3,020	3,240	3,500	3,810	4,150	17,720
133	Refundable Premium Assistance Tax Credit ¹³									0	0	-3,940	-4,060	-5,740	-6,290	-6,540	-26,570
134	Credit for employee health insurance expenses of small business ¹⁴	190	280	460	470	430	250	170	1,780	440	590	590	570	330	220	160	1,870
135	Deductibility of charitable contributions (health)	210	230	240	250	260	280	300	1,330	4,260	4,750	5,110	5,570	6,080	6,600	7,160	30,520
136	Tax credit for orphan drug research	1,040	1,260	1,520	1,830	2,210	2,660	3,210	11,430								
137	Special Blue Cross/Blue Shield deduction .	190	230	360	430	480	440	370	2,080								

**Table 14-2. ESTIMATES OF TAX EXPENDITURES FOR THE CORPORATE AND
INDIVIDUAL INCOME TAXES FOR FISCAL YEARS 2013-2019—Continued**
(In millions of dollars)

		Corporations								Individuals							
		2013	2014	2015	2016	2017	2018	2019	2015-19	2013	2014	2015	2016	2017	2018	2019	2015-19
138	Tax credit for health insurance purchased by certain displaced and retired individuals ¹⁵									10	0	0	0	0	0	0	0
139	Distributions from retirement plans for premiums for health and long-term care insurance									320	360	400	440	460	480	500	2,280
Income security:																	
140	Exclusion of railroad retirement system benefits									380	370	360	350	320	300	270	1,600
141	Exclusion of workers' compensation benefits									10,090	10,310	10,500	10,640	10,790	10,950	11,100	53,980
142	Exclusion of public assistance benefits (normal tax method)									770	790	820	860	900	940	980	4,500
143	Exclusion of special benefits for disabled coal miners									30	30	30	20	20	20	20	110
144	Exclusion of military disability pensions									110	110	110	110	110	110	110	550
	Net exclusion of pension contributions and earnings:																
145	Defined benefit employer plans									37,860	40,090	42,340	44,750	47,270	49,160	51,440	234,960
146	Defined contribution employer plans									50,670	59,380	61,050	77,020	88,740	92,770	94,820	414,400
147	Individual Retirement Accounts									19,310	17,450	17,480	18,540	19,630	20,650	21,720	98,020
148	Low and moderate income savers credit ...									1,190	1,200	1,210	1,260	1,300	1,280	1,300	6,350
149	Self-Employed plans									19,400	23,300	25,530	28,100	30,890	33,860	37,150	155,530
	Exclusion of other employee benefits:																
150	Premiums on group term life insurance									1,910	1,940	1,980	2,030	2,080	2,130	2,180	10,400
151	Premiums on accident and disability insurance									310	310	310	320	320	330	330	1,610
152	Income of trusts to finance supplementary unemployment benefits									20	20	30	40	40	50	60	220
153	Special ESOP rules	1,550	1,630	1,710	1,800	1,890	1,980	2,080	9,460	100	100	100	110	110	110	120	550
154	Additional deduction for the blind									30	30	30	30	40	40	40	180
155	Additional deduction for the elderly									2,380	2,560	2,800	3,040	3,310	3,610	3,850	16,610
156	Tax credit for the elderly and disabled									10	10	10	10	10	10	10	50
157	Deductibility of casualty losses									310	340	360	380	400	420	430	1,990
158	Earned income tax credit ¹⁶									4,070	4,330	4,330	4,400	4,520	4,640	4,550	22,440
Social Security:																	
	Exclusion of social security benefits:																
159	Social Security benefits for retired workers									26,440	28,730	29,840	30,900	31,920	33,010	34,260	159,930
160	Social Security benefits for disabled workers									8,200	8,560	8,740	8,930	9,100	9,250	9,420	45,440
161	Social Security benefits for spouses, dependents and survivors									3,760	3,970	4,100	4,300	4,470	4,540	4,740	22,150
Veterans benefits and services:																	
162	Exclusion of veterans death benefits and disability compensation									4,620	5,080	5,490	5,980	6,500	7,080	7,700	32,750
163	Exclusion of veterans pensions									410	430	450	470	480	490	510	2,400
164	Exclusion of GI bill benefits									980	1,110	1,160	1,240	1,320	1,410	1,500	6,630
165	Exclusion of interest on veterans housing bonds	0	0	10	10	10	10	10	50	10	10	10	10	20	20	20	80
General purpose fiscal assistance:																	
166	Exclusion of interest on public purpose State and local bonds	8,780	7,780	9,930	12,490	14,330	14,640	15,140	66,530	19,660	23,670	25,080	26,930	29,070	31,700	34,520	147,300
167	Build America Bonds ¹⁷	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
168	Deductibility of nonbusiness State and local taxes other than on owner-occupied homes									44,020	46,710	49,290	53,450	58,120	62,800	67,140	290,800

Table 14-2. ESTIMATES OF TAX EXPENDITURES FOR THE CORPORATE AND INDIVIDUAL INCOME TAXES FOR FISCAL YEARS 2013-2019—Continued
(In millions of dollars)

	Corporations								Individuals							
	2013	2014	2015	2016	2017	2018	2019	2015-19	2013	2014	2015	2016	2017	2018	2019	2015-19
Interest:																
169 Deferral of interest on U.S. savings bonds ...									1,020	1,080	1,090	1,100	1,120	1,130	1,140	5,580
Addendum: Aid to State and local governments:																
Deductibility of:																
Property taxes on owner-occupied homes									29,290	31,740	33,880	36,570	39,600	42,730	45,770	198,550
Nonbusiness State and local taxes other than on owner-occupied homes									44,020	46,710	49,290	53,450	58,120	62,800	67,140	290,800
Exclusion of interest on State and local bonds for:																
Public purposes	8,780	7,780	9,930	12,490	14,330	14,640	15,140	66,530	19,660	23,670	25,080	26,930	29,070	31,700	34,520	147,300
Energy facilities	10	10	10	10	10	10	10	50	10	20	20	20	20	20	20	100
Water, sewage, and hazardous waste disposal facilities	140	120	160	200	230	230	240	1,060	310	370	400	430	460	500	550	2,340
Small-issues	50	50	60	70	80	90	90	390	120	140	150	160	170	190	200	870
Owner-occupied mortgage subsidies	380	340	430	540	620	630	650	2,870	850	1,020	1,080	1,160	1,260	1,370	1,490	6,360
Rental housing	310	270	350	440	500	520	530	2,340	690	820	880	950	1,020	1,120	1,220	5,190
Airports, docks, and similar facilities	230	200	260	330	370	380	400	1,740	510	620	660	700	760	830	900	3,850
Student loans	160	140	180	220	250	260	270	1,180	350	420	440	480	510	560	610	2,600
Private nonprofit educational facilities	690	610	780	990	1,130	1,160	1,200	5,260	1,550	1,870	1,980	2,130	2,300	2,500	2,730	11,640
Hospital construction	1,060	940	1,190	1,500	1,720	1,760	1,820	7,990	2,370	2,850	3,020	3,240	3,500	3,810	4,150	17,720
Veterans' housing	0	0	10	10	10	10	10	50	10	10	10	10	20	20	20	80

¹ Firms can tax an energy grant in lieu of the energy production credit or the energy investment credit for facilities placed in service in 2009 and 2010 or whose construction commenced in 2009 and 2010. The effect of the grant on outlays (in millions of dollars) is as follows: 2013 \$8,080; 2014 \$4,710; 2015 \$2,520; 2016 \$1,580; 2017 \$330; 2018 \$0; 2019 \$0.

² In addition, the alcohol fuel mixture credit results in a reduction in excise tax receipts (in millions of dollars) as follows: 2013 \$10; 2014 \$0; 2015 \$0; 2016 \$0; 2017 \$0; 2018 \$0; 2019 \$0. The alternative fuel mixture credit results in a reduction in excise tax receipts (in millions of dollars) as follows: 2013 \$350; 2014 \$200; 2015 \$0; 2016 \$0; 2017 \$0; 2018 \$0; 2019 \$0.

³ In addition, the biodiesel producer tax credit results in a reduction in excise tax receipts (in millions of dollars) as follows: 2013 \$1600; 2014 \$610; 2015 \$0; 2016 \$0; 2017 \$0; 2018: \$0; 2019 \$0.

⁴ In addition, the provision has outlay effects of (in millions of dollars): 2013 \$40; 2014 \$50; 2015 \$50; 2016 \$50; 2017 \$50; 2018 \$50; 2019 \$50.

⁵ In addition, the provision has outlay effects of (in millions of dollars): 2013 \$50; 2014 \$60; 2015 \$60; 2016 \$60; 2017 \$60; 2018 \$60; 2019 \$60.

⁶ In addition, recovery zone bonds have outlay effects (in millions of dollars) as follows: 2013 \$150; 2014 \$140; 2015 \$150; 2016 \$150; and 2017 \$150; 2018 \$150; 2019 \$150.

⁷ The figures in the table indicate the effect of the American opportunity tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2013 \$4,040; 2014 \$6,170; 2015 \$6,280; 2016 \$6,280; 2017 \$6,090; 2018 \$5,970; 2019 \$2,680.

⁸ In addition, the credit for holders of zone academy bonds has outlay effects of (in millions of dollars): 2013 \$20; 2014 \$30; 2015 \$30; 2016 \$30; 2017 \$30; 2018 \$30; and 2019 \$30.

⁹ In addition, the provision for school construction bonds has outlay effects of (in millions of dollars): 2013 \$900; 2014 \$840; 2015 \$900; 2016 \$900; 2017 \$900; 2018 \$900; and 2019 \$900.

¹⁰ The figures in the table indicate the effect of the adoption tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2013 \$0.

¹¹ The figures in the table indicate the effect of the child tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2013 \$21,660; 2014 \$21,680; 2015 \$21,700; 2016 \$21,600; 2017 \$21,680; 2018 \$21,930; and 2019 \$15,790.

¹² The figures in the table indicate the effect on income taxes of the employer contributions for health. In addition, the effect on payroll tax receipts (in millions of dollars) is as follows: 2013 \$117,920; 2014 \$122,990; 2015 \$127,980; 2016 \$132,400; 2017 \$138,330; 2018 \$145,270; 2019 \$153,870.

¹³ In addition, the premium assistance credit provision has outlay effects (in millions of dollars) as follows: 2014 \$34,020; 2015 \$55,140; 2016 \$70,610; 2017 \$82,150; 2018 \$86,460; 2019 \$90,600.

¹⁴ In addition, the small business credit provision has outlay effects (in millions of dollars) as follows: 2013 \$80; 2014 \$100; 2015 \$110; 2016 \$120; 2017 \$110; 2018 \$70; 2019 \$50.

¹⁵ The figures in the table indicate the effect of the health coverage tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2013 \$120; 2014 \$30; 2015 \$0;

¹⁶ The figures in the table indicate the effect of the earned income tax credit on receipts. The effect of the credit on outlays (in millions of dollars) is as follows: 2013 \$56,760; 2014 \$58,430; 2015 \$58,070; 2016 \$58,360; 2017 \$59,500; 2018 \$60,900; and 2019 \$59,330.

¹⁷ In addition, Build America Bonds have outlay effects of (in millions of dollars): 2013 \$3,060; 2014 \$2,840; 2015 \$3,060; 2016 \$3,060; 2017 \$3,060; 2018 \$3,060; and 2019 \$3060.

Note: Provisions with estimates denoted normal tax method have no revenue loss under the reference tax law method.

All estimates have been rounded to the nearest \$10 million. Provisions with estimates that rounded to zero in each year are not included in the table.

