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ESTIMATES OF FEDERAL TAX
EXPENDITURES

COMMITTEE ON WAYS AND MEANS

PREPARED BY THE STAFFS

OF THE

TREASURY DEPARTMENT

AND

JOINT COMMITTEE ON INTERNAL
REVENUE TAXATION



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UNITED STATES OF AMERICA
DEPARTMENT OF THE TREASURY
BUREAU OF INTERNAL REVENUE
WASHINGTON, D. C.
COMMITTEE ON THE REVENUE

REPORT OF THE COMMITTEE
ON THE REVENUE
FOR THE YEAR 1900
IN RESPONSE TO A RESOLUTION
PASSED BY THE HOUSE OF REPRESENTATIVES
JANUARY 10, 1900



FEDERAL TAX EXPENDITURES

In the Senate version of the Revenue Act of 1971, a provision added on the floor would have required the inclusion in the budget of estimates of losses in revenue from provisions of the Federal income tax laws and also estimates of indirect "expenditures" through the operation of the Federal tax laws. Data of this type have commonly become known as "tax expenditures." The statement made by the conferees in this respect is as follows:

"The conferees concluded that it would be more appropriate to have such estimates of tax expenditures made by the Treasury Department and to have the estimates submitted annually to the Committee on Ways and Means of the House, the Committee on Finance of the Senate, and the Joint Committee on Internal Revenue Taxation. It is expected that these tax expenditure reports to the tax committees will initially be modeled after similar reports previously made and included in the annual reports of the Secretary of the Treasury in 1968 and 1970. Modifications may, of course, be made from time to time in consultation with the tax committees. In addition to making these reports to the tax committees on an annual basis, the Treasury Department may desire to include these data on tax expenditures in the annual report of the Secretary of the Treasury. The Treasury Department has indicated its willingness to submit information to the tax committees in the manner indicated above and as a result the amendment no longer appears necessary."

The Staffs of the Treasury Department and Joint Committee did cooperate in the preparation of such a report last year. This pamphlet, which is a continuation of this cooperative effort, presents data for 1972 and reproduces the data for calendar years 1967 through 1971 which were contained in the report issued on October 4, 1972.

In general terms "tax expenditure" items are intended to represent the amount of tax reductions which occur because of the allowance of an exclusion, deduction, preferential rate of tax, or deferral of tax liability. There are differences in points of view as to the "tax expenditure" concept,¹ including differences as to the items which should be included in, and excluded from, such a listing. Questions have also been raised as to whether there should also be included in such an analysis those items which are taxed more heavily than income generally (such as corporate income) or deductions which are subjected to special limitations (such as capital losses). In this report the staffs have not attempted to consider any changes in the items listed as "tax expenditures." Instead, the items included in this report are those which have previously been included in any of the earlier reported versions of tax expenditure estimates made by the Treasury Department prior to the Revenue Act of 1971 plus items in the Revenue Act of 1971 which are of a similar character. Among items not included as tax expenditures are the personal exemptions and the minimum standard deduction.

¹ See, e.g., the criticism in Bittker, "Accounting for Federal Tax Subsidies in the National Budget," XXII *National Tax Journal* 244 and the reply in Surrey and Hellmuth, "The Tax Expenditure Budget—Response to Professor Bittker," XXII *National Tax Journal* 528.

This report includes two tables. Table 1 shows estimated Federal income tax expenditures for the calendar years 1967 through 1972. The 1971 and 1972 tabulations are broken down into effects on corporate income tax liability and effects on individual income tax liability. Only the 1972 data represent a new tabulation. The data shown in this table are broken down into categories which are comparable to those in the functional classification of budget expenditures. The report also includes a table (Table 2) showing the estimated distribution, by adjusted gross income class, of the decrease in individual income tax liability estimated to result from tax expenditure items affecting such liability.

The purpose of these tax expenditure data is to provide information as to the economic benefits provided by the tax laws to the various sectors of the economy. To aid in the analysis, the cost and beneficiaries (in terms of areas of activity) are shown by the same functional categories as outlays in the Federal budget. The listing of any of these provisions involves no direct, or indirect, presumption about the desirability of any of them in terms of public policy. These tables, however, are intended as a tool which may be helpful to the tax committees of Congress in reviewing various provisions of the tax laws.

