GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER

Natwar M. Gandhi
Chief Financial Officer

July 27, 2012

The Honorable Vincent C. Gray
Mayor
Government of the District of Columbia
1350 Pennsylvania Avenue, NW, 6th Floor
Washington, DC 20004

The Honorable Phil Mendelson
Chairman
Council of the District of Columbia
The John A. Wilson Building
1350 Pennsylvania Avenue, NW, Suite 402
Washington, DC 20004

Dear Mayor Gray and Chairman Mendelson:

I write to provide you with a copy of the "District of Columbia Tax Expenditure Report," which was recently completed by the Office of Revenue Analysis. This report fulfills the requirement of D.C. Law 13-161, the "Tax Expenditure Budget Review Act of 2000," which directs the Chief Financial Officer to report every two years on the revenue loss to the District government resulting from tax exclusions, exemptions, credits, deferrals, and abatements.

This version of the tax expenditure budget reviews more than 200 provisions of the tax code and includes more information on similar provisions in Maryland and Virginia than previous reports. For each tax expenditure, the report provides the statutory basis and year of enactment, and also discusses the structure of the provision, its purpose, and its impacts. In addition, the report presents the distribution of benefits, by income level, for many of the income tax expenditures. The table of contents on p. 3 includes hyperlinks that allow readers to find parts of the report that may be of particular interest.

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I hope that the tax expenditure budget will be a valuable resource to you and your staff. If there are any questions about the report, please ask your staff to call Jason Juffras of the Office of Revenue Analysis at (202) 727-6689.

Sincerely,

Natwar M. Gandhi

Attachment

cc: All members of the Council of the District of Columbia
Allen Lew, City Administrator
Victor Hoskins, Deputy Mayor for Economic Development
Charles Willoughby, Inspector General
Yolanda Branche, District of Columbia Auditor

Government of the
District of Columbia

Vincent C. Gray
Mayor

Natwar M. Gandhi
Chief Financial Officer

District of Columbia
Tax Expenditure Report

Produced by the
Office of Revenue Analysis

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District of Columbia Tax Expenditure Report

Acknowledgements

This report is a product of the District of Columbia Office of Revenue Analysis (ORA). Jason Juffras, an ORA fiscal analyst, researched all of the tax expenditures, drafted the report, and estimated the federal conformity tax expenditures. In addition, the following ORA staff members estimated the forgone revenues from local tax expenditures: Norton Francis, the Director of Revenue Estimation; Betty Alleyne, financial economist; Lindsay Clark, fiscal analyst; Kelly Dinkins, data administrator; Daniel Muhammad, financial economist; Jeffrey Oakman, fiscal analyst; and Sharain Ward, financial economist.

Individuals from other units of the Office of the Chief Financial Officer also contributed their knowledge and expertise to the report, particularly Deborah Freis, senior policy analyst in the Office of Economic Development Finance, and Lester Morter, exemption specialist in the Real Property Tax Administration. I also thank the individuals from other D.C. government agencies who provided important information on many local tax expenditure provisions.

Natwar M. Gandhi
Chief Financial Officer

District of Columbia Tax Expenditure Report

Introduction

D.C. Law 13-161, the "Tax Expenditure Budget Review Act of 2000,"[1] requires the Chief Financial Officer to prepare a biennial tax expenditure budget that estimates the revenue loss to the District government resulting from tax expenditures during the current fiscal year and the next two fiscal years. The law defines "tax expenditures" as "the revenue losses attributable to provisions of federal law and the laws of the District of Columbia that allow, in whole or in part, a special exclusion, exemption, or deduction from taxes … or which provide a special credit, a preferential rate of tax, or a deferral of tax liability."[2]

The Chief Financial Officer prepared the first required tax expenditure budget as part of the proposed fiscal year 2003 budget. This report, which estimates the revenue forgone due to tax expenditures in fiscal years 2012 through 2015,[3] covers more than 200 separate tax expenditure provisions. This tax expenditure budget expands on the analysis done in prior versions by including comparisons of local tax expenditures to similar provisions in Maryland and Virginia, as well as nationwide data when available.

Understanding Tax Expenditures

Tax expenditures are often described as "spending by another name," or "disguised spending." Policymakers use tax abatements, credits, deductions, deferrals, and exclusions to promote a wide range of policy goals in education, human services, public safety, economic development, environmental protection, and other areas. Instead of pursuing these objectives through direct spending, policymakers reduce the tax liability associated with certain actions (such as hiring new employees) or conditions (such as being blind or elderly) so that individuals or businesses can keep and spend the money, often for particular purposes. For example, a program to expand access to higher education could offer tax deductions for college savings instead of increasing student loans or grants. Regardless of which approach the government uses, there is a real resource cost in terms of forgone revenue or direct expenditures.

Tax expenditures are frequently used as a policy tool in the District of Columbia. There are two types of tax expenditures: (1) federal conformity tax expenditures, which apply U.S. Internal Revenue Code provisions to the D.C. personal and corporate income taxes, and (2) tax expenditures authorized only in local law. By conforming to the federal definition of adjusted

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[1] D.C. Law 13-161 took effect on October 4, 2000, and is codified in § 47-318 and § 47-318.01 of the D.C. Official Code.

[2] See D.C. Official Code § 47-318(6).

[3] Although the law requires that the tax expenditure budget provide estimates of the revenue loss for the current fiscal year and the subsequent two fiscal years, this report covers the current year and the subsequent *three* fiscal years to be consistent with the District's four-year financial plan and budget. The four-year time frame for the District's financial plan and budget is mandated by Public Law 104-8, the "District of Columbia Financial Responsibility and Management Assistance Act of 1995," and is codified at D.C. Official Code § 47-392.01(b).

gross income (with several exceptions), the District adopts most of the exclusions and deductions from income that are part of the federal personal and corporate income tax systems. Most other states with an income tax use federal adjusted gross income as the basis for their income tax.

An example of a federal conformity tax expenditure is the home mortgage interest deduction: the District's personal income tax follows the federal practice of allowing taxpayers to deduct home mortgage interest payments. In addition to the 111 federal conformity provisions covered in this report,[4] there are 118 tax expenditures established by local law. An example of a local tax expenditure is the homestead deduction, which allows all D.C. taxpayers who live in their own home a deduction ($67,500 at the time of this writing) from the taxable value of the home. Both federal conformity and local tax expenditures warrant regular scrutiny to make sure they are effective, efficient, and equitable, and to highlight the tradeoffs between tax expenditures and other programs.

Since the previous tax expenditure budget was published in 2010, policymakers have established four new local tax expenditures. These are (1) the job growth tax credit for corporations and unincorporated businesses, (2) real property tax abatements for non-profit organizations located in designated neighborhoods, (3) real property tax abatements for high-technology commercial real estate database and service providers, and (4) a transfer tax exemption for bona-fide gifts of real property to the District of Columbia.

Tax expenditures differ from direct expenditures in several respects. Direct spending programs in the District receive an annual appropriation and the proposed funding levels are reviewed during the annual budget cycle. By contrast, tax expenditures remain in place unless policymakers act to modify or repeal them; in this respect, they are similar to entitlement programs. Direct spending programs are itemized on the expenditure side of the budget, whereas revenues are shown in the budget as aggregate figures without an itemization of tax expenditures.

The tax expenditure budget seeks to provide policymakers with a more complete picture of how the government uses its resources, so they can consider how to reallocate resources more effectively. For example, if ineffective or outmoded tax expenditures were eliminated, policymakers could free up resources to expand high-priority direct spending programs or cut overall tax rates. This report is designed to provide policymakers with the information they need about tax expenditures to make sound fiscal policy decisions.

Structure of the Report

This tax expenditure budget and accompanying report, prepared by the staff of the Office of Revenue Analysis (ORA), provides extensive background information on each tax expenditure, in addition to estimates of the revenue forgone for fiscal years 2012 through 2015. The report provides (1) the statutory basis and year of enactment for each provision, (2) a description of the tax expenditure and how it is structured, (3) the purpose of the tax expenditure, and (4) a discussion of impacts.

[4] A small number of federal conformity tax expenditures are not included in this report because they concern tax benefits for industries, such as agriculture and mining, that are non-existent or almost non-existent in the District of Columbia.