Table 14-3. INCOME TAX EXPENDITURES RANKED BY TOTAL FISCAL YEAR 2015-2019 PROJECTED REVENUE EFFECT

(In millions of dollars)

	Provision	2015	2015-19
128	Exclusion of employer contributions for medical insurance premiums and medical care	207,200	1,150,700
58	Deductibility of mortgage interest on owner-occupied homes	73,910	456,330
62	Exclusion of net imputed rental income	79,810	441,238
70	Capital gains (except agriculture, timber, iron ore, and coal)	68,850	422,270
146	Defined contribution employer plans	61,050	414,400
5	Deferral of income from controlled foreign corporations (normal tax method)	75,540	373,210
61	Capital gains exclusion on home sales	56,510	332,490
168	Deductibility of nonbusiness State and local taxes other than on owner-occupied homes	49,290	290,800
124	Deductibility of charitable contributions, other than education and health	46,630	275,810
76	Accelerated depreciation of machinery and equipment (normal tax method)	15,470	257,690
145	Defined benefit employer plans	42,340	234,960
166	Exclusion of interest on public purpose State and local bonds	35,010	213,830
59	Deductibility of State and local property tax on owner-occupied homes	33,880	198,550
72	Step-up basis of capital gains at death	32,370	179,310
159	Social Security benefits for retired workers	29,840	159,930
149	Self-Employed plans	25,530	155,530
69	Treatment of qualified dividends	26,650	148,950
51	Exclusion of interest on life insurance savings	23,040	132,370
121	Child credit	23,500	117,530
147	Individual Retirement Accounts	17,480	98,020
80	Deduction for US production activities	14,480	78,490
1	Exclusion of benefits and allowances to armed forces personnel	13,230	63,710
100	Lifetime Learning tax credit	15,240	59,680
63	Exception from passive loss rules for \$25,000 of rental loss	10,360	57,870
141	Exclusion of workers' compensation benefits	10,500	53,980
131	Deductibility of medical expenses	8,560	46,190
160	Social Security benefits for disabled workers	8,740	45,440
64	Credit for low-income housing investments	8,280	43,840
130	Medical Savings Accounts / Health Savings Accounts	4,890	39,790
129	Self-employed medical insurance premiums	6,970	37,800
162	Exclusion of veterans death benefits and disability compensation	5,490	32,750
135	Deductibility of charitable contributions (health)	5,350	31,850
110	Deductibility of charitable contributions (education)	5,370	31,540
7	Expensing of research and experimentation expenditures (normal tax method)	4,800	30,680
109	Parental personal exemption for students age 19 or over	5,400	27,880
132	Exclusion of interest on hospital construction bonds	4,210	25,710
2	Exclusion of income earned abroad by U.S. citizens	4,350	23,740
4	Inventory property sales source rules exception	3,890	22,962
122	Credit for child and dependent care expenses	4,310	22,810
158	Earned income tax credit	4,330	22,440
161	Social Security benefits for spouses, dependents and survivors	4,100	22,150
78	Graduated corporation income tax rate (normal tax method)	4,130	21,020
120	Exclusion of employee meals and lodging (other than military)	3,797	20,172
65	Accelerated depreciation on rental housing (normal tax method)	2,500	17,920
106	Exclusion of interest on bonds for private nonprofit educational facilities	2,760	16,900
155	Additional deduction for the elderly	2,800	16,610
97	Exclusion of scholarship and fellowship income (normal tax method)	3,090	16,570
15	New technology credit	3,000	16,040
73	Carryover basis of capital gains on gifts	2,560	15,090
84	Exclusion of reimbursed employee parking expenses	2,780	15,020
8	Credit for increasing research activities	3,170	12,930
50	Exemption of credit union income	1,970	12,810
136	Tax credit for orphan drug research	1,520	11,430
104	Qualified Tuition Programs	1,900	11,020
150	Premiums on group term life insurance	1,980	10,400
99	Lifetime Learning tax credit	1,720	10,180
55	Exclusion of interest spread of financial institutions	1,840	10,170
153	Special ESOP rules	1,810	10,010
56	Exclusion of interest on owner-occupied mortgage subsidy bonds	1,510	9,230

Table 14-3. INCOME TAX EXPENDITURES RANKED BY TOTAL FISCAL YEAR 2015-2019 PROJECTED REVENUE EFFECT—Continued
(In millions of dollars)

	Provision	2015	2015-19
102	Deductibility of student-loan interest	1,780	8,980
60	Deferral of income from installment sales	1,470	8,670
98	HOPE tax credit	0	7,950
57	Exclusion of interest on rental housing bonds	1,230	7,530
3	Exclusion of certain allowances for Federal employees abroad	1,220	6,730
164	Exclusion of GI bill benefits	1,160	6,630
148	Low and moderate income savers credit	1,210	6,350
46	Capital gains treatment of certain income	920	5,650
89	Exclusion of interest for airport, dock, and similar bonds	920	5,590
169	Deferral of interest on U.S. savings bonds	1,090	5,580
116	Employer provided child care exclusion	970	5,530
10	Excess of percentage over cost depletion, fuels	780	5,390
142	Exclusion of public assistance benefits (normal tax method)	820	4,500
111	Exclusion of employer-provided educational assistance	800	4,500
92	New markets tax credit	1,040	4,360
126	Exclusion of parsonage allowances	758	4,212
85	Exclusion for employer-provided transit passes	710	4,070
71	Capital gains exclusion of small corporation stock	480	3,980
16	Energy investment credit	1,470	3,900
53	Tax exemption of certain insurance companies owned by tax-exempt organizations	690	3,800
105	Exclusion of interest on student-loan bonds	620	3,780
134	Credit for employee health insurance expenses of small business.	1,050	3,650
37	Exclusion of interest on bonds for water, sewage, and hazardous waste facilities	560	3,400
114	Qualified school construction bonds	650	3,250
119	Adoption credit and exclusion	580	3,210
118	Assistance for adopted foster children	560	3,130
40	Tax incentives for preservation of historic structures	600	3,100
36	Excess of percentage over cost depletion, nonfuel minerals	590	3,060
31	30% credit for residential purchases/installations of solar and fuel cells	1,170	3,010
9	Expensing of exploration and development costs, fuels	510	2,770
19	Tax credits for clean-fuel burning vehicles	670	2,550
163	Exclusion of veterans pensions	450	2,400
139	Distributions from retirement plans for premiums for health and long-term care insurance	400	2,280
137	Special Blue Cross/Blue Shield deduction	360	2,080
157	Deductibility of casualty losses	360	1,990
125	Exclusion of certain foster care payments	390	1,870
94	Credit to holders of Gulf Tax Credit Bonds.	280	1,680
39	Expensing of multiperiod timber growing costs	300	1,650
20	Exclusion of utility conservation subsidies	340	1,640
151	Premiums on accident and disability insurance	310	1,610
140	Exclusion of railroad retirement system benefits	360	1,600
34	Advanced nuclear power production credit	0	1,270
79	Exclusion of interest on small issue bonds	210	1,260
115	Work opportunity tax credit	460	1,210
87	Exclusion of interest on bonds for Financing of Highway Projects and rail-truck transfer facilities	220	990
91	Empowerment zones, Enterprise communities, and Renewal communities	200	910
95	Recovery Zone Bonds	150	890
44	Expensing of certain multiperiod production costs	140	740
47	Income averaging for farmers	130	690
90	Exemption of certain mutuals' and cooperatives' income	120	630
107	Credit for holders of zone academy bonds	160	620
101	Education Individual Retirement Accounts	100	610
41	Industrial CO2 capture and sequestration tax credit	80	580
26	Amortize all geological and geophysical expenditures over 2 years	130	580
38	Capital gains treatment of certain timber income	90	570
13	Capital gains treatment of royalties on coal	90	570
43	Expensing of certain capital outlays	100	560
25	Natural gas distribution pipelines treated as 15-year property	100	560
144	Exclusion of military disability pensions	110	550

Table 14-3. INCOME TAX EXPENDITURES RANKED BY TOTAL FISCAL YEAR 2015-2019 PROJECTED REVENUE EFFECT—Continued
(In millions of dollars)

	Provision	2015	2015-19
82	Tonnage tax	70	520
113	Discharge of student loan indebtedness	90	480
77	Expensing of certain small investments (normal tax method)	-2,040	420
49	Expensing of reforestation expenditures	70	420
21	Credit for holding clean renewable energy bonds	70	350
74	Ordinary income treatment of loss from small business corporation stock sale	60	300
35	Expensing of exploration and development costs, nonfuel minerals	50	290
96	Tribal Economic Development Bonds	40	280
81	Special rules for certain film and TV production	120	250
68	Exceptions from imputed interest rules	40	240
152	Income of trusts to finance supplementary unemployment benefits	30	220
30	Credit for energy efficient appliances	120	220
54	Small life insurance company deduction	40	200
45	Treatment of loans forgiven for solvent farmers	40	200
154	Additional deduction for the blind	30	180
23	Credit for investment in clean coal facilities	140	180
123	Credit for disabled access expenditures	30	170
88	Investment credit for rehabilitation of structures (other than historic)	30	150
32	Qualified energy conservation bonds	30	150
14	Exclusion of interest on energy facility bonds	30	150
42	Deduction for endangered species recovery expenditures	20	140
165	Exclusion of interest on veterans housing bonds	20	130
143	Exclusion of special benefits for disabled coal miners	30	110
83	Deferral of tax on shipping companies	20	100
48	Deferral of gain on sale of farm refiners	20	100
12	Exception from passive loss limitation for working interests in oil and gas properties	20	100
108	Exclusion of interest on savings bonds redeemed to finance educational expenses	10	90
127	Indian employment credit	20	80
52	Special alternative tax on small property and casualty insurance companies	10	80
28	Credit for construction of new energy efficient homes	60	80
33	Advanced Energy Property Credit	90	70
156	Tax credit for the elderly and disabled	10	50
117	Employer-provided child care credit	10	50
17	Alcohol fuel credits	10	10
167	Build America Bonds	0	0
138	Tax credit for health insurance purchased by certain displaced and retired individuals	0	0
112	Special deduction for teacher expenses	0	0
103	Deduction for higher education expenses	0	0
86	Tax credit for certain expenditures for maintaining railroad tracks	0	0
66	Discharge of mortgage indebtedness	0	0
29	Credit for energy efficiency improvements to existing homes	0	0
18	Bio-Diesel and small agri-biodiesel producer tax credits	0	0
11	Alternative fuel production credit	0	0
6	Deferred taxes for financial firms on certain income earned overseas	0	0
27	Allowance of deduction for certain energy efficient commercial building property	20	-20
67	Discharge of business indebtedness	-80	-220
93	Expensing of environmental remediation costs	-170	-810
22	Deferral of gain from dispositions of transmission property to implement FERC restructuring policy	-220	-950
24	Temporary 50% expensing for equipment used in the refining of liquid fuels	-700	-3,860
133	Refundable Premium Assistance Tax Credit	-3,940	-26,570
75	Accelerated depreciation of buildings other than rental housing (normal tax method)	-7,540	-40,540

Table 14-4. PRESENT VALUE OF SELECTED TAX EXPENDITURES FOR ACTIVITY IN CALENDAR YEAR 2013

(In millions of dollars)

	Provision	2013 Present Value of Revenue Loss
5	Deferral of income from controlled foreign corporations (normal tax method)	36,010
7	Expensing of research and experimentation expenditures (normal tax method)	2,310
21	Credit for holding clean renewable energy bonds	310
9	Expensing of exploration and development costs - fuels	320
35	Expensing of exploration and development costs - nonfuels	50
39	Expensing of multiperiod timber growing costs	120
44	Expensing of certain multiperiod production costs - agriculture	0
43	Expensing of certain capital outlays - agriculture	0
49	Expensing of reforestation expenditures	30
51	Deferral of income on life insurance and annuity contracts	16,860
65	Accelerated depreciation on rental housing	5,100
75	Accelerated depreciation of buildings other than rental	-15,030
76	Accelerated depreciation of machinery and equipment	16,160
77	Expensing of certain small investments (normal tax method)	500
107	Credit for holders of zone academy bonds	160
64	Credit for low-income housing investments	6,780
104	Deferral for state prepaid tuition plans	3,070
145	Defined benefit employer plans	21,890
146	Defined contribution employer plans	66,610
147	Exclusion of IRA contributions and earnings	1,660
147	Exclusion of Roth earnings and distributions	3,400
147	Exclusion of non-deductible IRA earnings	150
149	Exclusion of contributions and earnings for Self-Employed plans	3,230
166	Exclusion of interest on public-purpose bonds	12,240
	Exclusion of interest on non-public purpose bonds	3,980
169	Deferral of interest on U.S. savings bonds	220

adjust the cost basis of capital assets and debt for changes in the general price level. Thus, under a comprehensive income tax baseline, the failure to take account of inflation in measuring depreciation, capital gains, and interest income would be regarded as a negative tax expenditure (i.e., a tax penalty), and failure to take account of inflation in measuring interest costs would be regarded as a positive tax expenditure (i.e., a tax subsidy).

Although the reference law and normal tax baselines are generally similar, areas of difference include:

Tax rates. The separate schedules applying to the various taxpaying units are included in the reference law baseline. Thus, corporate tax rates below the maximum statutory rate do not give rise to a tax expenditure. The normal tax baseline is similar, except that, by convention, it specifies the current maximum rate as the baseline for the corporate income tax. The lower tax rates applied to the first \$10 million of corporate income are thus regarded as a tax expenditure under the normal tax. By convention, the Alternative Minimum Tax is treated as part of the baseline rate structure under both the reference and normal tax methods.

Income subject to the tax. Income subject to tax is defined as gross income less the costs of earning that in-

come. Under the reference tax rules, gross income does not include gifts defined as receipts of money or property that are not consideration in an exchange nor does gross income include most transfer payments from the Government.² The normal tax baseline also excludes gifts between individuals from gross income. Under the normal tax baseline, however, all cash transfer payments from the Government to private individuals are counted in gross income, and exemptions of such transfers from tax are identified as tax expenditures. The costs of earning income are generally deductible in determining taxable income under both the reference and normal tax baselines.³

Capital recovery. Under the reference tax law baseline no tax expenditures arise from accelerated depreciation. Under the normal tax baseline, the depreciation allow-

² Gross income does, however, include transfer payments associated with past employment, such as Social Security benefits.

³ In the case of individuals who hold "passive" equity interests in businesses, the pro-rata shares of sales and expense deductions reportable in a year are limited. A passive business activity is defined generally to be one in which the holder of the interest, usually a partnership interest, does not actively perform managerial or other participatory functions. The taxpayer may generally report no larger deductions for a year than will reduce taxable income from such activities to zero. Deductions in excess of the limitation may be taken in subsequent years, or when the interest is liquidated. In addition, costs of earning income may be limited under the Alternative Minimum Tax.

ance for property is computed using estimates of economic depreciation.

Treatment of foreign income. Both the normal and reference tax baselines allow a tax credit for foreign income taxes paid (up to the amount of U.S. income taxes that would otherwise be due), which prevents double taxation of income earned abroad. Under the normal tax method, however, controlled foreign corporations (CFCs) are not regarded as entities separate from their controlling U.S. shareholders. Thus, the deferral of tax on income received by CFCs is regarded as a tax expenditure under this method. In contrast, except for tax haven activities, the reference law baseline follows current law in treating CFCs as separate taxable entities whose income is not subject to U.S. tax until distributed to U.S. taxpayers. Under this baseline, deferral of tax on CFC income is not a tax expenditure because U.S. taxpayers generally are not taxed on accrued, but unrealized, income.

