Order Code RS20264
Updated January 14, 2003

CRS Report for Congress

Received through the CRS Web

Tax Activity in the 107th Congress

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Summary

After passing a major multi-year tax cut in Mid-2001 (which was sunsetted after 10 years) and a stimulus bill in 2002, Congress considered, but did not complete, work on energy tax subsidies, tax incentives for charitable giving deductions, pension diversification in the wake of the ENRON problems, and tax shelters. The House passed several bills that would make the multiyear tax cut permanent as well as a bill to speed up certain provisions. This report will not be updated.

In the first half of 2001, a major multi-year tax cut was enacted and signed into law. The bill was passed with a sunset provision because there were not enough votes to set aside a budget rule. Several bills passed the House in 2002 to make the tax cut or parts of it permanent (H.R. 586 to make all provisions permanent on April 18, H.R. 2143 to make the estate tax repeal permanent on June 6, H.R. 4019 to make marriage tax relief provisions permanent on June 13). H.R. 4931 to make the retirement and pension provisions permanent was passed on June 21. The House also passed H.R. 4626, which would speed up marriage relief provisions on May 22.

The terrorist attacks of September 11 led to consideration of a stimulus package which was enacted and signed into law in March of 2002.

More detail on both of these bills is provided below.

While revenue concerns limited the consideration of some tax changes, the House, on July 19, approved H.R. 7, a bill to expand tax benefits for charitable giving and charities. H.R. 7 is estimated to cost $13.3 billion over 10-years, with about half the cost associated with a capped above-the-line deduction for charitable contributions for non-itemizers. This bill is a considerably scaled back version of the President's faith-based initiative that would have cost $80 billion. About half of the cost of H.R. 7 is due to allowing an above-the-line deduction for charitable giving by those who do not itemize deductions. The revenue cost was limited, however, because there was a cap on the deductions gradually rising to $200.. Singles would have limits half as big. The bill also includes provisions for tax free distributions from individual retirement accounts to charities, raising the cap on corporate charitable contributions, modify excise taxes on net investment income of charities and make a number of minor changes. The Senate Finance Committee approved a version of the Lieberman-Santorum bill (S. 1924) as substitute for H.R. 7 which included a temporary non-itemizer's deduction with a floor and a ceiling and several other provisions. The bill would also included revenue offsets including provisions to address tax shelters (S. 2498 and S. 2119).

On June 19, the Ways and Means Committee approved H.R. 4969, a bill to provide long term care relief, costing $5.3 billion over 10 years.

On July 11, Ways and Means Chairman Thomas introduced H.R. 5095, a bill that would repeal the ETI (export) benefits, restrict tax shelters associated with international activities and provide a number of tax benefits for multinational operations. The bill did not see further action.

The House (August 2, 2001) and Senate (April 25, 2002) passed H.R. 4 which includes a series of tax subsidies and incentives for energy. In response to the ENRON problem, the House has passed H.R. 3762 which requires permitting some diversification in 401(k) plans (H.R. 3762, April 12). The Senate approved a similar bill, S. 1971 which was reported in October, which also contained provisions concerning executive compensation and formally excluded incentive stock options from payroll tax withholding. On June 19, the Ways and Means Committee approved H.R. 4969, a bill to provide long term care relief, costing $5.3 billion over 10 years. In addition, general concerns about stock market performance and the slowly growing economy also led to the consideration of an investor relief package (H.R. 5553, reported out of the Ways and Means Committee) which included speedups in IRA and pension contribution limit increases, as well as an increase in the age at which distributions from IRAs must begin.

Another bill, H.R. 2884, to provide tax relief to victims of terrorist attacks on the United States, was signed by the President on January 24, 2002.

The Economic Stimulus Package

The terrorist attacks of September 11 increased concerns about an economic slowdown and Congressional leaders considered what tax measures, if any, to take to stimulate the economy. Among the provisions initially discussed were a credit for payroll taxes and a speedup of already enacted future rates cuts (P.L. 107-16). Business tax cuts and proposals for tax rebates were also debated.

On October 24 the House passed H.R. 3090, a tax cut costing $99 billion in 2002 and $159.4 billion over the next 10 years. This bill included temporary expensing for 30% of equipment cost, repeal of the corporate alternative minimum tax (with an immediate refund of accumulated credits), a 15-year write-off period for leasehold improvements, a supplemental rebate for those without enough tax liability to use the prior rebate, an acceleration of the 25% rate cut already enacted, a temporary increase in the individual alternative minimum tax exemption, a reduction in the capital gains rate from 20% and 10% to 18% and 8% for all property held a year, and a number of more minor provisions.

Senate Finance Committee Chairman Baucus proposed a plan which would allow businesses to expense 10% of investment ($15 billion in 2002, $3 billion in 2002-2011), increase the expensing ceiling for small business ($1 billion in 2002, no cost in 2002-2011), extend net operating loss carryback period from 2 years to 5 years ($4 billion in 2002, $1 billion in 2002-2011), extend tax provisions that are set to expire at the end of 2001, and provide refunds to taxpayers who did not receive a full rebate ($14 billion in 2002 only). On November 8, the H.R. 3090 was reported with slight amendments. Senate Republicans prepared an extensive list of amendments, and on November 14, the proposal failed to garner enough vote to overcome their points of order. Negotiations between the Senate, the House and the Administration are failed to produce a compromise. On December 19, the House passed a more limited version of the bill, H.R. 3529.