The report begins with a summary table that provides an overview of the District's tax expenditures. The summary table classifies the tax expenditure according to the type of tax and provides the statutory authority, year of enactment, policy area, and estimated revenue loss for fiscal years 2012 through 2015.

The body of the report is organized into separate parts for federal conformity and local tax expenditures, respectively. The local tax expenditure section includes sub-sections for each of the District's major taxes: personal and business income taxes, real property tax, deed recordation and transfer tax, sales tax, insurance premiums tax, and personal property tax. Each tax expenditure is described in detail, including benefit levels (the amount of abatements, credits, deductions, deferrals, exclusions, and exemptions) and eligibility criteria.

The different types of tax expenditures are as follows:

- <u>exclusions</u>, which are items that are not considered part of a taxpayer's gross income for tax purposes, even though they increase his or her resources or wealth. Exclusions do not appear on the tax form but still cause adjusted gross income to be lower than it otherwise would be. Employer contributions to health and retirement plans are examples.

- <u>exemptions</u>, which are per-person reductions in taxable income that taxpayers can claim because of their status or circumstances (such as being a senior citizen).

- <u>adjustments</u>, which are reductions in taxable income that are available to all tax filers who meet certain criteria, regardless of whether or not they itemize their deductions. Adjustments are also known as "above-the-line" deductions and are shown on the tax form.

- <u>deductions</u>, which are reductions to taxable income that must be itemized on the tax form. This option is not available to those who choose the standard deduction.

- <u>subtractions</u>, which are reductions from federal adjusted gross income that are used to derive District of Columbia adjusted gross income. Subtractions reflect income that is taxed by the federal government but not by the D.C. government.

- <u>credits</u>, which reduce tax liability directly instead of reducing the amount of income subject to taxation. Credits can be refundable (if the amount of the credit exceeds tax liability, the taxpayer gets the difference as a direct refund) or non-refundable (the amount of the credit cannot exceed tax liability).

- <u>abatements</u>, which are reductions in tax liability (typically real property tax liability) that are often applied on a percentage basis or through a negotiated process.

- <u>deferrals</u>, which delay the recognition of income to a future year or years. Because they shift the timing of tax payments, deferrals function like interest-free loans to the taxpayer.

- <u>rebates</u>, which are refunds provided to qualifying taxpayers as a separate payment (as contrasted with tax credits that are first applied as a reduction of tax liability).

- <u>special rules</u>, which is a category used for federal tax expenditures that involve blended tax rates or special accounting procedures and do not fit neatly into any other category.

Policy and Program Areas

Each tax expenditure was classified by one of 17 policy or program areas, such as education, health, social policy, and transportation. The policy areas, shown in the summary tables, largely mirror the categories used by the Joint Committee on Taxation (JCT) of the U.S. Congress in order to facilitate comparisons. Nevertheless, the categories were modified and expanded in several cases to make them more relevant to the District of Columbia. For example, the "business and commerce" category used by the JCT was changed to "economic development" to reflect a policy focus of particular importance in the District, and a "public safety" category was added (there are no public safety tax expenditures at the federal level).

The four policy areas with the largest number of federal conformity provisions are economic development (27 tax expenditures), income security (15), education (12), and health (11). Many federal tax expenditures that are classified under economic development concern the definition or timing of different types of business income, expenses, reserves, and depreciation.

The four policy areas with the largest number of local tax expenditures are housing (26 tax expenditures), economic development (24), and social policy (14), and income security (12).

Important Caveats

A particular caution about the interpretation of the revenue loss estimates in this report deserves emphasis. The forgone revenue estimate is intended to measure what is being "spent" through the tax system, or alternatively, the amount of relief or subsidy provided through that provision. Nevertheless, the forgone revenue is *not* identical to the amount of revenue that could be gained by repealing the tax expenditure. There are three main reasons why:

- First, the estimates of revenue loss are "static" and therefore do not reflect behavioral changes that might occur if a tax expenditure were repealed. For example, if the District eliminated the local supplement to the federal earned income tax credit, people might reduce their hours of work and their income tax payments could also drop.

- Second, the revenue loss for each tax expenditure is estimated independently, which does not account for the interaction effects among different tax provisions. For example, D.C. law establishes that taxpayers may not claim both the local supplement to the earned income tax credit and the D.C. low-income credit. If the local earned income credit were abolished, more taxpayers might then claim the low-income credit.

- Third, the D.C. government may not be able to collect the full amount owed due to administrative reasons. For example, if the District disallowed for local income tax purposes an exemption or exclusion that is allowed on the federal income tax (a process known as "decoupling"), the District would probably not recoup all of the forgone revenue. That is because taxpayers would have to make a separate calculation on their District income taxes to add back the dollars that had been excluded, and compliance with this requirement would not be universal (nor would audits detect all violations).

Because of the factors described above, the total forgone revenue from tax expenditures is *not* equivalent to the sum of the individual estimates of forgone revenue. As the U.S. Government Accountability Office has stated:

> While sufficiently reliable as a gauge of general magnitude, the sum of the individual revenue loss estimates has important limitations in that any interactions between tax expenditures will not be reflected in the sum … Thus, the revenue loss from all or several tax expenditures together might be greater or less than the sum of the estimated revenue losses from the individual tax expenditures, and no measure of the size or the magnitude of these potential interactions or behavioral responses to all or several tax expenditures is available.[5]

Methodology

Summary statistics from D.C. tax returns were an important source of data for the tax expenditure budget and were particularly useful for estimating the forgone revenue from local income tax provisions. Unfortunately, in many instances tax expenditures cannot be estimated from available tax data because they involve income, property, or economic activity that is not taxed, and the relevant information is never reported to the Office of Tax and Revenue (OTR). Therefore, ORA often used data from federal agencies (such as the Census Bureau and the Bureau of Economic Analysis) and D.C. government agencies to estimate the number of beneficiaries and the revenue lost from certain tax expenditures.

OTR generally lacks information on federal conformity tax expenditures because the amounts excluded and deducted are simply transferred to the local tax forms instead of being reported directly. Therefore, ORA's federal conformity estimates represent a District of Columbia portion of the nationwide tax expenditure estimates prepared by the JCT.[6] ORA estimated the D.C. portion using two fractions: (1) a ratio representing the D.C. share of the relevant activity or population, such as D.C. taxable income divided by national taxable income, and (2) a ratio representing the D.C. average tax rate divided by the U.S. average tax rate.

Because of the methodological challenges and data issues, it is important to view the revenue estimates as indicating orders of magnitude rather than providing precise point estimates.

In addition, U.S. Internal Revenue Service rules provide that, "No statistical tabulation may be released outside the agency with cells containing data from fewer than three returns," in order to protect the confidentiality of individual tax records.[7] Tax expenditures with fewer than three

[5] U.S. Government Accountability Office, Government Performance and Accountability: Tax Expenditures Represent a Substantial Federal Commitment and Need to Be Reexamined (GAO-05-960, September 2005), p. 3.

[6] In some cases, ORA used tax expenditure estimates from the U.S. Department of the Treasury when data from the Joint Committee on Taxation were not available.

[7] U.S. Internal Revenue Service, Publication 1075, "Tax Information Security Guidelines for Federal, State, and Local Agencies and Entities" (August 2010), p. 66. Even if the taxpayers are not specifically identified, it might be possible for someone to figure out the confidential information from an estimate of revenue involving so few people or businesses.

claimants are therefore listed in this report as "no estimate," except in the case of real property tax expenditures where different rules apply.[8]

Key Terms for Summary Tables

- too small: refers to a federal conformity tax expenditure with forgone revenue that was less than $50 million annually, according to the JCT. The revenue loss to the District from conforming to the federal policy would be very close to zero.

- sunset: means that there will be no revenue loss because the provision has expired.

- minimal: refers to a local tax expenditure for which precise data are lacking, but the forgone revenue is estimated to be less than $50,000 per year.

- no estimate: refers to a local tax expenditure for which precise data are lacking, but for which the revenue loss might not be minimal. In addition, "no estimate" refers to cases in which calculations cannot be made because of confidentiality rules.

Comments Welcomed

The Office of Revenue Analysis hopes that this report will contribute to a more informed discussion of budget and tax policy in the District of Columbia by providing clear and concise information both for policymakers and for the general public. ORA welcomes comments on the report and will use the feedback to improve future versions.