Descriptions of Income Tax Provisions

Descriptions of the individual and corporate income tax expenditures reported on in this chapter follow. These descriptions relate to current law as of December 31, 2013.

National Defense

1. Benefits and allowances to Armed Forces personnel.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. As an example, a rental voucher of \$100 is (approximately) equal in value to \$100 of cash income. In contrast to this treatment, certain housing and meals, in addition to other benefits provided military personnel, either in cash or in kind, as well as certain amounts of pay related to combat service, are excluded from income subject to tax.

2. Income earned abroad.—Under the baseline tax system, all compensation received by U.S. citizens is properly included in their taxable income. It makes no difference whether the compensation is a result of working abroad or whether it is labeled as a housing allowance. In contrast to this treatment, U.S. tax law allows U.S. citizens who live abroad, work in the private sector, and satisfy a foreign residency requirement to exclude up to \$80,000, plus adjustments for inflation since 2004 (\$97,600 in 2013), in foreign earned income from U.S. taxes. In addition, if these taxpayers receive a specific allowance for foreign housing from their employers, then they may also exclude such expenses to the extent that they do not exceed 30 percent of the earned income inclusion, with geographical adjustments, over 16 percent of the earned income limit. If taxpayers do not receive a specific allowance for housing expenses, they may deduct housing expenses up to the amount by which foreign earned income exceeds their foreign earned income exclusion.

3. Exclusion of certain allowances for Federal employees abroad.—In general, all compensation received by U.S. citizens is properly included in their taxable income. It makes no difference whether the compensation is a result of working abroad or whether it is labeled as an allowance for the high cost of living abroad. In contrast to this treatment, U.S. Federal civilian employees and Peace Corps members who work outside the continental United States are allowed to exclude from U.S. taxable income certain special allowances they receive to compensate them for the relatively high costs associated with living overseas. The allowances supplement wage income and cover expenses such as rent, education, and the cost of travel to and from the United States.

4. Sales source rule exceptions.—The United States generally taxes the worldwide income of U.S. persons and business entities. Under the baseline tax system, taxpayers receive a credit for foreign taxes paid which is limited to the pre-credit U.S. tax on the foreign source income. In contrast, the sales source rules for inventory property under current law allow U.S. exporters to use more foreign tax credits by allowing the exporters to attribute a larger portion of their earnings abroad than would be the case if the allocation of earnings was based on actual economic activity.

5. Income of U.S.-controlled foreign corporations.—Under the baseline tax system, the United States generally taxes the worldwide income of U.S. persons and business entities. In contrast, certain active income of foreign corporations controlled by U.S. shareholders is not subject to U.S. taxation when it is earned. The income becomes taxable only when the controlling U.S. shareholders receive dividends or other distributions from their foreign stockholding. The reference law tax baseline reflects this tax treatment where only realized income is taxed. Under the normal tax method, however, the currently attributable foreign source pre-tax income from such a controlling interest is considered to be subject to U.S. taxation, whether or not distributed. Thus, the normal tax method considers the amount of controlled foreign corporation income not yet distributed to a U.S. shareholder as tax-deferred income.

6. Exceptions under subpart F for active financing income.—The United States generally taxes the worldwide income of U.S. persons and business entities. The baseline tax system would not allow the deferral of tax or other relief targeted at particular industries or activities. In contrast, under current law, financial firms may defer taxes on income earned overseas in an active business. Under current law, this provision expires at the end of 2013.

General Science, Space, and Technology

7. Expensing R&E expenditures.—The baseline tax system allows a deduction for the cost of producing income. It requires taxpayers to capitalize the costs associated with investments over time to better match the streams of income and associated costs. Research and experimentation (R&E) projects can be viewed as invest-

ments because, if successful, their benefits accrue for several years. It is often difficult, however, to identify whether a specific R&E project is successful and, if successful, what its expected life will be. Because of this ambiguity, the reference law baseline tax system would allow of expensing of R&E expenditures. In contrast, under the normal tax method, the expensing of R&E expenditures is viewed as a tax expenditure. The baseline assumed for the normal tax method is that all R&E expenditures are successful and have an expected life of five years.

8. R&E credit.—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. In contrast, the Tax Code allows an R&E credit of 20 percent of qualified research expenditures in excess of a base amount.

The base amount of the credit is generally determined by multiplying a “fixed-base percentage” by the average amount of the company’s gross receipts for the prior four years. The taxpayer’s fixed base percentage generally is the ratio of its research expenses to gross receipts for 1984 through 1988. Taxpayers can elect the alternative simplified credit regime, which is equal to 14 percent of qualified research expenses that exceed 50 percent of the average qualified research expenses for the three preceding taxable years. The credit does not apply to expenses paid or incurred after December 31, 2013.

Energy

9. Exploration and development costs.—Under the baseline tax system, the costs of exploring and developing oil and gas wells would be capitalized and then amortized (or depreciated) over an estimate of the economic life of the well. This insures that the net income from the well is measured appropriately each year.

In contrast to this treatment, current law allows intangible drilling costs for successful investments in domestic oil and gas wells (such as wages, the cost of using machinery for grading and drilling, and the cost of unsalvageable materials used in constructing wells) to be deducted immediately, i.e., expensed. Because it allows recovery of costs sooner, expensing is more generous for the taxpayer than would be amortization. Integrated oil companies may deduct only 70 percent of such costs and must amortize the remaining 30 percent over five years. The same rule applies to the exploration and development costs of surface stripping and the construction of shafts and tunnels for other fuel minerals.

10. Percentage depletion.—The baseline tax system would allow recovery of the costs of developing certain oil and mineral properties using cost depletion. Cost depletion is similar in concept to depreciation, in that the costs of developing or acquiring the asset are capitalized and then gradually reduced over an estimate of the asset’s productive life, as is appropriate for measuring net income.

In contrast, the Tax Code generally allows independent fuel and mineral producers and royalty owners to take percentage depletion deductions rather than cost depletion

on limited quantities of output. Under percentage depletion, taxpayers deduct a percentage of gross income from mineral production. In certain cases the deduction is limited to a fraction of the asset’s net income. Over the life of an investment, percentage depletion deductions can exceed the cost of the investment. Consequently, percentage depletion offers more generous tax treatment than would cost depletion, which would limit deductions to an investment’s cost.

11. Alternative fuel production credit.—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code provides a credit of \$3 per oil-equivalent barrel of production (in 2004 dollars) for coke or coke gas during a four-year period for qualified facilities. Qualifying facilities producing coke and coke gas must be placed in service by December 31, 2009.

12. Oil and gas exception to passive loss limitation.—The baseline tax system accepts current law’s general rule limiting taxpayers’ ability to deduct losses from passive activities against nonpassive income (e.g., wages, interest, and dividends). Passive activities generally are defined as those in which the taxpayer does not materially participate, and there are numerous additional considerations brought to bear on the determination of which activities are passive for a given taxpayer. Losses are limited in an attempt to limit tax sheltering activities. Passive losses that are unused may be carried forward and applied against future passive income.

An exception from the passive loss limitation is provided for a working interest in an oil or gas property that the taxpayer holds directly or through an entity that does not limit the liability of the taxpayer with respect to the interest. Thus, taxpayers can deduct losses from such working interests against nonpassive income without regard to whether they materially participate in the activity.

13. Capital gains treatment of royalties on coal.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low tax rates to apply to certain types or sources of income. For individuals in 2013, tax rates on regular income vary from 10 percent to 39.6 percent, depending on the taxpayer’s income. In contrast, current law allows capital gains realized by individuals to be taxed at a preferentially low rate that is no higher than 20 percent. Certain sales of coal under royalty contracts qualify for taxation as capital gains rather than ordinary income, and so benefit from the preferentially low 20 percent maximum tax rate on capital gains.

14. Energy facility bonds.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows interest earned on State and local bonds used to finance construction of certain energy facilities to be exempt from tax. These bonds are generally subject to the State private-activity-bond annual volume cap.

15. **Energy production credit.**—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code provides a credit for certain electricity produced from wind energy, biomass, geothermal energy, solar energy, small irrigation power, municipal solid waste, or qualified hydropower and sold to an unrelated party. In addition to the electricity production credit, an income tax credit is allowed for the production of refined coal and Indian coal at qualified facilities.

16. **Energy investment credit.**—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. However, the Tax Code provides credits for investments in solar and geothermal energy property, qualified fuel cell power plants, stationary microturbine power plants, geothermal heat pumps, small wind property and combined heat and power property. Owners of renewable power facilities that qualify for the energy production credit may instead elect to take an energy investment credit.

17. **Alcohol fuel credits.**—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code provides an income tax credit for qualified cellulosic biofuel production. This provision expired on December 31, 2013.

18. **Bio-Diesel tax credit.**—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. However, the Tax Code allows an income tax credit for bio-diesel used or sold and for bio-diesel derived from virgin sources. In lieu of the bio-diesel credit, the taxpayer may claim a refundable excise tax credit. In addition, small agri-biodiesel producers are eligible for a separate income tax credit for ethanol production and a separate credit is available for qualified renewable diesel fuel mixtures. This provision expired on December 31, 2013.

19. **Tax credits for clean-fuel burning vehicles and refueling property.**—The baseline tax system would not allow credits or deductions for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code allows a number of credits for certain types of vehicles and property. These are available for alternative fuel vehicle refueling property, fuel cell vehicles, plug-in electric-drive motor vehicles, and two- and three-wheeled plug-in electric vehicles.

20. **Exclusion of utility conservation subsidies.**—The baseline tax system generally takes a comprehensive view of taxable income that includes a wide variety of (measurable) accretions to wealth. In certain circumstances, public utilities offer rate subsidies to non-business customers who invest in energy conservation measures. These rate subsidies are equivalent to payments from the utility to its customer, and so represent

accretions to wealth, income, that would be taxable to the customer under the baseline tax system. In contrast, the Tax Code exempts these subsidies from the non-business customer's gross income.

21. **Credit to holders of clean renewable energy bonds.**—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. In contrast, the Tax Code provides for the issuance of Clean Renewable Energy Bonds which entitles the bond holder to a Federal income tax credit in lieu of interest. The limit on the volume authorized in 2009–2010 is \$2.4 billion. As of March 2010, issuers of the unused authorization of such bonds could opt to receive direct payment with the yield becoming fully taxable.

22. **Deferral of gain from dispositions of transmission property to implement FERC restructuring policy.**—The baseline tax system generally would tax gains from sale of property when realized. It would not allow an exception for particular activities or individuals. However, the Tax Code allows utilities to defer gains from the sale of their transmission assets to a FERC-approved independent transmission company. The sale of property must be made prior to January 1, 2013.

23. **Credit for investment in clean coal facilities.**—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code provides investment tax credits for clean coal facilities producing electricity and for industrial gasification combined cycle projects.

24. **Temporary 50 percent expensing for equipment used in the refining of liquid fuels.**—The baseline tax system allows the taxpayer to deduct the decline in the economic value of an investment over its economic life. However, the Tax Code provides for an accelerated recovery of the cost of certain investments in refineries by allowing partial expensing of the cost, thereby giving such investments a tax advantage.

25. **Natural gas distribution pipelines treated as 15-year property.**—The baseline tax system allows taxpayers to deduct the decline in the economic value of an investment over its economic life. However, the Tax Code allows depreciation of natural gas distribution pipelines (placed in service between 2005 and 2011) over a 15 year period. These deductions are accelerated relative to deductions based on economic depreciation.

26. **Amortize all geological and geophysical expenditures over two years.**—The baseline tax system allows taxpayers to deduct the decline in the economic value of an investment over time. However, the Tax Code allows geological and geophysical expenditures incurred in connection with oil and gas exploration in the United States to be amortized over two years for non-integrated oil companies.

27. **Allowance of deduction for certain energy efficient commercial building property.**—The baseline tax system would not allow deductions in addition to nor-

mal depreciation allowances for particular investments in particular industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code allows a deduction, per square foot, for certain energy efficient commercial buildings.

28. Credit for construction of new energy efficient homes.—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. However, the Tax Code allows contractors a tax credit of \$2,000 for the construction of a qualified new energy-efficient home that has an annual level of heating and cooling energy consumption at least 50 percent below the annual consumption of a comparable dwelling unit. The credit equals \$1,000 in the case of a new manufactured home that meets a 30 percent standard. This provision expired on December 31, 2013.

29. Credit for energy efficiency improvements to existing homes.—The baseline tax system would not allow credits for particular activities, investments, or industries. However, the Tax Code provides an investment tax credit for expenditures made on insulation, exterior windows, and doors that improve the energy efficiency of homes and meet certain standards. The Tax Code also provides a credit for purchases of advanced main air circulating fans, natural gas, propane, or oil furnaces or hot water boilers, and other qualified energy efficient property. This provision expired on December 31, 2013.

30. Credit for energy efficient appliances.—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code provides tax credits for the manufacture of efficient dishwashers, clothes washers, and refrigerators. The size of the credit depends on the efficiency of the appliance. This provision expired on December 31, 2013.

31. Credit for residential energy efficient property.—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. However, the Tax Code provides a credit for the purchase of a qualified photovoltaic property and solar water heating property, as well as for fuel cell power plants, geothermal heat pumps and small wind property.