On January 24, the Senate began considering H.R. 622, a more limited bill that included only the expensing and rebate tax provisions (along with some spending provisions); the tax cost was $56 billion in 2002 and $21 billion from 2002-2011. The Senate continued to consider proposals and passed H.R. 622 with only unemployment benefits. The House added their tax provisions to this bill on February 14. On March 7, the House passed a more limited package of tax provisions along with unemployment benefits (H.R. 3090); the Senate passed the bill on March 8 and the President signed it on March 9.

The Multi-Year Tax Cut

Congressional leaders early expressed interest in tax cuts in the 107th Congress. Congress had passed several tax cuts in the 106th Congress, which were vetoed; some other provisions saw some action that was not completed, in part because of expected vetoes. Congressional leaders also supported the tax plan proposed by President Bush during his campaign, presented to them on February 8, 2001, and included with some amendments, in his address to the Congress of February 27. Several separate bills were been passed by the House; the Senate has passed an omnibus bill; the omnibus Senate bill and final agreement cost $1.35 trillion over 2001-2011. (Please note that revenue estimates from stand-alone bills are not comparable with those from omnibus bills because of interactions among provisions.)

Tax Rate Reductions & Alternative Minimum Tax

On March 1, the House Ways and Means Committee marked up H.R. 3, Chairman Thomas's $958 billion, 10-year bill that implements the rate reductions that form a part of President Bush's tax cut; this legislation was passed by the House on March 8. These reductions would gradually reduce tax rates from 15% to 10% on a new bracket of $12,00 for married couples and $6,000 for singles. This phase in would apply in 2001, when the rate would be reduced to 12% and cost $383 billion over 10 years. It would gradually reduce the 28% and 31% rates to 25% and the 36% and 39.6% rates to 33%, beginning in 2002 ($560 billion over 10 years). A more minor provision would also allow refundable tax credits to be taken against the Alternative Minimum Tax (AMT), at $15 billion over 10 years. Two amendments to the plan were adopted on March 1, one setting a time frame for changing withholding tables and the other keeping the transfers to the Social Security Trust Fund reflecting income tax payments on social security benefits from falling due to the tax cut.

The Chairman indicated that he planned to address AMT concerns, marriage penalty relief, the child credit, and estate tax repeal in subsequent tax legislation, but plans to keep the overall tax cut the same size as the Administration's $1.6 trillion figure.

The committee rejected a proposal by Ways and Means Committee Democrats for a $249.5 billion plan to lower the 15% tax rate, provide marriage penalty relief, and expand the earned income tax. This plan was a scaled back version of the plan announced by Democratic leaders Gephardt and Daschle. A $585 billion Democratic alternative which would provide a 12% rate for about $20,000 of taxable income, and other cuts, was rejected on the House floor on March 8. The committee also rejected a proposal for a trigger mechanism that would prevent the Social Security and Medicare surplus from being used for anything other than debt reduction. A number of members of both the House and Senate indicated interest in a trigger.

The Senate Finance Committee plan included a new 10% rate bracket effective 2001 and gradually reduces the tax rates at the top from 28%, 31%, 36% and 39.6% to 25%, 28%, 33%, and 36%, with full phase-in effective in 2007. The proposal would also raise the income level for the itemized deduction phase out and eliminate the personal exemption phase out. These reductions in rates would cost $846 billion. The plan would also make the child credit a permanent offset against the AMT, a cost that is combined with child credit provisions reported below. The plan would temporarily increase the AMT exemptions by $2,000 for singles and $4,000 for joint returns at a cost of $33 billion, but this provision would sunset at the end of 2006. These provisions were adopted as part of H.R. 1836. A Democratic amendment for a smaller bill with only the 10% rate bracket failed on the Senate floor.

The final bill included $874.9 billion of tax cuts largely following the Senate bill, but sets the top tax rate at 35%. Phase in rates differ somewhat.

Marriage Penalty and Child Credit

On March 22, the Ways and Means Committee reported H.R. 6 providing marriage tax penalty relief and child credits at a cost of $399.2 billion. This bill increased the child credit from $500 to $1000 (phased in by 2006), increased the standard deduction for married couples to twice that of singles, effect 2002, and expanded the 15% bracket to make it twice as wide for joint returns as for single returns, a provision phased in by 2008. Modifications were also made in the earned income credit, and minor modifications in the alternative minimum tax related to the credit.

Democrats proposed an alternative to provide a new 12% bracket for the first $20,000 of taxable income, increase the standard deduction, and modify the marriage penalty. This alternative was rejected by the committee. The Democratic alternative was rejected on the House floor on a party-line vote on March 29; then, H.R. 6 was approved with 64 Democrats supporting it.