[8] Specifically, D.C. Official Code § 47-1001 provides that, "The Mayor shall publish, by class and by individual property, a listing of all real property exempt from the real property tax in the District. Such listing shall include the address, lot and square number, the name of the owner, the assessed value of the land and improvements of such property, and the amount of the tax exemption in the previous fiscal year." IRS rules do not affect real property taxation because the federal government does not impose a real property tax.

Summary Data on District of Columbia Tax Expenditures

I. Federal Conformity Tax Expenditures
(Individual and Corporate Income Taxes)

#	Name of Tax Expenditure	Program Area	Year Enacted	Internal Revenue Code Section	FY 2012	FY 2013	FY 2014	FY 2015
					Revenue Forgone ($ in thousands)			
	Federal Exclusions							
1	Capital gains on assets transferred at death	Economic development	1921	1001, 1002, 1014, 1015, 1023, 1040, 1221, and 1222	$39,936	$46,694	$53,555	$62,660
2	Cash accounting, other than agriculture	Economic development	1916	446 and 448	$1,028	$1,028	$1,121	$1,172
3	Credit union income	Economic development	1937	501(c)(14) and 12 USC 1768	$324	$324	$454	$544
4	Distribution from redemption of stock to pay taxes imposed at death	Economic development	1950	303	$280	$374	$374	$436
5	Gain on like-kind exchanges	Economic development	1921	1031	$2,525	$2,924	$3,221	$3,666
6	Imputed interest	Economic development	1964	163(e), 483, 1274, and 1274A	$402	$482	$482	$530
7	Interest on small-issue qualified private-activity bonds	Economic development	1968	103, 141, 144, and 146	$286	$286	$286	$286
8	Magazine, paperback, and record returns	Economic development	1978	458	too small	too small	too small	too small
9	Discharge of certain student loan debt	Education	1984	108(f), 20 USC 1087ee(a)(5) and 42 USC 2541-1(g)(3)	$127	$127	$127	$127
10	Earnings of Coverdell education savings accounts	Education	1998	530	$127	$127	$253	$380
11	Earnings of qualified tuition programs	Education	1997	529	$760	$887	$1,014	$1,186
12	Employer-provided education assistance	Education	1978	127	$769	$769	sunset	sunset
13	Employer-provided tuition reduction	Education	1984	117(d)	$171	$171	$171	$171
14	Interest on education savings bonds	Education	1988	135	$25	$25	$25	$25
15	Interest on state and local private-activity bonds issued to finance education facilities	Education	1986	103, 141, 142(k), 145, 146, and 501(c)(3)	$3,130	$3,416	$3,527	$3,750
16	Interest on state and local private-activity student loan bonds	Education	1965	103, 141, 144(b), and 146	$508	$573	$573	$637
17	Scholarship and fellowship income	Education	1954	117	$3,041	$3,168	$3,421	$3,635
18	Cafeteria plan benefits	Employment	1974	125	$27,597	$30,844	$33,322	$36,787
19	Employee awards	Employment	1986	74(c) and 274(j)	$374	$374	$374	$374
20	Employee stock ownership plans	Employment	1974	401(a)(28), 404(a)(9), 404(k), 415(c)(6), 1042, 4975(e)(7), 4978, and 4979A	$1,138	$1,209	$1,215	$1,287
21	Employer-paid meals and lodging (other than military)	Employment	1918	119 and 132(e)(2)	$940	$1,025	$1,025	$1,071
22	Housing allowance for ministers	Employment	1921	107 and 265	$598	$598	$598	$598
23	Miscellaneous fringe benefits	Employment	1984	117(d) and 132	$6,835	$7,006	$7,262	$7,488
24	Spread of acquisition of stock under incentive stock option plans and employee stock purchase plans	Employment	1981	422 and 423	-$498	-$533	-$533	-$546
25	Voluntary employees' beneficiary association income	Employment	1928	419, 419A, 501(a), 501(c)(9), and 4976	$3,588	$3,759	$3,930	$4,119
26	Interest on state and local private-activity bonds issued to support energy facilities	Energy	1980	103, 141, 142(f), and 146	$28	$28	$28	$39
27	Accrued interest on savings bonds	General fiscal assistance	1951	454(c)	$1,124	$1,205	$1,205	$1,248
28	Allocation of interest expenses attributable to tax-exempt bond interest by financial institutions	General fiscal assistance	2009	141, 265(a), 265(b), and 291(e)	$194	$194	$194	$194
29	Interest on public-purpose state and local bonds	General fiscal assistance	1913	103, 141, and 146	$26,816	$28,260	$28,351	$28,726
30	Employer contributions for medical insurance premiums and medical care	Health	1918	105, 106, and 125	$109,363	$125,939	$137,558	$155,303
31	Interest on state and local private-activity bonds issued to support non-profit hospital construction	Health	1913	103, 141, 145(b), 145(c), 146, and 501(c)(3)	$2,161	$2,336	$2,447	$2,609
32	Medical care and TriCare medical insurance for military dependents, retirees, retiree dependents, and veterans	Health	1986	112 and 134	$2,376	$2,587	$2,746	$2,960
33	Medicare Part A -- hospital insurance benefits	Health	1970	N.A./administrative	$19,644	$20,684	$21,833	$23,056

#	Name of Tax Expenditure	Program Area	Year Enacted	Internal Revenue Code Section	FY 2012	FY 2013	FY 2014	FY 2015
					Revenue Forgone ($ in thousands)			
	Federal Exclusions (cont.)							
34	Medicare Part B -- supplementary medical benefits	Health	1970	N.A./administrative	$13,352	$14,884	$15,869	$17,360
35	Medicare Part D -- prescription drug benefits	Health	2003	N.A./administrative	$3,666	$4,213	$4,761	$5,470
36	Subsidy payments to employers maintaining prescription drug benefits for retirees eligible for Medicare	Health	2003	42 USC 1395w-132	$324	$194	sunset	sunset
37	Capital gain on sale of principal residence	Housing	1997	121	$17,920	$18,637	$19,456	$20,293
38	Income from discharge of principal residence acquisition indebtedness	Housing	1954	108	$467	too small	sunset	sunset
39	Interest on state and local private-activity bonds issued to finance housing	Housing	1980	103, 141, 142, 143, and 146	$2,050	$2,226	$2,336	$2,499
40	Compensatory damages for physical injury or sickness	Income security	1918	104(a)(2) - 104(a)(5)	$1,495	$1,495	$1,495	$1,495
41	Disaster mitigation payments	Income security	2005	139	too small	too small	too small	too small
42	Employer contributions for premiums on accident and disability insurance	Income security	1954	105 and 106	$3,076	$3,161	$3,247	$3,338
43	Employer contributions for premiums on group-term life insurance	Income security	1920	79	$1,452	$1,538	$1,623	$1,719
44	Employer pension contributions and earnings plans	Income security	1921	401-407, 410-418E, and 457	$90,652	$106,715	$105,006	$113,301
45	Income of trusts to finance supplemental unemployment benefits	Income security	1960	501(17)(A)	$34	$43	$51	$60
46	Investment income on life insurance and annuity contracts	Income security	1913	72, 101, 7702, and 7702A	$28,616	$29,333	$30,115	$30,914
47	Public assistance cash benefits	Income security	1933	N.A./administrative	$4,604	$5,127	$5,232	$5,588
48	Roth IRA earnings and distributions	Income security	1997	219 and 408	$4,285	$4,821	$5,625	$6,502
49	Social Security and Railroad Retirement benefits	Income security	1938	86	$14,400	$14,960	$15,880	$16,690
50	Survivor annuities paid to families of public safety officers	Income security	1997	101(h)	too small	too small	too small	too small
51	Workers' compensation benefits	Income security	1918	104(a)(1)	$3,332	$3,503	$3,759	$4,000
52	Active income of controlled foreign corporations	International commerce	1909	11, 882, and 951-964	$9,137	$9,655	$10,238	$10,853
53	Allowances for federal employees working abroad	International commerce	1943	912	$7,661	$8,086	$8,512	$8,989
54	Income earned abroad by U.S. citizens	International commerce	1926	911	$6,167	$6,354	$6,634	$6,886
55	Inventory property sales source rule exception	International commerce	1921	861, 862, 863, and 865	$4,925	$5,054	$5,054	$5,121
56	Benefits, allowances, and certain pay for armed forces personnel	National defense	1925	112 and 134	$3,058	$3,182	$3,557	$3,848
57	Military disability benefits	National defense	1942	104(a)(4), 104(a)(5) and 104(b)	$106	$106	$106	$106
58	Contributions in aid of construction for water and sewer utilities	Natural resources and environment	1996	118(c) and 118(d)	too small	too small	too small	too small
59	Earnings of certain environmental settlement funds	Natural resources and environment	2005	468B	too small	too small	too small	too small
60	Energy conservation subsidies provided by public utilities	Natural resources and environment	1992	136	$202	$202	$193	$193
61	Interest on state and local private-activity bonds issued to finance water, sewer, and hazardous-waste facilities	Natural resources and environment	1968	103, 141, 142, and 146	$537	$619	$680	$725
62	Employer-provided dependent care	Social policy	1981	129	$1,239	$1,341	$1,444	$1,538
63	Foster care payments	Social policy	1982	131	$568	$568	$568	$568
64	Employer-provided parking assistance	Transportation	1984	132(f)	$3,759	$3,930	$4,101	$4,286
65	Employer-provided transit assistance	Transportation	1992	132(f)	$684	$769	$769	$817
66	Interest on state and local private-activity bonds issued to finance airport, dock and mass commuting facilities	Transportation	1968	103, 141, 142, and 146	$794	$969	$969	$1,082
67	Interest on state and local private-activity bonds issued to finance highway projects and rail-truck transfer facilities	Transportation	2005	103, 141, 142(m), and 146	$238	$227	$216	$198
68	G.I. Bill education benefits	Veterans' benefits	1917	38 USC 5301	$686	$686	$739	$767
69	Veterans' benefits and services	Veterans' benefits	1917	38 USC 5301	$2,904	$3,010	$3,062	$3,145