32. Credit for qualified energy conservation bonds.—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. However, the Tax Code provides for the issuance of energy conservation bonds which entitle the bond holder to a Federal income tax credit in lieu of interest. The limit on the volume issued in 2009–2010 is \$3.2 billion. As of March 2010, issuers of the unused authorization of such bonds could opt to receive direct payment with the yield becoming fully taxable.

33. Advanced energy property credit.—The baseline tax system would not allow credits for particular activities, investments, or industries. However, the Tax

Code provides a 30 percent investment credit for property used in a qualified advanced energy manufacturing project. The Treasury Department may award up to \$2.3 billion in tax credits for qualified investments.

34. Advanced nuclear power facilities production credit.—The baseline tax system would not allow credits or deductions for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code allows a tax credit equal to 1.8 cents times the number of kilowatt hours of electricity produced at a qualifying advanced nuclear power facility. A taxpayer may claim no more than \$125 million per 1,000 MW of capacity. The Treasury Department may allocate up to 6,000 megawatts of credit-eligible capacity.

Natural Resources and Environment

35. Exploration and development costs.—The baseline tax system allows the taxpayer to deduct the depreciation of an asset according to the decline in its economic value over time. However, certain capital outlays associated with exploration and development of nonfuel minerals may be expensed rather than depreciated over the life of the asset.

36. Percentage depletion.—The baseline tax system allows the taxpayer to deduct the decline in the economic value of an investment over time. Under current law, however, most nonfuel mineral extractors may use percentage depletion (whereby the deduction is fixed as a percentage of revenue and can exceed total costs) rather than cost depletion, with percentage depletion rates ranging from 22 percent for sulfur to 5 percent for sand and gravel. Over the life of an investment, percentage depletion deductions can exceed the cost of the investment. Consequently, percentage depletion offers more generous tax treatment than would cost depletion, which would limit deductions to an investment's cost.

37. Sewage, water, solid and hazardous waste facility bonds.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows interest earned on State and local bonds used to finance construction of sewage, water, or hazardous waste facilities to be exempt from tax. These bonds are generally subject to the State private-activity-bond annual volume cap.

38. Capital gains treatment of certain timber.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low tax rates to apply to certain types or sources of income. However, under current law certain timber sales can be treated as a capital gain rather than ordinary income and therefore subject to the lower capital-gains tax rate. For individuals in 2013, tax rates on regular income vary from 10 percent to 39.6 percent, depending on the taxpayer's income. In contrast, current law allows capital gains to be taxed at a preferentially low rate that is no higher than 20 percent.

39. Expensing multi-period timber growing costs.—The baseline tax system requires the taxpayer to capitalize costs associated with investment property. However, most of the production costs of growing timber may be expensed under current law rather than capitalized and deducted when the timber is sold, thereby accelerating cost recovery.

40. Historic preservation.—The baseline tax system would not allow credits for particular activities, investments, or industries. However, expenditures to preserve and restore certified historic structures qualify for an investment tax credit of 20 percent under current law for certified rehabilitation activities. The taxpayer's recoverable basis must be reduced by the amount of the credit.

41. Industrial CO₂ capture and sequestration tax credit.—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. In contrast, the Tax Code allows a credit of \$20 per metric ton for qualified carbon dioxide captured at a qualified facility and disposed of in secure geological storage. In addition, the provision allows a credit of \$10 per metric ton of qualified carbon dioxide that is captured at a qualified facility and as a tertiary injectant in a qualified enhanced oil or natural gas recovery project.

42. Deduction for endangered species recovery expenditures.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low tax rates to apply to certain types or sources of income. In contrast, under current law farmers can deduct up to 25 percent of their gross income for expenses incurred as a result of site and habitat improvement activities that will benefit endangered species on their farm land, in accordance with site specific management actions included in species recovery plans approved pursuant to the Endangered Species Act of 1973.

Agriculture

43. Expensing certain capital outlays.—The baseline tax system requires the taxpayer to capitalize costs associated with investment property. However, farmers may expense certain expenditures for feed and fertilizer as well as for soil and water conservation measures as well as other capital improvements under current law.

44. Expensing multi-period livestock and crop production costs.—The baseline tax system requires the taxpayer to capitalize costs associated with an investment over time. However, the production of livestock and crops with a production period greater than two years (e.g., establishing orchards or constructing barns) is exempt from the uniform cost capitalization rules, thereby accelerating cost recovery.

45. Loans forgiven solvent farmers.—The baseline tax system requires debtors to include the amount of loan forgiveness as income or else reduce their recoverable basis in the property related to the loan. If the amount of forgiveness exceeds the basis, the excess forgiveness is taxable. However, for bankrupt debtors, the amount of

loan forgiveness reduces carryover losses, unused credits, and then basis, with the remainder of the forgiven debt excluded from taxation.

46. Capital gains treatment of certain income.—For individuals in 2013, tax rates on regular income vary from 10 percent to 39.6 percent, depending on the taxpayer's income. The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low tax rates to apply to certain types or sources of income. In contrast, current law allows capital gains to be taxed at a preferentially low rate that is no higher than 20 percent. Certain agricultural income, such as unharvested crops, qualify for taxation as capital gains rather than ordinary income, and so benefit from the preferentially low 20 percent maximum tax rate on capital gains.

47. Income averaging for farmers.—The baseline tax system generally taxes all earned income each year at the rate determined by the income tax. However, taxpayers may average their taxable income from farming and fishing over the previous three years.

48. Deferral of gain on sales of farm refiners.—The baseline tax system generally subjects capital gains to taxes the year that they are realized. However, the Tax Code allows a taxpayer who sells stock in a farm refiner to a farmers' cooperative to defer recognition of the gain if the proceeds are re-invested in a qualified replacement property.

49. Expensing of reforestation expenditures.—The baseline tax system requires the taxpayer to capitalize costs associated with an investment over time. In contrast, the Tax Code provides for the expensing of the first \$10,000 in reforestation expenditures with 7-year amortization of the remaining expenses.

Commerce and Housing

This category includes a number of tax expenditure provisions that also affect economic activity in other functional categories. For example, provisions related to investment, such as accelerated depreciation, could be classified under the energy, natural resources and environment, agriculture, or transportation categories.

50. Credit union income exemption.—Under the baseline tax system, corporations pay taxes on their profits under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. However, in the Tax Code the earnings of credit unions not distributed to members as interest or dividends are exempt from the income tax.

51. Deferral of income on life insurance and annuity contracts.—Under the baseline tax system, individuals and corporations pay taxes on their income when it is (actually or constructively) received or accrued, depending on their method of accounting. Nevertheless, the Tax Code provides favorable tax treatment for investment income earned within qualified life insurance and annuity contracts. In general, investment income earned on qualified life insurance contracts held until death is

permanently exempt from income tax. Investment income distributed prior to the death of the insured is tax-exempt to the extent that investment in the contract is overstated (because premiums paid for the cost of life insurance protection are credited to investment in the contract), while the remaining distributed amounts are tax-deferred because income is not taxed on a current basis, but is recognized only when distributed from the contract. Investment income earned on annuities benefits from tax deferral.

52. *Small property and casualty insurance companies.*—Under the baseline tax system, corporations pay taxes on their profits under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. Under current law, however, stock non-life insurance companies are generally exempt from tax if their gross receipts for the taxable year do not exceed \$600,000 and more than 50 percent of such gross receipts consist of premiums. Mutual non-life insurance companies are generally tax-exempt if their annual gross receipts do not exceed \$150,000 and more than 35 percent of gross receipts consist of premiums. Also, non-life insurance companies with no more than \$1.2 million of annual net premiums may elect to pay tax only on their taxable investment income.

53. *Insurance companies owned by exempt organizations.*—Under the baseline tax system, corporations pay taxes on their profits under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. Generally the income generated by life and property and casualty insurance companies is subject to tax, albeit by special rules. Insurance operations conducted by such exempt organizations as fraternal societies, voluntary employee benefit associations, and others, however, are exempt from tax.

54. *Small life insurance company deduction.*—Under the baseline tax system, corporations pay taxes on their profits under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. However, under current law small life insurance companies (with gross assets of less than \$500 million) can deduct 60 percent of the first \$3 million of otherwise taxable income. The deduction phases out for otherwise taxable income between \$3 million and \$15 million.

55. *Exclusion of interest spread of financial institutions.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. Consumers and non-profit organizations pay for some deposit-linked services, such as check cashing, by accepting a below-market interest rate on their demand deposits. If they received a market rate of interest on those deposits and paid explicit fees for the associated services, they would pay taxes on the full market rate and (unlike businesses) could not deduct the fees. The Government thus foregoes tax on the difference between the risk-free market interest rate and below-market interest rates on demand deposits, which

under competitive conditions should equal the value added of deposit services.

56. *Mortgage housing bonds.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows interest earned on State and local bonds used to finance homes purchased by first-time, low-to-moderate-income buyers to be exempt. These bonds are generally subject to the State private-activity-bond annual volume cap.

57. *Rental housing bonds.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows interest earned on State and local government bonds used to finance multi-family rental housing projects to be tax-exempt.

58. *Interest on owner-occupied homes.*—Under the baseline tax system, expenses incurred in earning income would be deductible. However, such expenses would not be deductible when the income or the return on an investment is not taxed. In contrast, the Tax Code allows an exclusion from a taxpayer's taxable income for the value of owner-occupied housing services and also allows the owner-occupant to deduct mortgage interest paid on his or her primary residence and one secondary residence as an itemized non-business deduction. In general, the mortgage interest deduction is limited to interest on debt no greater than the owner's basis in the residence, and is also limited to interest on debt of no more than \$1 million. Interest on up to \$100,000 of other debt secured by a lien on a principal or second residence is also deductible, irrespective of the purpose of borrowing, provided the total debt does not exceed the fair market value of the residence. As an alternative to the deduction, holders of qualified Mortgage Credit Certificates issued by State or local governmental units or agencies may claim a tax credit equal to a proportion of their interest expense.

59. *Taxes on owner-occupied homes.*—Under the baseline tax system, expenses incurred in earning income would be deductible. However, such expenses would not be deductible when the income or the return on an investment is not taxed. In contrast, the Tax Code allows an exclusion from a taxpayer's taxable income for the value of owner-occupied housing services and also allows the owner-occupant to deduct property taxes paid on his or her primary and secondary residences.

60. *Installment sales.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates, or deferral of tax, to apply to certain types or sources of income. Dealers in real and personal property (i.e., sellers who regularly hold property for sale or resale) cannot defer taxable income from installment sales until the receipt of the loan repayment. Nondealers (i.e., sellers of real property used in their business) are required to pay interest on deferred taxes attributable to their total installment obligations in excess of \$5 million. Only properties with sales prices exceeding \$150,000 are includ-

able in the total. The payment of a market rate of interest eliminates the benefit of the tax deferral. The tax exemption for nondealers with total installment obligations of less than \$5 million is, therefore, a tax expenditure.

61. Capital gains exclusion on home sales.—The baseline tax system would not allow deductions and exemptions for certain types of income. In contrast, the Tax Code allows homeowners to exclude from gross income up to \$250,000 (\$500,000 in the case of a married couple filing a joint return) of the capital gains from the sale of a principal residence. To qualify, the taxpayer must have owned and used the property as the taxpayer's principal residence for a total of at least two of the five years preceding the date of sale. In addition, the exclusion may not be used more than once every two years.

62. Imputed net rental income on owner-occupied housing.—Under the baseline tax system, the taxable income of a taxpayer who is an owner-occupant would include the implicit value of gross rental income on housing services earned on the investment in owner-occupied housing and would allow a deduction for expenses, such as interest, depreciation, property taxes, and other costs, associated with earning such rental income. In contrast, the Tax Code allows an exclusion from taxable income for the implicit gross rental income on housing services, while in certain circumstances allows a deduction for some costs associated with such income, such as for mortgage interest and property taxes.

63. Passive loss real estate exemption.—The baseline tax system accepts current law's general rule limiting taxpayers' ability to deduct losses from passive activities against nonpassive income (e.g., wages, interest, and dividends). Passive activities generally are defined as those in which the taxpayer does not materially participate and there are numerous additional considerations brought to bear on the determination of which activities are passive for a given taxpayer. Losses are limited in an attempt to limit tax sheltering activities. Passive losses that are unused may be carried forward and applied against future passive income.

In contrast to the general restrictions on passive losses, the Tax Code exempts owners of rental real estate activities from "passive income" limitations. The exemption is limited to \$25,000 in losses and phases out for taxpayers with income between \$100,000 and \$150,000.

64. Low-income housing credit.—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. However, under current law taxpayers who invest in certain low-income housing are eligible for a tax credit. The credit rate is set so that the present value of the credit is equal to 70 percent for new construction and 30 percent for (1) housing receiving other Federal benefits (such as tax-exempt bond financing), or (2) substantially rehabilitated existing housing. The credit can exceed these levels in certain statutorily defined and State designated areas where project development costs are higher. The credit is allowed in equal amounts over 10 years and is generally subject to a volume cap.

65. Accelerated depreciation of residential rental property.—Under an economic income tax, the costs of acquiring a building are capitalized and depreciated over time in accordance with the decline in the property's economic value due to wear and tear or obsolescence. This insures that the net income from the rental property is measured appropriately each year. However, the depreciation provisions of the Tax Code are part of the reference law rules, and thus do not give rise to tax expenditures under reference law. Under normal law, however, depreciation allowances reflect estimates of economic depreciation.