The Senate Finance Committee proposal includes a doubling of the standard deduction and of the width of the 15% rate bracket for joint returns as part of its omnibus bill. A $3,000 increase in the phase out level of the EIC was also included. The child credit would be increased to $600 in 2001 and gradually doubled (effective 2010); the credit would be refundable against up to 15% of earned income in excess of $10,000. The child credit provisions would cost $190 billion over 10 years; the marriage penalty provisions would cost $60 billion. These provisions were adopted as part of H.R. 1836 with slightly different effective dates, at a cost of $193 billion and $72.2 billion. A floor amendment to H.R. 1836 added provisions to expand the rate and limits of the dependent care credit at a cost of $5.4 billion.

The conference report included these credits and basic marriage penalty provisions at a cost of $171.2 billion and $59.8 billion; dependent care provisions cost $7.6 billion. The child credit was refundable to the extent of 10% of income over $10,000.

The Senate and final bills also included provisions for an employer child care credit, and all of the bills provided for an adoption tax credit; these provisions had a small revenue cost.

Estate and Gift Tax

On March 29, the Ways and Means Committee reported H.R. 8, a bill to gradually lower the tax over 10 years and then fully repeal it. The bill would convert the current credit to an exemption in 2002, repeal the phase-out of the exemption in 2002, and lower the top rates to 53% in 2002 and 50% in 2003. All rates would be lowered by one percentage per year in 2003-2006, lowered by 2 percentage points in 2007-2010, and reduced to zero in 2011. At that time, carryover basis would be substituted for step-up in basis, with an exemption of $1.3 million ($3 million for surviving spouse). The bill would cost $193 billion over 10 years; however, this revenue cost is substantially reduced by the phase in. Immediate repeal would cost up to $662 billion, an amount in excess of the projected estate tax yield of $409 billion because of projected behavioral responses that would lower income tax revenues (e.g. more life time transfers to donees in lower tax brackets, more purchase of life insurance with deferral aspects, lower compliance).

A substitute measure by Democrats, which was defeated, would have increased the exemption to $2 million in 2002 and gradually raised it to $2.5, along with repealing the state death tax credit. The bill was passed in the House on April 4, with 54 Democrats supporting it.

The Bush Administration's tax proposal also included a gradual repeal of the tax, and legislation similar to H.R. 8, but with a quicker phase-in, was passed in the 106th Congress (but vetoed by President Clinton).

The Senate Finance Committee proposal would phase out estate and gift tax provisions costing $144 billion over 10 years as part of its omnibus bill. Most of the repeal would take place outside the budget window, when carryover basis provisions similar to the House provision would be allowed. Offsetting revenue is gained in the early years from repeal of the State tax credit which is reduced by 50% in 2002, and repealed in 2004. (Rates over 50% and the bubble would be repealed in 2002; rates above 49%, 48%, 47%, 46% and 45% would be repealed respectively in 2003, 2004, 2005, 2006, and 2007-2010. The unified credit would be increased to $1 million in 2002 and 2003, $2 million in 2004, $3 million in 2005 -2008, $3.5 million in 2009, and $4 million in 2010. A gift tax with at a 40% rate and a $1 million exemption would be retained. These provisions were generally adopted as part of H.R. 1836 in the Senate, at a cost of

$134 billion. A Democratic amendment that would have reformed rather than repealed the tax failed.

The final bill included provisions similar to the Senate bill costing $138 billion.

IRAs and Pensions

On April 25, the Ways and Means reported H.R. 10, a bill which, along with certain pension revisions, expanded IRA contribution limits. H.R. 10 would increase the limits for IRA contributions from $2000 to $3,000 in 2002, $4,000 in 2003 and $5,000 in 2004, with inflation indexing thereafter. The revenue cost for these IRA provisions would rise over time, beginning at $0.6 billion in FY2002 and $1.5 billion in FY2003, but rising to $5.8 billion by 2011. The cost would be $10 billion over 5 years and $34 billion over 10 years. The committee rejected along party lines a proposal to provide a refundable tax credit for workers with adjusted gross incomes of less than $25,000. H.R. 10 was passed by the House.

The Senate Finance Committee included similar provisions costing $40 billion over 10 years as part of its omnibus bill. The proposal phases in the expansion of IRA limits more slowly and includes a temporary credit for elective deferrals and IRAs that sunsets in 2006. These provisions were adopted as part of H.R. 1836 in the Senate and included in the final bill, at a cost of $50 billion.

Education Tax Subsidies

On March 13, the Senate Finance Committee approved $20.7 billion in education tax benefits in separate legislation. The Senate Finance Committee plan included in their omnibus bill education provisions costing $33 billion that expand existing education savings accounts for higher education in a variety of ways, allow tax-free distributions from prepaid tuition programs, expand the use of tax exempt bonds, and eliminate restrictions on student loan interest deductions. A provision that allows an above the line deduction for higher education expenses accounts for $11 billion of the cost but sunsets at the end of 2005 as part of their omnibus bill. Minor amendments were made in the committee including a tax credit for student loan interest payments. These provisions were adopted as part of H.R. 1836 in the Senate. With some minor reductions these provisions were included in the final bill at a cost of $29.4 billion.