#	Name of Tax Expenditure	Program Area	Year Enacted	Internal Revenue Code Section	Revenue Forgone ($ in thousands) FY 2012	FY 2013	FY 2014	FY 2015

Federal Adjustments

#	Name of Tax Expenditure	Program Area	Year Enacted	Internal Revenue Code Section	FY 2012	FY 2013	FY 2014	FY 2015
70	Classroom expenses of elementary and secondary school educators	Education	2002	62	$187	sunset	sunset	sunset
71	Higher education expenses	Education	2001	222	$634	sunset	sunset	sunset
72	Interest on student loans	Education	1997	221	$507	$634	$634	$713
73	Contributions to health savings accounts	Health	2003	223	$1,367	$1,794	$1,794	$2,074
74	Health insurance premiums and long-term care premiums paid by the self-employed	Health	1986	162(l)	$3,925	$4,343	$4,710	$5,181
75	Contributions to self-employment retirement plans	Income security	1962	401-407, 410-418E, and 457	$12,131	$12,631	$12,988	$13,442
76	Employee contributions to traditional Individual Retirement Accounts	Income security	1974	219 and 408	$6,125	$8,538	$10,022	$13,210
77	Overnight travel expenses of National Guard and Reserve members	National defense	2003	62(a)(2)(E) and 162	$62	$62	$62	$62

Federal Deductions

#	Name of Tax Expenditure	Program Area	Year Enacted	Internal Revenue Code Section	FY 2012	FY 2013	FY 2014	FY 2015
78	Accelerated depreciation of buildings other than rental housing	Economic development	1954	167 and 168	$317	$317	$317	$317
79	Accelerated depreciation of equipment	Economic development	1954	167 and 168	$4,814	$9,868	$15,583	$19,908
80	Small life insurance company taxable income	Economic development	1984	806	$65	$65	$65	$65
81	Amortization of business start-up costs	Economic development	1980	195	$1,028	$934	$841	$758
82	Completed contract rules	Economic development	1986	460	$454	$454	$518	$555
83	Exception from passive loss rules for $25,000 of rental real estate loss	Economic development	1986	469(i)	$12,250	$13,857	$15,633	$17,641
84	Expensing of depreciable small business property	Economic development	1958	179	$2,449	$1,972	-$1,252	-$259
85	Expensing of magazine circulation expenditures	Economic development	1950	173	too small	too small	too small	too small
86	Film and television production costs	Economic development	2004	181	$22	$6	sunset	sunset
87	Gain on non-dealer installment sales	Economic development	1986	453 and 453A(b)	$3,758	$4,950	$4,804	$5,556
88	Life insurance company reserves	Economic development	1984	803(a)(2), 805(a)(2), and 807	$1,555	$1,685	$1,750	$1,859
89	Loss from sale of small business corporation stock	Economic development	1958	1244	$56	$56	$56	$56
90	Property and casualty insurance company reserves	Economic development	1986	832(b)	$259	$259	$259	$259
91	Research and development expenditures	Economic development	1954	174	$2,954	$3,851	$4,564	$5,834
92	Amortization of certified pollution control facilities	Energy	2005	169(d)(5)	$130	$130	$65	$49
93	Depreciation recovery periods for specific energy property	Energy	1986	168(e)	$130	$130	$65	$49
94	Energy-efficient commercial property	Energy	2005	179D	$158	$158	$158	$158
95	Blue Cross and Blue Shield companies	Health	1986	833	$259	$259	$324	$365
96	Medical and dental care expenses	Health	1942	213	$24,420	$26,544	$29,729	$32,970
97	Accelerated depreciation of rental housing	Housing	1954	167 and 168	$4,248	$3,903	$3,997	$3,829
98	Mortgage interest on owner-occupied residences	Housing	1913	163(h)	$87,024	$91,093	$98,769	$105,386
99	State and local property taxes on owner-occupied residences	Housing	1913	164	$14,586	$15,191	$16,017	$16,801
100	Casualty and theft losses	Income security	1913	165(c)(3), 165(e), and 165(h) - 165(k)	$331	$331	$331	$331
101	Deduction of foreign taxes instead of a credit	International commerce	1913	901	$194	$194	$194	$194
102	Financing income of certain controlled foreign corporations	International commerce	1962	953 and 954	$2,592	sunset	sunset	sunset
103	Charitable contributions	Social policy	1917/1935	170 and 642(c)	$54,536	$57,133	$59,510	$62,211
104	Costs of removing architectural and transportation barriers to the disabled and elderly	Social policy	1976	190	$93	$93	$93	$93

Federal Special Rules

#	Name of Tax Expenditure	Program Area	Year Enacted	Internal Revenue Code Section	FY 2012	FY 2013	FY 2014	FY 2015
105	60-40 rule for gain or loss from section 1256 contracts	Economic development	1981	1256	$748	$748	$841	$894
106	Interest rate and discounting period assumptions for reserves of property and casualty insurance companies	Economic development	1986	831, 832(b), and 846	$454	$518	$454	$454
107	Inventory accounting	Economic development	1938	475, 491-492	$3,505	$3,700	$3,923	$4,157
108	Ordinary gain or loss treatment for Fannie Mae and Freddie Mac preferred stock by certain financial institutions	Economic development	2008	P.L. 110-343, section 301	$65	-$65	-$65	-$65
109	Special alternative tax on small property and casualty insurance companies	Economic development	1954	321(a), 501(c)(15), 832, and 834	$65	$65	$65	$65
110	Apportionment of research and development expenses for determining foreign tax credits	International commerce	1977	861-863 and 904	$259	$259	$259	$259
111	Interest-charge domestic international sales corporations	International commerce	1986	991-997	$65	$65	$65	$65

II. Local Tax Expenditures

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
					Revenue Forgone ($ in thousands)			

D.C. INCOME TAX
(Individual and Business Income Taxes)

Exemptions

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
112	Additional personal exemption for the blind	Income security	1987	§ 47-1806.02(d)	$96	$103	$106	$109
113	Additional personal exemption for the elderly	Income security	1987	§ 47-1806.02(e)	$4,346	$4,670	$4,800	$4,930