66. Discharge of mortgage indebtedness.—Under the baseline tax system, all income would generally be taxed under the regular tax rate schedule. The baseline tax system would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows an exclusion from a taxpayer's taxable income for any discharge of indebtedness of up to \$2 million (\$1 million in the case of a married individual filing a separate return) from a qualified principal residence. The provision applies to debt discharged after January 1, 2007, and before January 1, 2014.

67. Discharge of business indebtedness.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows an exclusion from a taxpayer's taxable income for any discharge qualified real property business indebtedness by taxpayers other than a C corporation. If the canceled debt is not reported as current income, however, the basis of the underlying property must be reduced by the amount canceled.

68. Imputed interest rules.—Under the baseline tax system, holders (issuers) of debt instruments are generally required to report interest earned (paid) in the period it accrues, not when paid. In addition, the amount of interest accrued is determined by the actual price paid, not by the stated principal and interest stipulated in the instrument. But under current law, and in general, any debt associated with the sale of property worth less than \$250,000 is excepted from the general interest accounting rules. This general \$250,000 exception is not a tax expenditure under reference law but is under normal law. Exceptions above \$250,000 are a tax expenditure under reference law; these exceptions include the following: (1) sales of personal residences worth more than \$250,000, and (2) sales of farms and small businesses worth between \$250,000 and \$1 million.

69. Treatment of qualified dividends.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low tax rates to apply to certain types or sources of income. For individuals in 2013, tax rates on regular income vary from 10 percent to 39.6 percent, depending on the taxpayer's income. In contrast, under current law, qualified dividends are taxed at a preferentially low rate that is no higher than 20 percent.

70. Capital gains (other than agriculture, timber, and coal).—The baseline tax system generally

would tax all income under the regular tax rate schedule. It would not allow preferentially low tax rates to apply to certain types or sources of income. For individuals in 2013, tax rates on regular income vary from 10 percent to 39.6 percent, depending on the taxpayer's income. In contrast, under current law, capital gains on assets held for more than one year are taxed at a preferentially low rate that is no higher than 20 percent.

71. Capital gains exclusion for small business stock.—The baseline tax system would not allow deductions and exemptions, or provide preferential treatment of certain sources of income or types of activities. In contrast, the Tax Code provides an exclusion of 50 percent (from a 28 percent tax rate) for capital gains from qualified small business stock held by individuals for more than 5 years; 75 percent for stock issued after February 17, 2009 and before September 28, 2010; and 100 percent for stock issued after September 27, 2010 and before January 1, 2014. A qualified small business is a corporation whose gross assets do not exceed \$50 million as of the date of issuance of the stock.

72. Step-up in basis of capital gains at death.—Under the baseline tax system, unrealized capital gains would be taxed when assets are transferred at death or by gift. It would not allow for exempting gains upon transfer of the underlying assets to the heirs. In contrast, capital gains on assets held at the owner's death are not subject to capital gains tax under current law. The cost basis of the appreciated assets is adjusted to the market value at the owner's date of death which becomes the basis for the heirs.

73. Carryover basis of capital gains on gifts.—Under the baseline tax system, unrealized capital gains would be taxed when assets are transferred at death or by gift. In contrast, when a gift of appreciated asset is made under current law, the donor's basis in the transferred property (the cost that was incurred when the transferred property was first acquired) carries over to the donee. The carryover of the donor's basis allows a continued deferral of unrealized capital gains.

74. Ordinary income treatment of losses from sale of small business corporate stock shares.—The baseline tax system limits to \$3,000 the write-off of losses from capital assets, with carryover of the excess to future years. In contrast, the Tax Code allows up to \$100,000 in losses from the sale of small business corporate stock (capitalization less than \$1 million) to be treated as ordinary losses and fully deducted.

75. Depreciation of non-rental-housing buildings.—Under an economic income tax, the costs of acquiring a building are capitalized and depreciated over time in accordance with the decline in the property's economic value due to wear and tear or obsolescence. This insures that the net income from the property is measured appropriately each year. However, the depreciation provisions of the Tax Code are part of the reference law rules, and thus do not give rise to tax expenditures under reference law. Under normal law, however, depreciation allowances reflect estimates of economic depreciation.

76. Accelerated depreciation of machinery and equipment.—Under an economic income tax, the costs of acquiring machinery and equipment are capitalized and depreciated over time in accordance with the decline in the property's economic value due to wear and tear or obsolescence. This insures that the net income from the property is measured appropriately each year. However, the depreciation provisions of the Tax Code are part of the reference law rules, and thus do not give rise to tax expenditures under reference law. Under normal law, however, depreciation allowances reflect estimates of economic depreciation.

77. Expensing of certain small investments.—Under the reference law baseline, the costs of acquiring tangible property and computer software would be depreciated using the Tax Code's depreciation provisions. Under the normal tax baseline, depreciation allowances are estimates of economic depreciation. However, the Tax Code allows qualifying investments by small businesses in tangible property and certain computer software to be expensed rather than depreciated over time.

78. Graduated corporation income tax rate schedule.—Because the corporate rate schedule is part of reference tax law, it is not considered a tax expenditure under the reference method. A flat corporation income tax rate is taken as the baseline under the normal tax method; therefore the lower rate is considered a tax expenditure under this concept.

79. Small issue industrial development bonds.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows interest earned on small issue industrial development bonds (IDBs) issued by State and local governments to finance manufacturing facilities to be tax exempt. Depreciable property financed with small issue IDBs must be depreciated, however, using the straight-line method. The annual volume of small issue IDBs is subject to the unified volume cap discussed in the mortgage housing bond section above.

80. Deduction for U.S. production activities.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows for a deduction equal to a portion of taxable income attributable to domestic production.

81. Special rules for certain film and TV production.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow deductions and exemptions or preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, under current law taxpayers may deduct up to \$15 million per production (\$20 million in certain distressed areas) in non-capital expenditures incurred during the year. This provision expires at the end of 2013.

Transportation

82. *Tonnage tax.*—The baseline tax system generally would tax all profits and income under the regular tax rate schedule. U.S. shipping companies may choose to be subject to a tonnage tax based on gross shipping weight in lieu of an income tax, in which case profits would not be subject to tax under the regular tax rate schedule.

83. *Deferral of tax on U.S. shipping companies.*—The baseline tax system generally would tax all profits and income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows certain companies that operate U.S. flag vessels to defer income taxes on that portion of their income used for shipping purposes, primarily construction, modernization and major repairs to ships, and repayment of loans to finance these investments.

84. *Exclusion of employee parking expenses.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, would be included in taxable income. Dedicated payments and in-kind benefits represent accretions to wealth that do not differ materially from cash wages. In contrast, the Tax Code allows an exclusion from taxable income for employee parking expenses that are paid for by the employer or that are received by the employee in lieu of wages. In 2013, the maximum amount of the parking exclusion is \$245 per month. The tax expenditure estimate does not include any subsidy provided through employer-owned parking facilities.

85. *Exclusion of employee transit pass expenses.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, would be included in taxable income. Dedicated payments and in-kind benefits represent accretions to wealth that do not differ materially from cash wages. In contrast, the Tax Code allows an exclusion from a taxpayer's taxable income for passes, tokens, fare cards, and vanpool expenses that are paid for by an employer or that are received by the employee in lieu of wages to defray an employee's commuting costs. The maximum amount of the transit exclusion is \$130 (indexed) per month in 2014. (There had been a parity provision that had temporary resulted in a higher maximum equal to those for parking passes for several years, which expired on December 31, 2013.)

86. *Tax credit for certain expenditures for maintaining railroad tracks.*—The baseline tax system would not allow credits for particular activities, investments, or industries. However, under current law eligible taxpayers may claim a credit equal to the lesser of 50 percent of maintenance expenditures and the product of \$3,500 and the number of miles of track owned or leased. This provision expires at the end of 2013.

87. *Exclusion of interest on bonds for financing of highway projects and rail-truck transfer facilities.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax

Code provides for \$15 billion of tax-exempt bond authority to finance qualified highway or surface freight transfer facilities. The authority to issue these bonds expires on December 31, 2015.

Community and Regional Development

88. *Rehabilitation of structures.*—The baseline tax system would uniformly tax all returns to investments and not allow credits for particular activities, investments, or industries. However, the Tax Code allows a 10-percent investment tax credit for the rehabilitation of buildings that are used for business or productive activities and that were erected before 1936 for other than residential purposes. The taxpayer's recoverable basis must be reduced by the amount of the credit.

89. *Airport, dock, and similar facility bonds.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allows interest earned on State and local bonds issued to finance high-speed rail facilities and Government-owned airports, docks, wharves, and sport and convention facilities to be tax-exempt. These bonds are not subject to a volume cap.

90. *Exemption of income of mutuals and cooperatives.*—Under the baseline tax system, corporations pay taxes on their profits under the regular tax rate schedule. In contrast, the Tax Code provides for the incomes of mutual and cooperative telephone and electric companies to be exempt from tax if at least 85 percent of their revenues are derived from patron service charges.

91. *Empowerment zones, the DC Enterprise Zone, and renewal communities.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income, tax credits, and write-offs faster than economic depreciation. In contrast, under current law qualifying businesses in designated economically depressed areas can receive tax benefits such as an employer wage credit, increased expensing of investment in equipment, special tax-exempt financing, accelerated depreciation, and certain capital gains incentives. A taxpayer's ability to accrue new tax benefits for empowerment zones expired December 31, 2013.

92. *New markets tax credit.*—The baseline tax system would not allow credits for particular activities, investments, or industries. However, under current law taxpayers who make qualified equity investments in a community development entity (CDE), which then makes qualified investments in low-income communities, are eligible for a tax credit received over 7 years. A CDE must first receive an allocation of tax credit from Treasury before it can sell the tax credit to the investor in exchange for the equity investment. The total equity investment available for the credit across all CDEs is \$3.5 billion for 2013, the last year for which allocations can be made.

93. *Expensing of environmental remediation costs.*—Under the baseline tax system, the costs would be amortized (or depreciated) over an estimate of the economic life of the building. This insures that the net income from the buildings is measured appropriately each year. However, the Tax Code allows taxpayers who clean up certain hazardous substances at a qualified site to expense the clean-up costs, even though the expenses will generally increase the value of the property significantly or appreciably prolong the life of the property.

94. *Credit to holders of Gulf and Midwest Tax Credit Bonds.*—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, under current law taxpayers that own Gulf and Midwest Tax Credit bonds receive a non-refundable tax credit rather than interest. The credit is included in gross income.

95. *Recovery Zone Bonds.*—The baseline tax system would not allow credits for particular activities, investments, or industries. In addition, it would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code allowed local governments to issue up to \$10 billion in taxable Recovery Zone Economic Development Bonds in 2009 and 2010 and receive a direct payment from Treasury equal to 45 percent of interest expenses. In addition, local governments could issue up to \$15 billion in tax exempt Recovery Zone Facility Bonds. These bonds financed certain kinds of business development in areas of economic distress.

96. *Tribal Economic Development Bonds.*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, the Tax Code was modified in 2009 to allow Indian tribal governments to issue tax exempt “tribal economic development bonds.” There is a national bond limitation of \$2 billion.

Education, Training, Employment, and Social Services

97. *Scholarship and fellowship income.*—Scholarships and fellowships are excluded from taxable income to the extent they pay for tuition and course-related expenses of the grantee. Similarly, tuition reductions for employees of educational institutions and their families are not included in taxable income. From an economic point of view, scholarships and fellowships are either gifts not conditioned on the performance of services, or they are rebates of educational costs. Thus, under the baseline tax system of the reference law method, this exclusion is not a tax expenditure because this method does not include either gifts or price reductions in a taxpayer’s gross income. The exclusion, however, is considered a tax expenditure under the normal tax method, which includes gift-like transfers of Government funds in gross income (many scholarships are derived directly or indirectly from Government funding).

98. *HOPE tax credit.*—The baseline tax system would not allow credits for particular activities, investments, or industries. Under current law, however, the non-refundable HOPE tax credit allows a credit for 100 percent of an eligible student’s first \$1,200 of tuition and fees and 50 percent of the next \$1,200 of tuition and fees. The credit only covers tuition and fees paid during the first two years of a student’s post-secondary education. In 2013, the credit is phased out ratably for taxpayers with modified AGI between \$107,000 and \$127,000 if married filing jointly (\$53,000 and \$63,000 for other taxpayers), indexed.

99. *Lifetime Learning tax credit.*—The baseline tax system would not allow credits for particular activities, investments, or industries. Under current law, however, the non-refundable Lifetime Learning tax credit allows a credit for 20 percent of an eligible student’s tuition and fees, up to a maximum credit per return of \$2,000. In 2013, the credit is phased out ratably for taxpayers with modified AGI between \$107,000 and \$127,000 if married filing jointly (\$53,000 and \$63,000 for other taxpayers), indexed. The credit applies to both undergraduate and graduate students.

100. *American Opportunity Tax Credit.*—The baseline tax system would not allow credits for particular activities, investments, or industries. Under current law in 2013, however, the American Opportunity tax credit allows a partially refundable credit of up to \$2,500 per eligible student for qualified tuition and related expenses paid during each of the first four years of the student’s post-secondary education. The credit is phased out for taxpayers with modified adjusted gross income between \$80,000 and \$90,000 (\$160,000 and \$180,000 for married taxpayers filing a joint return). The credit expires at the end of 2017.