The estimates of tax expenditures are difficult to determine and are subject to important limitations. It is believed, however, that despite these limitations, the order of magnitude of the amounts involved may be helpful to the tax committees.

The major limitations with respect to the estimates of tax expenditures are:

1. The estimate of each tax expenditure item is made independently of any other tax expenditure item. As a result, if two or more items were to be eliminated, the result of the combination of changes being made at the same time might produce a lesser or greater revenue effect than the sum of the amounts shown for each item individually. This, of course, also means that the addition of the various tax expenditure items is of quite limited usefulness. This is why totals are not shown for table 1, except in a footnote.

2. In the case of many of the items, especially those for which information is not available on tax returns, the lack of data makes estimates quite tenuous. Where information is not available on tax returns, it has been necessary to obtain information from whatever sources are available, and, when sources are limited, to make assumptions on which to base the estimates.

3. The estimates for the various tax expenditure items do not take into account any effects that the removal of one or more of the items might have on investment patterns, consumption, or other aspects of economic activity. In other words, the estimates shown do not take into account the induced effects of changing the provisions. Repeal of a provision, therefore, would not necessarily raise the revenue associated with removal of that provision.

4. Often, tax expenditure items which have been added in recent years do not become fully effective until the lapse of several years. As a result, the eventual annual cost of some items added in recent years is not fully reflected in the year 1972. Conversely, if various items now in the law were to be eliminated, it is unlikely, in many cases, that the full revenue effects shown would be realized until an extended period of years has passed.

5. In some cases, if a tax expenditure item were to be eliminated, it is probable that Congress would, at least to some extent, desire to deal with the underlying problem by a direct expenditure program. The effect of any such program is not taken into account in the estimates shown. In addition, if some of these provisions were removed from the tax laws, this removal might be accompanied by revisions in tax rates, personal exemptions or the minimum standard deduction, as has happened in the past. This has not been taken into account in the estimates.

6. There are features of the law which are not taken into account in the estimates shown. For example, personal exemptions, the minimum standard deduction, the foreign tax credit, and the effect of income splitting and head-of-household treatment, as well as the graduation in the rate structure of the individual income tax, are not taken into account in these tables. Also, the effect of estate and gift taxes is not shown nor is the interrelationship of these provisions with some of the tax expenditure items taken into account.

7. Differences in personal income levels and corporate profits can also account for differences in the cost of tax expenditure items from year to year. Also, some tax expenditure items themselves may be larger or smaller from year to year, wholly independent of tax considerations.

TABLE 1—ESTIMATED FEDERAL INCOME TAX EXPENDITURES,¹ CALENDAR YEARS 1967-72²

[In millions of dollars]

Item	1971					1972	
	Corpo- rations	Indi- viduals	Total	Corpo- rations	Indi- viduals	Total	
NATIONAL DEFENSE							
Exclusion of benefits and allowances to Armed Forces personnel.....			500			3 700	
INTERNATIONAL AFFAIRS							
Exemption for certain income earned abroad by U.S. citizens.....			40			50	
Exclusion of income earned by individuals in U.S. possessions.....			10			10	
Western Hemisphere trade corporations.....			50			50	
Exclusion of gross-up on dividends of less-developed country corporations.....			50			60	
Deferral of income of controlled foreign corporations.....			150			3 325	
Exclusion of income earned by corporations in U.S. possessions.....			70			80	
Deferral of income of domestic international sales corporations.....						100	
AGRICULTURE							
Farming: Expensing and capital gain treatment.....			800			900	
Timber: Capital gain treatment for certain income.....			130			175	
NATURAL RESOURCES							
Expensing of exploration and development costs.....			300			3 4 650	
Excess of percentage over cost depletion.....			1,300			3 1,700	
Capital gain treatment of royalties on coal and iron ore.....			5			5	
COMMERCE AND TRANSPORTATION							
Investment credit.....			2,300			3,800	
Depreciation on buildings (other than rental housing) in excess of straight-line.....			500			500	
Asset depreciation range.....						3 860	
Dividend exclusion.....			225			300	
Capital gains: Corporation (other than farming and timber) ³			500			400	
Capital gains: Individuals (other than farming and timber) ³			(⁶)			7,000	
Bad debt reserves of financial institutions in excess of actual.....			600			7 400	
Exemption of credit unions.....			40			3 90	
Deductibility of interest on consumer credit.....			1,300			3 1,100	
Expensing of research and development expenditures.....			500			570	
\$25,000 surtax exemption.....			1,800			2,500	
Deferral of tax on shipping companies.....			10			30	
Rail freight car amortization.....						3 80	