Subtractions from Federal Adjusted Gross Income

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
114	Qualified high-technology companies: capital gains	Economic development	2001	§ 47-1803.2(a)(2)(Q)	$0	$0	$0	$0
115	Qualified high-technology companies: depreciable business assets	Economic development	2001	§ 47.1803.3(a)(18)	no estimate	no estimate	no estimate	no estimate
116	College savings plan contributions	Education	2001	§ 47-4501 - § 47-4512	$881	$881	$881	$881
117	Public school teacher expenses	Education	2007	§ 47-1803.03(b-2)	$92	$92	$92	$92
118	Health insurance premiums paid for a same-sex spouse or domestic partner (business income tax)	Health	2006	§ 47-1803.02(a)(2)(W)	$550	$577	$606	$636
119	Health insurance premiums paid for a same-sex spouse or domestic partner (personal income tax)	Health	1992	§47-1803.03(a)(15)	$56	$55	$56	$59
120	Health professional loan repayments	Health	2006	§ 7-751.01 - § 7-	$58	$58	$58	$58
121	Long-term care insurance premiums	Health	2005	§ 47-1803.03(b-1)	$186	$186	$186	$186
122	Housing relocation assistance	Housing	2002	§ 42-2851.05	$0	$0	$0	$0
123	D.C. and federal government pension income	Income security	1987	§ 47-1803.02(a)(2)(N)	$4,361	$4,305	$4,419	$4,612
124	D.C. and federal government survivor benefits	Income security	1987	§ 47-1803.02(a)(2)(N)	$3,928	$3,877	$3,980	$4,154
125	Disability payments for the permanently and totally disabled	Income security	1985	§ 47-1803.02(a)(2)(M)	$72	$71	$73	$76
126	Income of persons with a permanent and total disability	Income security	2005	§ 47-1803.02(a)(2)(V)	$457	$451	$463	$484
127	Railroad retirement system benefits	Income security	1985	§ 47-1803.02(a)(2)(L)	$82	$81	$83	$87
128	Social Security benefits for retired workers	Income security	1985	§ 47-1803.02(a)(2)(L)	$14,763	$14,574	$14,959	$15,613
129	Social Security benefits for survivors and dependents	Income security	1985	§ 47-1803.02(a)(2)(L)	$2,074	$2,047	$2,101	$2,193
130	Social Security benefits for the disabled	Income security	1985	§ 47-1803.02(a)(2)(L)	$3,614	$3,567	$3,662	$3,822
131	Environmental savings account contributions and earnings	Natural resources and environment	2001	§ 8-637.03	minimal	minimal	minimal	minimal
132	Rental assistance to police officers	Public safety	1993	§ 42-2902	minimal	minimal	minimal	minimal
133	Compensatory damages awarded in a discrimination case	Social policy	2002	§ 47-1803.02(a)(2)(U) and § 47-1806.10	$25	$25	$26	$27
134	Poverty lawyer loan assistance	Social policy	2007	§ 47-1803.02(a)(2)(X)	$33	$33	$33	$33

Credits

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
135	Economic development zone incentives for businesses	Economic development	1988	§ 6-1501, § 6-1502, § 6 1504, and § 47-	$0	$0	$0	$0
136	Qualified high-technology companies: business income tax reduction	Economic development	2001	§ 47-1817.06	$5,144	$5,305	$5,396	$5,646
137	Qualified high-technology companies: employee relocation incentives	Economic development	2001	§ 47-1817.02	$3,470	$3,578	$3,640	$3,809
138	Qualified high-technology companies: employment incentives	Economic development	2001	§ 47-1817.03	included in #137	included in #137	included in #137	included in #137
139	Qualified high-technology companies: incentives to employ disadvantaged workers	Economic development	2001	§ 47-1817.05	included in #137	included in #137	included in #137	included in #137
140	Qualified high-technology companies: incentives to retrain disadvantaged workers	Economic development	2001	§ 47-1817.04	included in #137	included in #137	included in #137	included in #137
141	First-time home purchase for D.C. government employees	Employment	2000	§ 42-2506	$116	$116	$116	$116
142	Job growth tax credit	Employment	2010	§ 47-1807.09	$0	$158	$399	$721
143	Paid leave for organ or bone marrow donors	Health	2006	§ 47-1807.08	no estimate	no estimate	no estimate	no estimate
144	Employer-assisted home purchases	Housing	2002	§ 47-1807.07	minimal	minimal	minimal	minimal
145	Lower-income, long-term homeownership	Housing	2002	§ 47-1806.09 - § 47-1806.09f	$5	$5	$5	$5
146	Property tax circuit-breaker	Housing	1977	§ 47-1806.06	$4,041	$4,041	$4,041	$4,041
147	Earned income tax credit	Income security	2000	§ 47-1806.04(f)	$46,864	$48,364	$47,870	$49,856
148	Low-income credit	Income security	1987	§ 47-1806.04(e)	$1,437	$1,437	$1,437	$1,437
149	Brownfield revitalization and cleanup	Natural resources and environment	2001	§ 8-637.01	$0	$0	$0	$0
150	Child and dependent care	Social policy	1977	§ 47-1806.04(c)	$6,680	$6,680	$6,680	$6,680

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
					Revenue Forgone ($ in thousands)			

REAL PROPERTY TAX

Abatements

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
151	New or improved buildings used by high-technology companies	Economic development	2001	§ 47-811.03	$0	$0	$0	$0
152	Non-profit organizations locating in designated neighborhoods	Economic development	2010	§ 47-857.11 - § 47-857.16	$500 maximum	$500 maximum	$500 maximum	$500 maximum
153	Improvements to low-income housing	Housing	2002	§ 47-866	$0	$0	$0	$0
154	New residential developments	Housing	2002	§ 47-857.01 - § 47-857.10	$3,331	$3,331	$3,157	$1,491
155	NoMA residential developments	Housing	2009	§ 47-859.01 - § 47-859.05	$4,263	$4,689	$4,689	$4,689
156	Preservation of section 8 housing in qualified areas	Housing	2002	§ 47-865	$0	$0	$6	$11
157	Single-room-occupancy housing	Housing	1994	§ 42-3508.06	$0	$0	$0	$0
158	Vacant rental housing	Housing	1985	§ 42-3508.02	$0	$0	$0	$0

Exemptions

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
159	Development of a qualified supermarket, restaurant, or retail store	Economic development	1988	§ 47-1002(23)	$1,980	$2,278	$2,659	$3,049
160	High-technology commercial real estate database and service provider	Economic development	2010	§ 47-4626	$700	$700	$700	$700
161	Educational institutions	Education	1942	§ 47-1002(10)	$102,031	$102,031	$102,337	$102,541
162	Libraries	Education	1942	§ 47-1002(7)	$431	$431	$432	$433
163	Embassies, chanceries, and associated properties of foreign governments	General law	1942	§ 47-1002(3)	$41,125	$41,125	$41,248	$41,330
164	Federal government property	General law	1942	§ 47-1002(1)	$823,442	$823,442	$825,912	$827,559
165	Miscellaneous exemptions	General law	multiple years	multiple code sections	$69,063	$69,063	$69,270	$69,408
166	Hospital buildings	Health	1942	§ 47-1002(9)	$13,137	$13,137	$13,177	$13,203
167	Historic property	Housing	1974	§ 47-842 - § 47-844	$119	$119	$120	$120
168	Homestead exemption	Housing	1978	§ 47-850	$54,673	$61,436	$62,389	$64,471
169	Lower-income homeownership households and cooperative housing associations	Housing	1983	§ 47-3503	$1,079	$1,079	$1,082	$1,084
170	Multi-family and single-family rental and cooperative housing for low- and moderate-income persons	Housing	1978	§ 47-1002(20)	$12,949	$12,949	$12,988	$13,013
171	Nonprofit housing associations	Housing	1983	§ 47-3505	$7,553	$7,553	$7,576	$7,591
172	Resident management corporations	Housing	1992	§ 47-1002(24)	$0	$0	$0	$0
173	Correctional Treatment Facility	Public safety	1997	§ 47-1002(25)	$3,495	$3,495	$3,505	$3,512
174	Art galleries	Social policy	1942	§ 47-1002(6)	$2,102	$2,085	$2,091	$2,095
175	Cemeteries	Social policy	1942	§ 47-1002(12)	$5,548	$5,548	$5,565	$5,576
176	Charitable organizations	Social policy	1942	§ 47-1002(8)	$14,272	$14,272	$14,315	$14,343
177	Churches, synagogues, and mosques	Social policy	1942	§ 47-1002(12)	$59,481	$59,481	$59,660	$59,779
178	Washington Metropolitan Area Transit Authority properties	Transportation	1966	§ 9-1107.01	$9,723	$9,723	$9,752	$9,771