101. *Education Individual Retirement Accounts (IRA).*—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. While contributions to an education IRA are not tax-deductible under current law, investment income earned by education IRAs is not taxed when earned, and investment income from an education IRA is tax-exempt when withdrawn to pay for a student’s education expenses. The maximum contribution to an education IRA in 2013 is \$2,000 per beneficiary. In 2013, the maximum contribution is phased down ratably for taxpayers with modified AGI between \$190,000 and \$220,000 if married filing jointly (\$95,000 and \$110,000 for other taxpayers).

102. *Student-loan interest.*—The baseline tax system accepts current law’s general rule limiting taxpayers’ ability to deduct non-business interest expenses. In contrast, taxpayers may claim an above-the-line deduction of up to \$2,500 on interest paid on an education loan. In 2013, the maximum deduction is phased down ratably for taxpayers with modified AGI between \$125,000 and \$155,000 if married filing jointly (\$60,000 and \$75,000 for other taxpayers).

103. Deduction for higher education expenses.—The baseline tax system would not allow a deduction for personal expenditures. In contrast, the Tax Code provides a maximum annual deduction of \$4,000 for qualified higher education expenses for taxpayers with adjusted gross income up to \$130,000 on a joint return (\$65,000 for other taxpayers). Taxpayers with adjusted gross income up to \$160,000 on a joint return (\$80,000 for other taxpayers) may deduct up to \$2,000. This provision expired on December 31, 2013.

104. Qualified tuition programs.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. Some States have adopted prepaid tuition plans, prepaid room and board plans, and college savings plans, which allow persons to pay in advance or save for college expenses for designated beneficiaries. Under current law, investment income, or the return on prepayments, is not taxed when earned, and is tax-exempt when withdrawn to pay for qualified expenses.

105. Student-loan bonds.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, interest earned on State and local bonds issued to finance student loans is tax-exempt under current law. The volume of all such private activity bonds that each State may issue annually is limited.

106. Bonds for private nonprofit educational institutions.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, under current law interest earned on State and local Government bonds issued to finance the construction of facilities used by private nonprofit educational institutions is not taxed.

107. Credit for holders of zone academy bonds.—The baseline tax system would not allow credits for particular activities, investments, or industries. Under current law, however, financial institutions that own zone academy bonds receive a non-refundable tax credit rather than interest. The credit is included in gross income. Proceeds from zone academy bonds may only be used to renovate, but not construct, qualifying schools and for certain other school purposes. The total amount of zone academy bonds that may be issued was limited to \$1.4 billion in 2009 and 2010. As of March 2010, issuers of the unused authorization of such bonds could opt to receive direct payment with the yield becoming fully taxable. An additional \$0.4 billion of these bonds with a tax credit was authorized to be issued before January 1, 2013.

108. U.S. savings bonds for education.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. Under current law, however, interest earned on U.S. savings bonds issued after December 31, 1989 is tax-exempt if the bonds are transferred to an educational institution to pay for educational expenses.

The tax exemption is phased out for taxpayers with AGI between \$112,050 and \$142,050 if married filing jointly (\$74,700 and \$89,700 for other taxpayers) in 2013.

109. Dependent students age 19 or older.—Under the baseline tax system, a personal exemption for the taxpayer is allowed. However, additional exemptions for targeted groups within a given filing status would not be allowed. In contrast, the Tax Code allows taxpayers to claim personal exemptions for dependent children who are over the age of 18 and under the age of 24 and who (1) reside with the taxpayer for over half the year (with exceptions for temporary absences from home, such as for school attendance), (2) are full-time students, and (3) do not claim a personal exemption on their own tax returns.

110. Charitable contributions to educational institutions.—The baseline tax system would not allow a deduction for personal expenditures. In contrast, the Tax Code provides taxpayers a deduction for contributions to nonprofit educational institutions. Moreover, taxpayers who donate capital assets to educational institutions can deduct the asset's current value without being taxed on any appreciation in value. An individual's total charitable contribution generally may not exceed 50 percent of adjusted gross income; a corporation's total charitable contributions generally may not exceed 10 percent of pre-tax income.

111. Employer-provided educational assistance.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. Under current law, however, employer-provided educational assistance is excluded from an employee's gross income even though the employer's costs for this assistance are a deductible business expense. The maximum exclusion is \$5,250 per taxpayer.

112. Special deduction for teacher expenses.—The baseline tax system would not allow a deduction for personal expenditures. In contrast, under current law educators in both public and private elementary and secondary schools, who work at least 900 hours during a school year as a teacher, instructor, counselor, principal or aide, may subtract up to \$250 of qualified expenses when figuring their adjusted gross income (AGI). This provision expired on December 31, 2013.

113. Discharge of student loan indebtedness.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, the Tax Code allows certain professionals who perform in underserved areas or specific fields, and as a consequence have their student loans discharged, not to recognize such discharge as income.

114. Qualified school construction bonds.—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code was modified in 2009 to provide a tax credit in lieu of interest to holders of qualified school construction bonds. The national vol-

ume limit is \$22.4 billion over 2009 and 2010. As of March 2010, issuers of such bonds could opt to receive direct payment with the yield becoming fully taxable.

115. *Work opportunity tax credit (WOTC).*—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code provides employers with a tax credit for qualified wages paid to individuals. The credit applies to employees who begin work on or before December 31, 2013 and who are certified as members of various targeted groups. The amount of the credit that can be claimed is 25 percent of qualified wages for employment less than 400 hours and 40 percent for employment of 400 hours or more. Generally, the maximum credit per employee is \$2,400 and can only be claimed on the first year of wages an individual earns from an employer. However, the credit for long-term welfare recipients can be claimed on second year wages as well and has a \$9,000 maximum. Also, certain categories of veterans are eligible for a higher maximum credit of up to \$9,600. Employees must work at least 120 hours to be eligible for the credit. Employers must reduce their deduction for wages paid by the amount of the credit claimed.

116. *Employer-provided child care exclusion.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, under current law up to \$5,000 of employer-provided child care is excluded from an employee's gross income even though the employer's costs for the child care are a deductible business expense.

117. *Employer-provided child care credit.*—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, current law provides a credit equal to 25 percent of qualified expenses for employee child care and 10 percent of qualified expenses for child care resource and referral services. Employer deductions for such expenses are reduced by the amount of the credit. The maximum total credit is limited to \$150,000 per taxable year.

118. *Assistance for adopted foster children.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. Taxpayers who adopt eligible children from the public foster care system can receive monthly payments for the children's significant and varied needs and a reimbursement of up to \$2,000 for non-recurring adoption expenses; special needs adoptions receive the maximum benefit even if that amount not spent. These payments are excluded from gross income under current law.

119. *Adoption credit and exclusion.*—The baseline tax system would not allow credits for particular activities. Instead, taxpayers can receive a tax credit for qualified adoption expenses under current law. The maximum credit is \$12,970 per child for 2013, and is phased-out ratably for taxpayers with modified AGI between \$194,580 and \$234,580. The credit amounts and the phase-out thresholds are indexed for inflation. Taxpayers

may also exclude qualified adoption expenses provided or reimbursed by an employer from income, subject to the same maximum amounts and phase-out as the credit. The same expenses cannot qualify for tax benefits under both programs; however, a taxpayer may use the benefits of the exclusion and the tax credit for different expenses.

120. *Employer-provided meals and lodging.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, under current law employer-provided meals and lodging are excluded from an employee's gross income even though the employer's costs for these items are a deductible business expense.

121. *Child credit.*—The baseline tax system would not allow credits for particular activities or targeted at specific groups. Under current law, however, taxpayers with children under age 17 can qualify for a \$1,000 partially refundable per child credit. Any unclaimed credit due to insufficient tax liability may be refundable – taxpayers may claim a refund for 15 percent of earnings in excess of a \$3,000 floor, up to the amount of unused credit. Alternatively, taxpayers with three or more children may claim a refund of the amount of payroll taxes paid in excess of EITC received (up to the amount of unused credit) if this results in a larger refund. The credit is phased out for taxpayers at the rate of \$50 per \$1,000 of modified AGI above \$110,000 (\$75,000 for single or head of household filers and \$55,000 for married taxpayers filing separately). After 2017 refundability is based on earnings in excess of \$10,000 indexed from 2000, rather than from \$3,000 (unindexed); taxpayers with three or more children may continue to use the alternative calculation.

122. *Child and dependent care expenses.*—The baseline tax system would not allow credits for particular activities or targeted at specific groups. In contrast, the Tax Code provides parents who work or attend school and who have child and dependent care expenses a tax credit. In 2013, expenditures up to a maximum \$3,000 for one dependent and \$6,000 for two or more dependents are eligible for the credit. The credit is equal to 35 percent of qualified expenditures for taxpayers with incomes of \$15,000. The credit is reduced to a minimum of 20 percent by one percentage point for each \$2,000 of income in excess of \$15,000.

123. *Disabled access expenditure credit.*—The baseline tax system would not allow credits for particular activities, investments, or industries. In contrast, the Tax Code provides small businesses (less than \$1 million in gross receipts or fewer than 31 full-time employees) a 50-percent credit for expenditures in excess of \$250 to remove access barriers for disabled persons. The credit is limited to \$5,000.

124. *Charitable contributions, other than education and health.*—The baseline tax system would not allow a deduction for personal expenditures. In contrast, the Tax Code provides taxpayers a deduction for contributions to charitable, religious, and certain other nonprofit organizations. Taxpayers who donate capital assets to charitable organizations can deduct the assets' current value without being taxed on any appreciation in value.

An individual's total charitable contribution generally may not exceed 50 percent of adjusted gross income; a corporation's total charitable contributions generally may not exceed 10 percent of pre-tax income.

125. Foster care payments.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. Foster parents provide a home and care for children who are wards of the State, under contract with the State. However, compensation received for this service is excluded from the gross incomes of foster parents; the expenses they incur are nondeductible.

126. Parsonage allowances.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, would be included in taxable income. Dedicated payments and in-kind benefits represent accretions to wealth that do not differ materially from cash wages. In contrast, the Tax Code allows an exclusion from a clergyman's taxable income for the value of the clergyman's housing allowance or the rental value of the clergyman's parsonage.

127. Indian employment credit.—The baseline tax system would not allow credits for particular activities, investments, or industries. Instead, it generally would seek to tax uniformly all returns from investment-like activities. In contrast, the Tax Code provides employers with a tax credit for qualified wages paid to employees who are enrolled members of Indian tribes. The amount of the credit that can be claimed is 20 percent of the excess of qualified wages and health insurance costs paid by the employer in the current tax year over the amount of such wages and costs paid by the employer in 1993. Qualified wages and health insurance costs with respect to any employee for the taxable year may not exceed \$20,000. Employees must live on or near the reservation where he or she works to be eligible for the credit. Employers must reduce their deduction for wages paid by the amount of the credit claimed. The credit does not apply to taxable years beginning after December 31, 2013.

Health

128. Employer-paid medical insurance and expenses.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, under current law, employer-paid health insurance premiums and other medical expenses (including long-term care) are deducted as a business expense by employers, but they are not included in employee gross income.

129. Self-employed medical insurance premiums.—Under the baseline tax system, all compensation and remuneration, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, under current law self-employed taxpayers may deduct their family health insurance premiums. Taxpayers without self-employment income are not eligible for this special deduction. The deduction is not available for any month in which the self-employed individual

is eligible to participate in an employer-subsidized health plan and the deduction may not exceed the self-employed individual's earned income from self-employment.

130. Medical and health savings accounts.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. Also, the baseline tax system would not allow a deduction for personal expenditures. In contrast, individual contributions to Archer Medical Savings Accounts (Archer MSAs) and Health Savings Accounts (HSAs) are allowed as a deduction in determining adjusted gross income whether or not the individual itemizes deductions. Employer contributions to Archer MSAs and HSAs are excluded from income and employment taxes. Archer MSAs and HSAs require that the individual have coverage by a qualifying high deductible health plan. Earnings from the accounts are excluded from taxable income. Distributions from the accounts used for medical expenses are not taxable. The rules for HSAs are generally more flexible than for Archer MSAs and the deductible contribution amounts are greater (in 2013, \$3,250 for taxpayers with individual coverage and \$6,450 for taxpayers with family coverage). Thus, HSAs have largely replaced MSAs.

131. Medical care expenses.—The baseline tax system would not allow a deduction for personal expenditures. In contrast, under current law personal expenditures for medical care (including the costs of prescription drugs) exceeding 7.5 percent of the taxpayer's adjusted gross income are deductible. For tax years beginning after 2012, only medical expenditures exceeding 10 percent of the taxpayer's adjusted gross income are deductible. However, for the years 2013, 2014, 2015 and 2016, if either the taxpayer or the taxpayer's spouse turns 65 before the end of the taxable year, the threshold remains at 7.5 percent of adjusted income.

132. Hospital construction bonds.—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, under current law interest earned on State and local government debt issued to finance hospital construction is excluded from income subject to tax.

133. Refundable Premium Assistance Tax Credit.—The baseline tax system would not allow credits for particular activities or targeted at specific groups. In contrast, for taxable years ending after 2013, the Tax Code provides a premium assistance credit to any eligible taxpayer for any qualified health insurance purchased through a Health Insurance Exchange. In general, an eligible taxpayer is a taxpayer with annual household income between 100% and 400% of the federal poverty level for a family of the taxpayer's size and that does not have access to affordable minimum essential health care coverage. The amount of the credit equals the lesser of (i) the actual premiums paid by the taxpayer for such coverage or (ii) the difference between the cost of a statutorily-identified benchmark plan offered on the exchange and a required payment by the taxpayer that increases with income.