HOUSING AND COMMUNITY DEVELOPMENT

Deductibility of interest on mortgages on owner-occupied homes	1,900	2,200	2,600	2,800	2,400	2,400	3,500	3,500
Deductibility of property taxes on owner-occupied homes	1,800	2,350	2,800	2,900	2,700	2,700	3,250	3,250
Depreciation on rental housing in excess of straight-line	250	250	275	255	200	500	250	600
Housing rehabilitation					15	25	25	40

HEALTH, LABOR, AND WELFARE

Disability insurance benefits	(6)	100	120	130	155	155	175	175
Provisions relating to aged, blind, and disabled:								
Combined cost for additional exemption, retirement income credit, and exclusion of OASDHI for aged	2,300	2,700	2,800	2,950	3,250	3,250	3,550	3,550
Additional exemption for blind	10	10	10	10	10	10	10	10
Sick pay exclusion	85	95	105	105	120	120	225	225
Exclusion of unemployment insurance benefits	300	325	350	400	800	800	700	700
Exclusion of workmen's compensation benefits	150	180	210	210	320	320	375	375
Exclusion of public assistance benefits	50	50	50	50	65	65	65	65
Net exclusion of pension contributions and earnings:								
Plans for employees	3,000	4,000	3,150	3,075	3,650	3,650	4,000	4,000
Plans for self-employed persons	60	135	160	175	250	250	200	200
Exclusion of other employee benefits:								
Premiums on group term life insurance	400	400	440	440	500	500	550	550
Deductibility of accident and accidental death premiums	25	25	25	25	30	30	35	35
Medical insurance premiums and medical care	1,100	1,400	1,450	1,450	2,000	2,000	2,500	2,500
Privately financed supplementary unemployment benefits	25	15	15	20	5	5	5	5
Meals and lodging	150	165	170	170	170	170	170	170
Exclusion of interest on life insurance savings	900	1,000	1,050	1,050	1,100	1,100	1,200	1,200
Deductibility of charitable contributions (other than education)	2,200	3,000	3,450	3,550	3,200	3,200	3,100	3,100
Deductibility of medical expenses	1,500	1,600	1,700	1,700	1,900	1,900	1,900	1,900
Deductibility of child and dependent care expenses	25	25	25	25	30	30	180	180
Deductibility of casualty losses	70	80	80	80	165	165	150	150
Excess of percentage standard deduction over minimum standard deduction	93,200	93,600	3,800	3,000	700	700	1,040	1,040
Pollution control amortization			15	15	15	15	25	25
Credit for employing public assistance recipients under WIN program							5	5
5-year amortization of child care facilities							5	5

EDUCATION

Parental personal exemption for student age 19 or over	500	500	525	500	550	550	640	640
Deductibility of contributions to educational institutions	170	200	200	200	275	275	275	275
Exclusion of scholarships and fellowships	50	60	60	60	110	110	125	125

VETERANS BENEFITS AND SERVICES

Exclusion of certain veterans' benefits	550	600	600	650	700	700	480	480
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GENERAL GOVERNMENT

Political contributions							100	100
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See footnotes at end of table, p. 6.

(Continued)

TABLE 1.—ESTIMATED FEDERAL INCOME TAX EXPENDITURES,¹ CALENDAR YEARS 1967-72 ²—Continued

[In millions of dollars]

Item	1971				1972					
	1967	1968	1969	1970	Corpo- rations	Indi- viduals	Total	Corpo- rations	Indi- viduals	Total
AID TO STATE AND LOCAL FINANCING										
Exemption of interest on State and local debt-----	1,800	2,000	2,200	2,300	1,800	800	2,600	1,900	1,000	³ 2,900
Deductibility of nonbusiness State and local taxes (other than on owner-occupied homes) --	2,800	4,150	5,100	5,600	-----	5,600	5,600	-----	5,300	5,300
Total-----	(¹⁰)	(¹⁰)	(¹⁰)	(¹⁰)	(¹⁰)	(¹⁰)	(¹⁰)	(¹⁰)	(¹⁰)	(¹⁰)

¹ Estimates are prepared on an individual basis for each item on the assumption that the item would be eliminated from the law without any other changes in the law with respect to the other items. If two or more changes in the law are made, the aggregate revenue effect will frequently not equal the sum of the revenue effects of the individual changes. Accordingly, the costs of the items are not additive.