Credits

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
179	First-time homebuyer credit for D.C. government employees	Employment	2000	§ 42-2506	$291	$291	$292	$292
180	Assessment increase cap	Housing	2001	§ 47-864	$28,416	$28,416	$28,501	$28,558
181	Credit for senior citizens and persons with disabilities	Housing	1986	§ 47-863	$14,590	$14,590	$14,634	$14,663
182	Brownfield revitalization and cleanup	Natural resources and environment	2001	§ 8-637.01	$0	$0	$0	$0
183	Condominium and cooperative trash collection	Natural resources and environment	1990	§ 47-872 and § 47-873	$5,177	$5,281	$5,386	$5,494

Deferrals, Rebates, and Multiple Categories

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
184	Economic development zone incentives for real property owners	Economic development	1988	§ 6-1501 - § 6-1503	$0	$0	$0	$0
185	Public charter school tax rebate	Education	2005	§ 47-867	$554	$554	$560	$565
186	Homeowners in enterprise zones	Housing	2002	§ 47-858.01 - § 47-858.05	$0	$0	$0	$0
187	Low-income homeowners	Housing	2005	§ 47-845.02	$2,758	$2,758	$2,766	$2,771
188	Low-income, senior-citizen homeowners	Housing	2005	§ 47-845.03	$827	$827	$830	$831

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
					Revenue Forgone ($ in thousands)			

DEED RECORDATION AND TRANSFER TAX

Exemptions

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
189	Educational institutions	Education	1962 and 1980	§ 42-1102(3) and § 47-902(3)	$1,026	$1,026	$1,029	$1,031
190	Bona-fide gifts to the District of Columbia	General law	2011	§ 47-902(24)	$0	$0	$0	$0
191	Embassies, chanceries, and associated properties of foreign governments	General law	1962 and 1980	§ 42-1102(3) and § 47-902(3)	$417	$417	$418	$419
192	Federal government	General law	1962 and 1980	§ 42-1102(2) and § 47-902(2)	$672	$672	$674	$675
193	Other properties exempt from real property taxation	General law	1962 and 1980	§ 42-1102(2) and § 47-902(2)	$923	$923	$926	$928
194	Special act of Congress (recordation tax)	General law	1962	§ 42-1102(4)	$367	$367	$368	$368
195	Cooperative housing associations	Housing	1983	§ 42-1102(14), § 47-3503(a)(2), § 47-3503(a)(3), § 47-902(11), and §47-3503(b)(2)	$355	$355	$356	$356
196	Inclusionary zoning program (transfer tax)	Housing	2007	§ 47-902(23)	$4	$15	$31	$62
197	Lower-income homeownership households	Housing	1983	§ 42-1102(12), § 47-3503(a)(1), § 47-3503(a)(3), § 47-902(9), and §47-	$142	$142	$143	$143
198	Nonprofit housing associations	Housing	1983	§ 42-1102(13), § 47-3503(c), § 47-902(10), and §47-3505(b)	$213	$213	$213	$214
199	Resident management corporations	Housing	1992	§ 42-1102(20), § 47-3506.01(b)(1), § 47-902(15), and §47-3506.01(b)(2)	$0	$0	$0	$0
200	Charitable entities	Social policy	1962 and 1980	§ 42-1102(3) and § 47-902(3)	$1,539	$1,539	$1,543	$1,546
201	Churches, synagogues, and mosques	Social policy	1962 and 1980	§ 42-1102(3) and § 47-902(3)	$256	$256	$257	$258
202	Tax-exempt entities subject to a long-term lease	Tax administration and equity	2003	§ 42-1102(27) and § 47-902(21)	no estimate	no estimate	no estimate	no estimate

SALES TAX

Exemptions

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
203	Energy products used in manufacturing	Economic development	1949	§ 47-2005(11)	$3,705	$3,551	$3,551	$3,551
204	Internet access service	Economic development	1999	§ 47-2001(n)(2)(F)	$3,326	$3,326	$3,326	$3,326
205	Materials used in development of a qualified supermarket	Economic development	2000	§ 47-2005(28)	$530	$528	$549	$571
206	Professional and personal services	Economic development	1949	§ 47-2001(n)(2)(B)	$250,508	$255,268	$261,394	$283,810
207	Qualified high-technology companies: certain sales	Economic development	2001	§ 47-2001(n)(2)(G)	$631	$644	$657	$670
208	Qualified high-technology companies: technology purchases	Economic development	2001	§ 47-2005(31)	$172	$175	$179	$183
209	Transportation and communication services	Economic development	1949	§ 47-2001(n)(2)(A)	$43,231	$42,341	$43,485	$47,214
210	Federal and D.C. governments	General law	1949	§ 47-2005(1)	$182,625	$184,451	$187,771	$192,278
211	Medicine, drugs, and medical devices	Health	1949	§ 47-2005(14) and (15)	$9,636	$9,636	$9,636	$9,636
212	Groceries	Social policy	1949	§ 47-2001(n)(2)(E)	$56,299	$57,368	$59,491	$64,593
213	Materials used in war memorials	Social policy	1957	§ 47-2005(16)	$0	$0	$0	$0
214	Non-profit (501(c)(4)) organizations	Social policy	1987	§ 47-2005(22)	$31,147	$31,833	$32,692	$35,496
215	Semi-public institutions	Social policy	1949	§ 47-2005(3)	$46,364	$47,384	$48,663	$50,561
216	Miscellaneous	Tax administration and equity	1949	§ 47-2005	no estimate	no estimate	no estimate	no estimate
217	Motor fuels	Tax administration and equity	1981	§ 47-2005(20)	$21,616	$21,832	$22,050	$22,271
218	Public utility companies	Tax administration and equity	1949	§ 47-2005(5)	$89,847	$89,847	$89,847	$89,847
219	State and local governments	Tax administration and equity	1949	§ 47-2005(2)	minimal	minimal	minimal	minimal
220	Valet parking services	Tax administration and equity	2002	§ 47-2001(n)(2)(H)	$390	$383	$393	$413

INSURANCE PREMIUMS TAX

Credit

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
221	Certified capital investment by insurance companies	Economic development	2004	§ 31-5233	$9,200	$9,200	$4,000	$0

PERSONAL PROPERTY TAX

Exemptions

#	Name of Tax Expenditure	Program Area	Year Enacted	D.C. Code Section	FY 2012	FY 2013	FY 2014	FY 2015
222	Digital audio radio satellite companies	Economic development	2000	§ 47-1508(a)(8)	no estimate	no estimate	no estimate	no estimate
223	Qualified high-technology companies	Economic development	2001	§ 47-1508(a)(10)	$183	$182	$182	$182
224	Qualified supermarkets	Economic development	2000	§ 47-1508(a)(9)	$304	$307	$312	$316
225	Non-profit organizations	Social policy	1902	§ 47-1508(a)(1)	$4	$4	$4	$4
226	Motor vehicles and trailers	Transportation	1954	§ 47-1508(a)(3)	$2,244	$2,266	$2,307	$2,330
227	Public utility and toll telecommunications providers	Tax administration and equity	2001	§ 47-1508(a)(3A)	$9	$9	$9	$9
228	Wireless telecommunication companies	Tax administration and equity	1998	§ 47-1508(a)(7)	minimal	minimal	minimal	minimal
229	Works of art lent to the National Gallery	Tax administration and equity	1950	§ 47-1508(a)(2)	$0	$0	$0	$0

PART I: FEDERAL CONFORMITY TAX EXPENDITURES

Income Tax
Exclusions

1. Capital gains on assets transferred at death

Internal Revenue Code Sections: 1001, 1002, 1014, 1015, 1023, 1040, 1221, and 1222
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$39,936	$46,694	$53,555	$62,660
Total	**$39,936**	**$46,694**	**$53,555**	**$62,660**

DESCRIPTION: When property is transferred upon the death of an owner, unrealized capital gains on the property are excluded from personal taxable income. The new basis of taxation for the heir is the market value of the property on the date of the owner's death, rather than the original cost of the asset (this is sometimes called the "step-up basis"). This policy departs from the normal treatment of capital gains, which are taxed on the difference between the sales price and the original cost of the asset. The major assets that typically generate capital gains are corporate stock, real estate, and owner-occupied housing.