134. Credit for employee health insurance expenses of small business.—The baseline tax system would not allow credits for particular activities or targeted at specific groups. In contrast, the Tax Code provides a tax credit to qualified small employers that make a certain level of non-elective contributions towards the purchase of certain health insurance coverage for its employees. To receive a credit, an employer must have fewer than 25 full-time-equivalent employees whose average annual full-time-equivalent wages from the employer are less than \$50,000 (indexed for taxable years after 2013). However, to receive a full credit, an employer must have no more than 10 full-time employees, and the average wage paid to these employees must be no more than \$25,000 (indexed for taxable years after 2013). A qualifying employer may claim the credit for any taxable year beginning in 2010, 2011, 2012, and 2013 and for up to two years for insurance purchased through a Health Insurance Exchange thereafter. For taxable beginning in 2010, 2011, 2012, and 2013, the maximum credit is 35 percent of premiums paid by qualified taxable employers and 25 percent of premiums paid by qualified tax-exempt organizations. For taxable years beginning in 2014 and later years, the maximum tax credit will increase to 50 percent of premiums paid by qualified taxable employers and 35 percent of premiums paid by qualified tax-exempt organizations.

135. Charitable contributions to health institutions.—The baseline tax system would not allow a deduction for personal expenditures. In contrast, the Tax Code provides individuals and corporations a deduction for contributions to nonprofit health institutions. Tax expenditures resulting from the deductibility of contributions to other charitable institutions are listed under the education, training, employment, and social services function.

136. Orphan drugs.—The baseline tax system would not allow credits for particular activities, investments, or industries. In contrast, under current law drug firms can claim a tax credit of 50 percent of the costs for clinical testing required by the Food and Drug Administration for drugs that treat rare physical conditions or rare diseases.

137. Blue Cross and Blue Shield.—The baseline tax system generally would tax all profits under the regular tax rate schedule. It would not allow preferentially low tax rates to apply to certain types or sources of income. In contrast, Blue Cross and Blue Shield health insurance providers in existence on August 16, 1986 and certain other nonprofit health insurers are provided exceptions from otherwise applicable insurance company income tax accounting rules that substantially reduce their tax liabilities, provided that their percentage of total premium revenue expended on reimbursement for clinical services provided to enrollees is not less than 85 percent for the taxable year.

138. Tax credit for health insurance purchased by certain displaced and retired individuals.—The baseline tax system would not allow credits for particular activities, investments, or industries. In contrast, the Trade Act of 2002 provides a refundable tax credit of 65 percent for the purchase of health insurance coverage by

individuals eligible for Trade Adjustment Assistance and certain Pension Benefit Guarantee Corporation pension recipients. The American Recovery and Reinvestment Act and a subsequent extension increased the credit to 80 percent in coverage months preceding March 2011. The Trade Adjustment Assistance Extension Act of 2011 extended an enhanced credit of 72.5% through December 2013, but eliminated the credit entirely beginning January 1, 2014.

139. Distributions for premiums for health and long-term care insurance.—Under the baseline tax system, all compensation, including dedicated and deferred payments, should be included in taxable income. In contrast, the Tax Code provides for tax-free distributions of up to \$3,000 from governmental retirement plans for premiums for health and long term care premiums of public safety officers.

Income Security

140. Railroad retirement benefits.—Under the baseline tax system, all compensation, including dedicated and deferred payments, should be included in taxable income. In contrast, railroad retirement benefits are not generally subject to the income tax unless the recipient's gross income reaches a certain threshold under current law. The threshold is discussed more fully under the Social Security function.

141. Workers' compensation benefits.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. However, workers compensation is not subject to the income tax under current law.

142. Public assistance benefits.—Under the reference law baseline tax system, gifts and transfers are not treated as income to the recipients. In contrast, the normal tax method considers cash transfers from the Government as part of the recipients' income, and thus, treats the exclusion for public assistance benefits under current law as a tax expenditure.

143. Special benefits for disabled coal miners.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. However, disability payments to former coal miners out of the Black Lung Trust Fund, although income to the recipient, are not subject to the income tax.

144. Military disability pensions.—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, most of the military pension income received by current disabled retired veterans is excluded from their income subject to tax.

145. Defined benefit employer plans.—Under the baseline tax system, all compensation, including deferred and dedicated payments, should be included in taxable income. In contrast, under current law certain contributions to defined benefit pension plans are excluded from an employee's gross income even though employers can deduct their contributions. In addition, the tax on the in-

vestment income earned by defined benefit pension plans is deferred until the money is withdrawn.

146. *Defined contribution employer plans.*—Under the baseline tax system, all compensation, including deferred and dedicated payments, should be included in taxable income. In contrast, under current law individual taxpayers and employers can make tax-preferred contributions to employer-provided 401(k) and similar plans (e.g. 403(b) plans and the Federal Government's Thrift Savings Plan). In 2013, an employee could exclude up to \$17,500 (indexed) of wages from AGI under a qualified arrangement with an employer's 401(k) plan. Employees age 50 or over could exclude up to \$23,000 in contributions (indexed). The defined contribution plan limit, including both employee and employer contributions, is \$51,000 in 2013 (indexed). The tax on contributions made by both employees and employers and the investment income earned by these plans is deferred until withdrawn.

147. *Individual Retirement Accounts (IRAs).*—Under the baseline tax system, all compensation, including deferred and dedicated payments, should be included in taxable income. In contrast, under current law individual taxpayers can take advantage of traditional and Roth IRAs to defer or otherwise reduce the tax on the return to their retirement savings. The IRA contribution limit is \$5,500 in 2012 (indexed); taxpayers age 50 or over are allowed to make additional "catch-up" contributions of \$1,000. Contributions to a traditional IRA are generally deductible but the deduction is phased out for workers with incomes above certain levels who, or whose spouses, are active participants in an employer-provided retirement plan. Contributions and account earnings are includible in income when withdrawn from traditional IRAs. Roth IRA contributions are not deductible, but earnings and withdrawals are exempt from taxation. Income limits also apply to Roth IRA contributions.

148. *Low and moderate-income savers' credit.*—The baseline tax system would not allow credits for particular activities or targeted at specific groups. In contrast, the Tax Code provides an additional incentive for lower-income taxpayers to save through a nonrefundable credit of up to 50 percent on IRA and other retirement contributions of up to \$2,000. This credit is in addition to any deduction or exclusion. The credit is completely phased out by \$59,500 for joint filers, \$444,250 for head of household filers, and \$29,500 for other filers in 2013.

149. *Self-Employed plans.*—Under the baseline tax system, all compensation, including deferred and dedicated payments, should be included in taxable income. In contrast, under current law self-employed individuals can make deductible contributions to their own retirement plans equal to 25 percent of their income, up to a maximum of \$51,000 in 2013. Total plan contributions are limited to 25 percent of a firm's total wages. The tax on the investment income earned by self-employed SEP, SIMPLE, and qualified plans is deferred until withdrawn.

150. *Employer-provided life insurance benefits.*—Under the baseline tax system, all compensation, including deferred and dedicated payments, should be included in taxable income. In contrast, under current law

employer-provided life insurance benefits are excluded from an employee's gross income (to the extent that the employer's share of the total costs does not exceed the cost of \$50,000 of such insurance) even though the employer's costs for the insurance are a deductible business expense.

151. *Employer-provided accident and disability benefits.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, and under current law, employer-provided accident and disability benefits are excluded from an employee's gross income even though the employer's costs for the benefits are a deductible business expense.

152. *Employer-provided supplementary unemployment benefits.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. Employers may establish trusts to pay supplemental unemployment benefits to employees separated from employment. Investment income earned by such trusts is exempt from taxation.

153. *Employer Stock Ownership Plan (ESOP) provisions.*—ESOPs are a special type of tax-exempt employee benefit plan. Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income. In contrast, employer-paid contributions (the value of stock issued to the ESOP) are deductible by the employer as part of employee compensation costs. They are not included in the employees' gross income for tax purposes, however, until they are paid out as benefits. In addition, the following special income tax provisions for ESOPs are intended to increase ownership of corporations by their employees: (1) annual employer contributions are subject to less restrictive limitations than other qualified retirement plans; (2) ESOPs may borrow to purchase employer stock, guaranteed by their agreement with the employer that the debt will be serviced by his payment (deductible by him) of a portion of wages (excludable by the employees) to service the loan; (3) employees who sell appreciated company stock to the ESOP may defer any taxes due until they withdraw benefits; and (4) dividends paid to ESOP-held stock are deductible by the employer.

154. *Additional deduction for the blind.*—Under the baseline tax system, the standard deduction is allowed. An additional standard deduction for a targeted group within a given filing status would not be allowed. In contrast, the Tax Code allows taxpayers who are blind to claim an additional \$1,500 standard deduction if single, or \$1,200 if married in 2013.

155. *Additional deduction for the elderly.*—Under the baseline tax system, the standard deduction is allowed. An additional standard deduction for a targeted group within a given filing status would not be allowed. In contrast, the Tax Code allows taxpayers who are 65 years or older to claim an additional \$1,500 standard deduction if single, or \$1,200 if married in 2013.

156. *Tax credit for the elderly and disabled.*—Under the baseline tax system, a credit targeted at a specific group within a given filing status or for particular

activities would not be allowed. In contrast, the Tax Code allows taxpayers who are 65 years of age or older, or who are permanently disabled, to claim a tax credit equal to 15 percent of the sum of their earned and retirement income. The amount to which the 15 percent rate is applied is limited to no more than \$5,000 for single individuals or married couples filing a joint return where only one spouse is 65 years of age or older or disabled, and up to \$7,500 for joint returns where both spouses are 65 years of age or older or disabled. These limits are reduced by one-half of the taxpayer's adjusted gross income over \$7,500 for single individuals and \$10,000 for married couples filing a joint return.

157. *Casualty losses.*—Under the baseline tax system, neither the purchase of property nor insurance premiums to protect its value are deductible as costs of earning income. Therefore, reimbursement for insured loss of such property is not included as a part of gross income, and uninsured losses are not deductible. In contrast, the Tax Code provides a deduction for uninsured casualty and theft losses of more than \$100 each, to the extent that total losses during the year exceed 10 percent of the taxpayer's adjusted gross income.

158. *Earned income tax credit (EITC).*—The baseline tax system would not allow credits for particular activities or targeted at specific groups. In contrast, the Tax Code provides an EITC to low-income workers at a maximum rate of 45 percent of income. For a family with one qualifying child, the credit is 34 percent of the first \$9,560 of earned income in 2013. The credit is 40 percent of the first \$13,430 of income for a family with two qualifying children, and it is 45 percent of the first \$13,430 of income for a family with three or more qualifying children. Low-income workers with no qualifying children are eligible for a 7.65 percent credit on the first \$6,370 of earned income. The credit is phased out at income levels and rates which depend upon how many qualifying children are eligible and marital status. In 2013, the phasedown for married filers begins at incomes \$5,340 greater than for otherwise similar unmarried filers. Earned income tax credits in excess of tax liabilities owed through the individual income tax system are refundable to individuals. After 2017, the additional benefit for families with three or more children will be eliminated and the marriage penalty relief will be reduced to \$3,000 (indexed from 2008).

Social Security

159. *Social Security benefits for retired workers.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, would be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. Thus, the portion of Social Security benefits that is attributable to employer contributions and earnings on employer and employee contributions (and not attributable to employee contributions) would be subject to tax. In contrast, the Tax Code may not tax all of the Social Security benefits that exceed the beneficiary's contributions from previously taxed income. Actuarially, previous-

ly taxed contributions generally do not exceed 15 percent of benefits, even for retirees receiving the highest levels of benefits. Up to 85 percent of recipients' Social Security and tier 1 railroad retirement benefits are included in (phased into) the income tax base if the recipient's provisional income exceeds certain base amounts. (Provisional income is equal to other items included in adjusted gross income plus foreign or U.S. possession income, tax-exempt interest, and one half of Social Security and tier 1 railroad retirement benefits.) The untaxed portion of the benefits received by taxpayers who are below the income amounts at which 85 percent of the benefits are taxable is counted as a tax expenditure.

160. *Social Security benefits for the disabled.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. Under current law, however, benefit payments from the Social Security Trust Fund for disability are fully or partially excluded from a beneficiary's gross income. (See provision number 161, Social Security benefits for retired workers.)

161. *Social Security benefits for dependents and survivors.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. Under current law, however, benefit payments from the Social Security Trust Fund for dependents and survivors are fully or partially excluded from a beneficiary's gross income. (See provision number 159, Social Security benefits for retired workers.)

Veterans Benefits and Services

162. *Veterans death benefits and disability compensation.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. In contrast, all compensation due to death or disability paid by the Veterans Administration is excluded from taxable income under current law.

163. *Veterans pension payments.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. Under current law, however, pension payments made by the Veterans Administration are excluded from gross income.

164. *G.I. Bill benefits.*—Under the baseline tax system, all compensation, including dedicated payments and in-kind benefits, should be included in taxable income because they represent accretions to wealth that do not materially differ from cash wages. Under current law, however, G.I. Bill benefits paid by the Veterans Administration are excluded from gross income.

165. **Tax-exempt mortgage bonds for veterans.**—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, under current law, interest earned on general obligation bonds issued by State and local governments to finance housing for veterans is excluded from taxable income.