² Roughly reflect fiscal years 1968 through 1973.

³ Changes in the 1972 figures as compared to 1971 which are due wholly or in part to revised data and/or new sources of data and/or improved estimating methods.

⁴ The estimate for 1972 considers this tax expenditure in isolation rather than in conjunction with percentage depletion as has been done for the years 1967-71.

⁵ Assumes present restriction on capital losses is retained.

⁶ Not available.

⁷ This will decline over time as present law becomes fully effective.

⁸ This item is being superseded by use of the investment credit.

⁹ Standard deduction.

¹⁰ As explained more fully in the text and in footnote 1, these totals are of limited significance and utility. However, as a matter of convenience the mathematical sums of the respective 10 columns are given here: \$36,550,000,000; \$44,140,000,000; \$46,635,000,000; \$43,945,000,000; \$9,860,000,000; \$41,850,000,000; \$51,710,000,000; \$13,350,000,000; \$46,460,000,000; and \$59,810,000,000. Much of the increase in the total figures given for 1971 and 1972 over that for 1970 is due to the fact that the 1970 figure does not include any estimate for capital gains of individuals while the 1971 and 1972 totals include \$5,600,000,000 and \$7,000,000,000, respectively.

Note: Changes in the figures from year to year not only reflect changes in the tax laws, in utilization of the items and in personal income and profit levels but also, in some instances, reflect revised and/or new sources of data and/or improved estimating methods.

TABLE 2.—ESTIMATED DISTRIBUTION OF SELECTED ITEMS OF TAX PREFERENCES OF INDIVIDUALS BY ADJUSTED GROSS INCOME CLASS, CALENDAR YEAR 1972

[In millions of dollars]

Adjusted gross income class	Exclusion of benefits and allowances to Armed Forces personnel	Exemption for certain income earned abroad by U.S. citizens	Exclusion of income earned by individuals in U.S. possessions	Deferral of income of foreign controlled subsidiaries	Farming: Expensing and capital gain treatment	Timber: Capital gain treatment for certain income	Expensing of exploration and development costs	Excess of percentage over cost depletion	Investment credit	Depreciation on buildings (other than rental housing) in excess of straight-line	Asset depreciation range	Dividend exclusion
0 to \$3,000	15	(1)	(1)	(1)	15	(1)	(1)	1	(1)	1	(1)	2
\$3,000 to \$5,000	150	1	(1)	(1)	50	2	1	5	45	3	(1)	10
\$5,000 to \$7,000	180	3	1	(1)	90	2	1	4	55	5	(1)	18
\$7,000 to \$10,000	130	5	1	(1)	130	3	2	11	95	10	(1)	27
\$10,000 to \$15,000	115	7	2	1	170	4	9	18	125	19	1	56
\$15,000 to \$20,000	55	16	3	1	100	3	7	20	90	17	1	55
\$20,000 to \$50,000	50	17	3	6	185	9	17	75	185	58	4	109
\$50,000 to \$100,000	4	1	(1)	6	60	8	11	61	80	36	2	20
\$100,000 and over	1	(1)	(1)	11	50	19	22	105	75	21	1	3
Total	700	50	10	25	850	50	70	300	750	170	10	300

¹ Less than \$500,000.

(Continued)

TABLE 2.—ESTIMATED DISTRIBUTION OF SELECTED ITEMS OF TAX PREFERENCES OF INDIVIDUALS BY ADJUSTED GROSS INCOME CLASS, CALENDAR YEAR 1972—Continued

[In millions of dollars]