PURPOSE: Although the original rationale for the exclusion is not clear, a current argument is that death is not an appropriate event to trigger a recognition of income.[9] In addition, there would be an administrative burden both for taxpayers and the IRS to determine the original price of some assets that were purchased long ago (and for which records may be lacking).

IMPACT: The Congressional Research Service states that, "The exclusion of capital gains at death is most advantageous to individuals who need not dispose of their assets to achieve financial liquidity. Generally speaking, these individuals tend to be wealthier. The deferral of tax on the appreciation involved, combined with the exemption for the appreciation before death, is a significant benefit for those investors and their heirs."[10]

With regard to economic efficiency, CRS notes that, "Failure to tax capital gains at death encourages lock-in of assets, which in turn means less current turnover of funds available for investment."[11] In addition, "Lower capital gains taxes may disproportionately benefit real estate investments and may cause corporations to retain more earnings than would otherwise be the case, causing efficiency losses. At the same time, lower capital gains taxes reduce the distortion that favors corporate debt over equity, which produces an efficiency gain." [12]

[9] U.S. Senate, Committee on the Budget, Tax Expenditures: Compendium of Background Material on Individual Provisions, Senate Print 111-58, prepared by the Congressional Research Service (December 2010), p. 417.

[10] U.S. Senate, Committee on the Budget, p. 416.

[11] U.S. Senate, Committee on the Budget, p. 416.

[12] U.S. Senate, Committee on the Budget, pp. 417-418.

Income Tax
Exclusions

2. Cash accounting, other than agriculture

Internal Revenue Code Sections: 446 and 448
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1916

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	$1,028	$1,028	$1,121	$1,172
Total	**$1,028**	**$1,028**	**$1,121**	**$1,172**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Employee-owned service businesses and other small businesses with average annual gross receipts of less than $5 million for the last three years have the option of using the cash method of accounting instead of the accrual method. Using the cash method for tax purposes effectively defers corporation and personal income taxes by allowing qualified businesses to record income when it is received rather than when it is earned (the accrual method).

PURPOSE: The purpose of the exclusion is to simplify record keeping and eliminate an additional drain on the working capital of small businesses

IMPACT: Small businesses and personal service corporations benefit from this provision. The Congressional Research Service states that cash accounting allows businesses to "exercise greater control over the timing of receipts and payments for expenses. By shifting income or deductions from one tax year to another, taxpayers can defer the payment of income taxes or take advantage of lower rates. At the same time, the cash method of accounting entails lower costs of compliance. It is also the method most familiar to the individuals and small businesses able to use it for tax purposes."[13]

[13] U.S. Senate, Committee on the Budget, p. 477.

Income Tax
Exclusions

3. Credit union income

Internal Revenue and U.S. Code Sections: 501(c)(14) and 12 USC 1768
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1937

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$324	$324	$454	$544
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$324**	**$324**	**$454**	**$544**

DESCRIPTION: The income of a credit union is exempt from corporate income tax. Credit unions are non-profit cooperatives organized by people with a common bond (such as membership in the same profession) that distinguishes them from the general public. Members of the credit union pool their funds to make loans to one another. The earnings that the credit union distributes to its depositors (as opposed to earnings that it retains) are subject to taxation.

Credit unions initially gained tax-exempt status in 1937 when they were included in a broader exemption for domestic building and loan associations. In 1951, a specific tax exemption for credit unions was enacted.

PURPOSE: According to the U.S. Government Accountability Office (GAO), credit unions "continue to be exempt because of their cooperative, not-for-profit structure, which is distinct from other depository institutions, and because credit unions have historically emphasized serving people of modest means."[14]

IMPACT: Credit unions and their members benefit from this provision. The Congressional Research Service states that, "For a given addition to retained earnings, this tax exemption permits credit unions to pay members higher dividends and charge members lower interest rates on loans. Over the past 25 years, this tax exemption may have contributed to the more rapid growth of credit unions compared to other depository institutions."[15]

Proponents of the exemption emphasize that credit unions are directed by volunteers for the purpose of serving their members, rather than maximizing profits. CRS also points out that, "Supporters argue that credit unions are subject to certain regulatory constraints not required of other depository institutions and that these constraints may reduce the competitiveness of credit unions. For example, credit unions may only accept deposits of members and lend only to members, other credit unions, or credit union organizations."[16]

[14] U.S. Government Accountability Office, "Financial Institutions: Issues Regarding the Tax-Exempt Status of Credit Unions," Highlights of GAO-06-220T, Testimony before the Committee on Ways and Means, House of Representatives, November 3, 2005.

[15] U.S. Senate, Committee on the Budget, p. 301.

[16] U.S. Senate, Committee on the Budget, p. 303.

On the other hand, "Proponents of taxation argue that deregulation has caused extensive competition among all depository institutions, including credit unions, and that the tax exemption gives credit unions an unwarranted advantage. Proponents of taxation argue that depository institutions should have a level playing field in order for market forces to allocate resources effectively."[17] In fact, the U.S. Department of the Treasury's 1984 tax reform report to President Reagan recommended repealing the exclusion of credit union income on precisely those grounds.[18]

It is also not clear to what extent credit unions serve people of low or moderate incomes and pass on the savings from the tax exclusion to credit union members. In testimony to the U.S. House Committee on Ways and Means in November 2005, a GAO official stated that, "(S)ome studies, including one of our own, indicate that credit unions serve a slightly lower proportion of households with low and moderate incomes than banks."[19]

[17] U.S. Senate, Committee on the Budget, p. 303.

[18] U.S. Treasury Department, Tax Reform for Fairness, Simplicity, and Economic Growth, The Treasury Department Report to the President, Volume 1, Overview (November 1984), p. 133.

[19] U.S. Government Accountability Office, "Financial Institutions: Issues Regarding the Tax-Exempt Status of Credit Unions," Statement of Richard Hillman, Managing Director, Financial Markets and Community Investments, before the Committee on Ways and Means, House of Representatives (GAO-06-220T), November 3, 2005, p. 9.

Income Tax
Exclusions

4. Distribution from redemption of stock to pay taxes imposed at death

Internal Revenue Code Sections: 303
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1950

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$280	$374	$374	$436
Total	**$280**	**$374**	**$374**	**$436**

DESCRIPTION: When a shareholder in a closely-held business dies, a partial redemption of the stock (selling the stock back to the corporation) is treated as a sale or exchange of an asset eligible for long-term capital gain treatment, rather than as dividend income. The treatment of the redemption as a capital gain means that there is a "step up" in basis: the stock is valued for purposes of federal income tax as of the date that it was transferred to the decedent's heir or heirs, rather than the value at the initial time of purchase by the decedent. As a result, there will be little or no federal tax due on the redemption (depending on the exact timing of the redemption).[20]

In order to qualify for this tax benefit, at least 35 percent of the decedent's estate must consist of the stock of the corporation. The benefits of the exclusion cannot exceed the estate taxes and expenses (funeral and administrative) that are incurred by the estate.

PURPOSE: According to the Congressional Research Service, this provision was adopted due to "congressional concern that estate taxes would force some estates to liquidate their holdings in a family business. There was further concern that outsiders could join the business, and the proceeds from any stock sales used to pay taxes would be taxable income under the income tax."[21]

IMPACT: Family businesses benefit from this provision, because it creates an incentive to sell stock back to the business in order to pay estate taxes. CRS observes that only a small percentage of businesses (approximately 3.5 percent) are subject to the estate tax, so a small number of wealthy families stand to benefit from the exclusion.[22] CRS also states that, "There are no special provisions in the tax code, however, for favorable tax treatment of other needy redemptions, such as to pay for medical expenses. To take advantage of this provision the decedent's estate does not need to show that the estate lacks sufficient liquid assets to pay taxes

[20] There could be some tax liability if the stock appreciates between the time it is bequeathed to the heir or heirs and the time it is sold back to the closely-held business.

[21] U.S. Senate, Committee on the Budget, p. 514.

[22] U.S. Senate, Committee on the Budget, p. 513.

and expenses. Furthermore, the proceeds of the redemption do not have to be used to pay taxes or expenses."[23]

[23] U.S. Senate, Committee on the Budget, p. 514.