General Government

166. **Public purpose State and local bonds.**—The baseline tax system generally would tax all income under the regular tax rate schedule. It would not allow preferentially low (or zero) tax rates to apply to certain types or sources of income. In contrast, under current law interest earned on State and local government bonds issued to finance public-purpose construction (e.g., schools, roads, sewers), equipment acquisition, and other public purposes is tax-exempt. Interest on bonds issued by Indian tribal governments for essential governmental purposes is also tax-exempt.

167. **Build America Bonds.**—The baseline tax system would not allow credits for particular activities or targeted at specific group. In contrast, the Tax Code in 2009 allowed State and local governments to issue taxable bonds through 2010 and receive a direct payment from Treasury equal to 35 percent of interest expenses. Alternatively, State and local governments could issue

taxable bonds and the private lenders receive the 35 percent credit which is included in taxable income.

168. **Deductibility of certain nonbusiness State and local taxes.**—Under the baseline tax system, a deduction for personal consumption expenditures would not be allowed. In contrast, the Tax Code allows taxpayers who itemize their deductions to claim a deduction for State and local income taxes (or, at the taxpayer's election, State and local sales taxes) and property taxes, even though these taxes primarily pay for services that, if purchased directly by taxpayers, would not be deductible. The ability for taxpayers to elect to deduct State and local sales taxes in lieu of State and local income taxes applies to taxable years beginning after December 31, 2003 and before January 1, 2014. (The estimates for this tax expenditure do not include the estimates for the deductibility of State and local property tax on owner-occupied homes. See item 59.)

Interest

169. **U.S. savings bonds.**—The baseline tax system would uniformly tax all returns to investments and not allow an exemption or deferral for particular activities, investments, or industries. In contrast, taxpayers may defer paying tax on interest earned on U.S. savings bonds until the bonds are redeemed.

APPENDIX

Performance Measures and the Economic Effects of Tax Expenditures

The Government Performance and Results Act of 1993 (GPRA) directs Federal agencies to develop annual and strategic plans for their programs and activities. These plans set out performance objectives to be achieved over a specific time period. Most of these objectives are achieved through direct expenditure programs. Tax expenditures – spending programs implemented through the tax code by reducing tax obligations for certain activities -- contribute to achieving these goals in a manner similar to direct expenditure programs.

Tax expenditures by definition work through the tax system and, particularly, the income tax. Thus, they may be relatively advantageous policy approaches when the benefit or incentive is related to income and is intended to be widely available.⁴ Because there is an existing public administrative and private compliance structure for the tax system, income based programs that require little oversight might be efficiently run through the tax system. In addition, some tax expenditures actually simplify the operation of the tax system (for example, the exclusion

for up to \$500,000 of capital gains on home sales). Tax expenditures also implicitly subsidize certain activities in a manner similar to direct expenditures. For example, exempting employer-sponsored health insurance from income taxation is equivalent to a direct spending subsidy equal to the forgone tax obligations for this type of compensation. Spending, regulatory or tax-disincentive policies can also modify behavior, but may have different economic effects. Finally, a variety of tax expenditure tools can be used, e.g., deductions; credits; exemptions; deferrals; floors; ceilings; phase-ins; phase-outs; and these can be dependent on income, expenses, or demographic characteristics (age, number of family members, etc.). This wide range of policy instruments means that tax expenditures can be flexible and can have very different economic effects.

Tax expenditures also have limitations. In many cases they add to the complexity of the tax system, which raises both administrative and compliance costs. For example, personal exemptions, deductions, credits, and phase-outs can complicate filing and decision-making. The income tax system may have little or no contact with persons who have no or very low incomes, and does not require information on certain characteristics of individuals used in some spending programs, such as wealth or duration of employment. These features may reduce the effectiveness of tax expenditures for addressing socioeconomic dispari-

⁴ Although this chapter focuses upon tax expenditures under the income tax, tax expenditures also arise under the unified transfer, payroll, and excise tax systems. Such provisions can be useful when they relate to the base of those taxes, such as excise tax exemption for certain types of consumption deemed meritorious.

ties. Tax expenditures also generally do not enable the same degree of agency discretion as an outlay program. For example, grant or direct Federal service delivery programs can prioritize activities to be addressed with specific resources in a way that is difficult to emulate with tax expenditures.

Outlay programs have advantages where the direct provision of government services is particularly warranted, such as equipping and maintaining the armed forces or administering the system of justice. Outlay programs may also be specifically designed to meet the needs of low-income families who would not otherwise be subject to income taxes or need to file a tax return. Outlay programs may also receive more year-to-year oversight and fine tuning through the legislative and executive budget process. In addition, many different types of spending programs include direct Government provision; credit programs; and payments to State and local governments, the private sector, or individuals in the form of grants or contracts provide flexibility for policy design. On the other hand, certain outlay programs may rely less directly on economic incentives and private-market provision than tax incentives, thereby reducing the relative efficiency of spending programs for some goals. Finally, spending programs, particularly on the discretionary side, may respond less rapidly to changing activity levels and economic conditions than tax expenditures.

Regulations may have more direct and immediate effects than outlay and tax-expenditure programs because regulations apply directly and immediately to the regulated party (i.e., the intended actor), generally in the private sector. Regulations can also be fine-tuned more quickly than tax expenditures because they can often be changed as needed by the Executive Branch without legislation. Like tax expenditures, regulations often rely largely on voluntary compliance, rather than detailed inspections and policing. As such, the public administrative costs tend to be modest relative to the private resource costs associated with modifying activities. Historically, regulations have tended to rely on proscriptive measures, as opposed to economic incentives. This reliance can diminish their economic efficiency, although this feature can also promote full compliance where (as in certain safety-related cases) policymakers believe that trade-offs with economic considerations are not of paramount importance. Also, regulations generally do not directly affect Federal outlays or receipts. Thus, like tax expenditures, they may escape the degree of scrutiny that outlay programs receive. Some policy objectives are achieved using multiple approaches. For example, minimum wage legislation, the earned income tax credit, and the food stamp program (SNAP) are regulatory, tax expenditure, and direct outlay programs, respectively, all having the objective of improving the economic welfare of low-wage workers and families.

A Framework for Evaluating the Effectiveness of Tax Expenditures

Across all major budgetary categories - from housing and health to space, technology, agriculture, and national

defense - tax expenditures make up a significant portion of Federal activity and affect every area of the economy. For these reasons, a comprehensive evaluation framework that examines incentives, direct results, and spillover effects will benefit the budgetary process by informing decisions on tax expenditure policy.

As described above, tax expenditures, like spending and regulatory programs, have a variety of objectives and economic effects. These include: encouraging certain types of activities (e.g., saving for retirement or investing in certain sectors); increasing certain types of after-tax income (e.g., favorable tax treatment of Social Security income); and reducing private compliance costs and Government administrative costs (e.g., the exclusion for up to \$500,000 of capital gains on home sales). Some of these objectives are well suited to quantitative measurement and evaluation, while others are less well suited.

Performance measurement is generally concerned with inputs, outputs, and outcomes. In the case of tax expenditures, the principal input is usually the revenue effect. Outputs are quantitative or qualitative measures of goods and services, or changes in income and investment, directly produced by these inputs. Outcomes, in turn, represent the changes in the economy, society, or environment that are the ultimate goals of programs. Evaluations assess whether programs are meeting intended goals, but may also encompass analyzing whether initiatives are superior to other policy alternatives.

The Administration is working towards examining the objectives and effects of the wide range of tax expenditures in our budget, despite challenges related to data availability, measurement, and analysis. Evaluations include an assessment of whether tax expenditures are achieving intended policy results in an efficient manner, with minimal burdens on individual taxpayers, consumers, and firms; and an examination of possible unintended effects and their consequences.

As an illustration of how evaluations can inform budgetary decisions, consider education, and research investment credits.

Education. There are millions of individuals taking advantage of tax credits designed to help pay for educational expenses. There are a number of different credits available as well as other important forms of Federal support for higher education such as subsidized loans and grants. An evaluation would explore the possible relationships between use of the credits and the use of loans and grants, seeking to answer, for example, whether the use of credits reduce or increase the likelihood of the students applying for loans. Such an evaluation would allow stakeholders to determine the most effective program - whether it is a tax credit, a subsidized loan, or a grant.

Investment. A series of tax expenditures reduce the cost of investment, both in specific activities such as research and experimentation, extractive industries, and certain financial activities and more generally throughout the economy, through accelerated depreciation for plant and equipment. These provisions can be evaluated along a number of dimensions. For example, it is useful to consider the strength of the incentives by measuring their ef-

fects on the cost of capital (the return which investments must yield to cover their costs) and effective tax rates. The impact of these provisions on the amounts of corresponding forms of investment (e.g., research spending, exploration activity, equipment) might also be estimated. In some cases, such as research, there is evidence that the investment can provide significant positive externalities—that is, economic benefits that are not reflected in the market transactions between private parties. It could be useful to quantify these externalities and compare them with the size of tax expenditures. Measures could also indicate the effects on production from these investments such as numbers or values of patents, energy production and reserves, and industrial production. Issues to be considered include the extent to which the preferences increase production (as opposed to benefiting existing output) and their cost-effectiveness relative to other policies. Analysis could also consider objectives that are more difficult to measure but still are ultimate goals, such as promoting the Nation's technological base, energy security, environmental quality, or economic growth. Such an assessment is likely to involve tax analysis as well as consideration of non-tax matters such as market structure, scientific, and other information (such as the effects of increased domestic fuel production on imports from various regions, or the effects of various energy sources on the environment).

The tax proposals subject to these analyses include items that indirectly affect the estimated value of tax expenditures (such as changes in income tax rates), proposals that make reforms to improve tax compliance and administration, as well as proposals which would change, add, or delete tax expenditures.

Barriers to Evaluation. Developing a framework that is sufficiently comprehensive, accurate, and flexible is a significant challenge. Evaluations are constrained by the availability of appropriate data and challenges in economic modeling:

1. **Data availability.** Data may not exist, or may not exist in an analytically appropriate form, to conduct rigorous evaluations of certain types of expenditures. For example, measuring the effects of tax expenditures designed to achieve tax neutrality for individuals and firms earning income abroad, and foreign firms could require data from foreign governments or firms which are not readily available.
2. **Analytical constraints.** Evaluations of tax expenditures face analytical constraints even when data are available. For example, individuals might have access to several tax expenditures and programs aimed at improving the same outcome. Isolating the effect of a single tax credit is challenging absent a well-specified research design.
3. **Resources.** Tax expenditure analyses are seriously constrained by staffing considerations. Evaluations typically require expert analysts who are often engaged in other more competing areas of work related to the budget.

The Executive Branch is focused on addressing these challenges to lay the foundation for the analysis of tax expenditures comprehensively, alongside evaluations of the effectiveness of direct spending initiatives.

Current Administration Proposals on Tax Expenditures

The Administration considers performance measurement, evaluations, and the economic effects of tax expenditures each year in its deliberation for the Budget and proposals are informed by these analyses. The President's National Commission on Fiscal Responsibility and Reform submitted a report in 2010 in which they said that the income tax system is unduly complicated and that the government should "sharply reduce rates, broaden the base, simplify the tax code, and reduce the many 'tax expenditures'—another name for spending through the tax code."

The current Budget and enacted Administration policies include several proposals that would change existing tax expenditures to raise revenue, eliminate ineffective or counterproductive tax expenditures, and enhance effective tax expenditures. The tax expenditure proposals in the budget further the Administration's goals of economic recovery and growth, clean and secure energy, a world-class education for all Americans, and fairness in the tax code. Some of these proposals are highlighted below.

Reduce the value of certain tax expenditures. The Administration proposes to limit the tax rate at which upper-income taxpayers can use itemized deductions and other tax preferences to reduce tax liability to a maximum of 28 percent, a limitation that would affect only the highest-income households. The limit would apply to all itemized deductions, tax-exempt interest, employer-sponsored health insurance, deductions and income exclusions for employee retirement contributions, and certain above-the-line deductions, effective for taxable years beginning after December 31, 2014. These are among the largest tax expenditures. This proposal would make the tax code more equitable because the value of the tax expenditure as a percentage of the deduction is proportional to one's tax bracket, so it is less valuable to those in lower brackets.

Enhance and make permanent the Research and Experimentation (R&E) credit and modify and make permanent the Renewable Energy Production Tax Credit. The extension of the R&E credit every year creates uncertainty reducing firms' incentive to expand their research activities. For this reason, and more generally to achieve the President's R&D goals, the Budget proposes making the R&E credit permanent. For similar reasons, the Budget also proposes to permanently extend and enhance the production tax credit for renewable energy property.

Make permanent the American Opportunity Tax Credit (AOTC), the expansion of the EITC for larger families, EITC marriage penalty relief, and the refundability of the child tax credit. These provisions were extended through 2017 in ATRA and the Budget assumes in its baseline that these provisions would be permanently extended. Although permanent extension would increase the cost of

these tax expenditures, it would increase the equity of the overall tax system and provide benefits to low and middle income families.

Eliminate a range of tax expenditures in the context of business tax reform. The President's framework for business tax reform calls for eliminating dozens of tax loopholes and subsidies and reinvesting the revenue to lower the corporate tax rate to 28 percent. Consistent with the framework, the Budget includes a number of proposals to eliminate inefficient business tax expenditures. For

example, current law provides a number of credits and deductions that are targeted towards certain oil, gas, and coal activities. These tax preferences run counter to our policies for reducing greenhouse gas emissions. In accordance with the President's agreement at the G-20 summit in Pittsburgh to phase out subsidies for fossil fuels so that we can transition to a 21st century energy economy, the Administration proposes to repeal a number of tax preferences available for fossil fuels.