Adjusted gross income class	Provisions relating to aged, blind, and disabled											
	Deductibility of interest on consumer credit	Deductibility of interest on mortgages on owner-occupied homes	Deductibility of property taxes on owner-occupied homes	Depreciation on rental housing in excess of straight-line	Housing re-habilitation	Disability insurance benefits	Combined cost for additional exemption, retirement income credit, and exclusion of OASDHI for aged	Additional exemption for blind	Sick pay exclusion	Exclusion of unemployment insurance benefits	Exclusion of workmen's compensation benefits	Exclusion of public assistance benefits
0 to \$3,000	(1)	(1)	5	1	(1)	30	880	1	8	60	12	25
\$3,000 to \$5,000	10	15	25	4	(1)	45	820	2	16	95	26	20
\$5,000 to \$7,000	40	85	95	7	(1)	35	460	2	18	95	41	15
\$7,000 to \$10,000	145	310	240	14	(1)	35	640	2	34	160	66	5
\$10,000 to \$15,000	275	845	590	28	1	12	265	1	62	200	96	(1)
\$15,000 to \$20,000	235	835	640	25	1	7	135	1	55	60	63	(1)
\$20,000 to \$50,000	285	1,160	1,135	86	3	7	235	1	27	25	65	(1)
\$50,000 to \$100,000	60	195	340	53	8	3	75	(1)	4	5	5	(1)
\$100,000 and over	50	55	180	32	12	1	40	(1)	1	(1)	1	(1)
Total	1,100	3,500	3,250	250	25	175	3,550	10	225	700	375	65

1 Less than \$500,000.

(Continued)

TABLE 2.—ESTIMATED DISTRIBUTION OF SELECTED ITEMS OF TAX PREFERENCES OF INDIVIDUALS BY ADJUSTED GROSS INCOME CLASS, CALENDAR YEAR 1972—Continued

[In millions of dollars]

Adjusted gross income class	Net exclusion of pension contributions and earnings		Exclusion of other employee benefits						Deductibility			Deductibility of casualty losses
	Plans for employees	Plans for self-employed	Premiums on term group life insurance	Deductibility of accidental death premiums	Medical insurance of premiums and medical care	Privately financed supplementary unemployment benefits	Meals and lodging	Exclusion of interest on life insurance savings	Deductibility of charitable contributions (other than education)	Deductibility of medical expenses	Deductibility of child and dependent care expense	
0 to \$3,000	45	(1)	10	(1)	45	(1)	3	10	5	5	1	(1)
\$3,000 to \$5,000	150	(1)	40	2	180	(1)	13	35	20	60	12	5
\$5,000 to \$7,000	240	1	50	3	225	1	22	65	80	155	21	5
\$7,000 to \$10,000	580	2	95	6	430	1	33	105	195	300	36	10
\$10,000 to \$15,000	1,080	5	150	10	675	2	37	175	410	460	42	25
\$15,000 to \$20,000	740	9	90	5	400	1	27	160	380	320	43	30
\$20,000 to \$50,000	885	93	95	6	420	(1)	28	400	820	435	25	40
\$50,000 to \$100,000	195	76	15	2	85	(1)	5	130	450	115	—	15
\$100,000 and over	85	14	5	1	40	(1)	2	120	740	50	—	20
Total	4,000	200	550	35	2,500	5	170	1,200	3,100	1,900	180	150

¹ Less than \$500,000.

(Continued)

TABLE 2.—ESTIMATED DISTRIBUTION OF SELECTED ITEMS OF TAX PREFERENCES OF INDIVIDUALS BY ADJUSTED GROSS INCOME CLASS, CALENDAR YEAR 1972—Continued

[In millions of dollars]

Adjusted gross income class	Excess of percentage standard deduction over minimum standard deduction	Capital gains: individuals	Parental personal exemption for student age 19 or over	Deductibility of contributions to educational institutions	Exclusion of scholarships and fellowships	Exclusion of certain veterans' benefits	Tax credit or deduction for political contributions	Exemption of interest on State and local debt	Deductibility of nonbusiness State and local taxes (other than on owner occupied homes)
0 to \$3,000	0	20	(1)	(1)	4	20	(1)	5	(1)
\$3,000 to \$5,000	1	70	8	3	26	45	1	(1)	30
\$5,000 to \$7,000	12	120	39	7	32	50	2	(1)	110
\$7,000 to \$10,000	63	190	102	20	26	110	7	5	335
\$10,000 to \$15,000	609	340	207	58	19	140	21	10	785
\$15,000 to \$20,000	254	340	122	70	12	60	17	25	835
\$20,000 to \$50,000	98	1,260	69	90	6	45	37	125	1,770
\$50,000 to \$100,000	2	1,080	72	20	(1)	9	11	375	770
\$100,000 and over	1	3,580	21	7	(1)	1	4	455	665
Total	1,040	7,000	640	275	125	480	100	1,000	5,300

¹ Less than \$500,000.