Income Tax
Exclusions

5. Gain on like-kind exchanges

Internal Revenue Code Section: 1031
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$1,296	$1,490	$1,685	$1,938
Personal Income Tax Loss	$1,229	$1,434	$1,536	$1,728
Total	**$2,525**	**$2,924**	**$3,221**	**$3,666**

DESCRIPTION: When business or investment property is exchanged for property of a "like kind," no gain or loss is recognized on the exchange and therefore no tax is paid on any appreciation in the property's value at the time of the exchange. This exclusion contrasts to the general rule that any sale or exchange of money or property is a taxable event.

PURPOSE: According to the Congressional Research Service, the rationale for allowing these tax-free exchanges is "that the investment in the new property is merely a continuation of the investment in the old."[24]

IMPACT: CRS states that, "The like-kind exchange rules have been liberally interpreted by the courts to allow tax-free exchanges of property of the same general type but of very different quality and use. All real estate, in particular is considered 'like-kind'… The provision is very popular with real estate interests, some of whom specialize in arranging property exchanges. It is useful primarily to persons who wish to alter their real estate holdings without paying tax on their appreciated gain. Stocks and financial instruments are generally not eligible for this provision, so it is not useful for rearranging financial portfolios."

CRS further points out that the exclusion serves to "simplify transactions and make it less costly for businesses and investors to replace property. Taxpayers gain further benefit from the loose definition of 'like-kind,' because they can also switch their property holdings to types they prefer without tax consequences. This might be justified as reducing the inevitable bias a tax on capital gains causes against selling property, but it is difficult to argue for restricting the relief primarily to those taxpayers engaged in sophisticated real estate transactions."[25] In addition, the "like-kind" rule creates an economic distortion by encouraging investment in land and buildings, rather than in stock and other financial assets, when real estate might not otherwise represent the most productive use of capital.

[24] U.S. Senate, Committee on the Budget, p. 426.

[25] U.S. Senate, Committee on the Budget, p. 427.

Income Tax
Exclusions

6. Imputed interest

Internal Revenue Code Sections: 163(e), 483, 1274 and 1274A
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1964

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	$402	$482	$482	$530
Total	**$402**	**$482**	**$482**	**$530**

Note: “Too small” means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: For debt instruments that do not bear a market rate of interest, the Internal Revenue Service assigns or “imputes” a market rate to them to estimate interest payments for tax purposes. The imputed interest must be included as income to the recipient and is deducted by the payer. There are several exceptions to this general rule, covering debt associated with the sale of property when the total sales price is no more than $250,000; the sale of farms or small businesses by individuals when the sales price is no more than $1 million; and the sale of a personal residence. An interest rate greater than 9 percent may not be assigned to debt instruments given in exchange for real property for amounts less than an inflation-adjusted maximum (currently $3.3 million or $4.6 million, depending on the debt instrument used).

The tax expenditure is the revenue loss caused by the exceptions to the imputed interest rule listed above. A common example of this exemption is a low-interest, no-interest, or “gift” loan involved in the sale of property between family members.

PURPOSE: The purpose of the exclusion is to reduce the tax burden on the sales of homes, small businesses, and farms, and to allow buyers to structure the purchase of property that would otherwise be unaffordable under financial market rates and conditions. Essentially, the exclusion allows a limited set of transactions to take place without restrictions on seller financing. The restrictions on the exclusion are intended to prevent the tax avoidance that may result if the seller charges an artificially high sales price (to shift income toward tax-favored capital gains) and an artificially low interest rate (to shift income out of taxable interest payments).

IMPACT: Sellers of residences, small businesses, and farms who would have to pay tax on interest they do not charge, and otherwise will not receive, benefit from this provision. The imputed interest rules have been less important since the Tax Reform Act of 1986 took effect, because tighter depreciation rules limited the arbitrage opportunities from seller-financed transactions.[26]

[26] U.S. Senate, Committee on the Budget, p. 461.

Income Tax
Exclusions

7. Interest on small-issue qualified private-activity bonds (IDBs)

Internal Revenue Code Sections:	103, 141, 144, and 146
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1968

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$65	$65	$65	$65
Personal Income Tax Loss	$221	$221	$221	$221
Total	**$286**	**$286**	**$286**	**$286**

DESCRIPTION: Interest income on state and local bonds that are used to finance loans of $1 million or less for the construction of private manufacturing facilities is tax-exempt. These bonds, which are known as "small-issue industrial development bonds" (IDBs) are classified as private-activity bonds rather than governmental bonds because a substantial portion of the benefits accrues to private individuals or businesses.

The $1 million loan limit for a single project may be raised to $20 million if the aggregate amount of related capital expenditures (including those financed by tax-exempt bond proceeds) made over a six-year period is not expected to exceed $20 million. Total borrowing for any borrower is limited to $40 million. The small-issue IDBs are also subject to caps on the the volume of private-activity bonds that each state can issue.

State and local governments initially faced no restrictions on the use of tax-exempt bonds for economic development. Congress first imposed limits on the amount of the bond issuance and the size of the projects supported in 1968.

PURPOSE: The Congressional Research Service notes that small-issue IDBs are supported by Congress as a way to encourage investment in manufacturing.[27] Because the interest on the bonds is tax-exempt, buyers are willing to accept lower interest rates for the small-issue IDBs than they would for taxable securities, which in return reduces the cost of financing for the manufacturers.

IMPACT: CRS states that, "It is not clear that the Nation benefits from these bonds. Any increase in investment, jobs, and tax base obtained by communities from their use of these bonds likely is offset by the loss of job and tax base elsewhere in the economy. National benefit could arise from relocating jobs and tax base to achieve social or distributional objectives. The use of the bonds, however, is not targeted to specific geographic areas that satisfy explicit federal criteria such as median income or unemployment …" CRS also points out that, "With a greater supply of public bonds, the interest rate on bonds necesasrily increases to lure investors. In addition, expanding the availability of tax-exempt bonds also increases the assets available to individuals and corporations to shelter their income from taxation."[28]

[27] U.S. Senate, Committee on the Budget, p. 481.

[28] U.S. Senate, Committee on the Budget, p. 481.

Income Tax
Exclusions

8. Magazine, paperback and record returns

Internal Revenue Code Section: 458
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1978

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	too small	too small	too small	too small
Total	**too small**	**too small**	**too small**	**too small**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Generally, if a buyer returns goods to the seller, the seller's income is reduced in the year in which the items are returned. This tax expenditure involves an exemption from this rule for publishers and distributors of magazines, paperbacks, and records (records include discs, tapes, and similar objects that contain pre-recorded sounds).

Publishers and distributors may elect to exclude from corporate or personal taxable income any goods sold during a tax year that are returned shortly after the close of the tax year. Specifically, magazines must be returned within two months and 15 days after the end of the tax year, and paperbacks and records must be returned within four months and 15 days. This allows publishers and distributors to sell more copies to wholesalers and retailers than they expect will be sold to consumers.

PURPOSE: The purpose of the exclusion is to avoid taxing publishers and distributors of magazines, paperbacks, and records on accrued income when goods that are sold in one year are returned after the close of the year.

IMPACT: Publishers and distributors of magazines, paperbacks and records benefit from this provision. The Congressional Research Service notes that, "The special tax treatment granted to publishers and distributors of magazines, paperbacks, and records is not available to producers and distributors of other goods. On the other hand, publishers and distributors of magazines, paperbacks, and records often sell more copies to wholesalers and retailers than they expect will be sold to consumers."[29] In 1984, the U.S. Treasury Department's tax reform report to President Reagan recommended repealing the exclusion as an unnecessary subsidy.[30]

[29] U.S. Senate, Committee on the Budget, p. 468.

[30] U.S. Department of the Treasury, Tax Reform for Fairness, Simplicity, and Economic Growth, Volume 1, Overview, p. 150.

Income Tax
Exclusions

9. Discharge of certain student loan debt

Internal Revenue and U.S. Code Sections:	108(f), 20 U.S.C. 1087ee(a)(5) and 42 U.S.C. 254l-1(g)(3)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1984

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$127	$127	$127	$127
Total	**$127**	**$127**	**$127**	**$127**

DESCRIPTION: In general, canceled or forgiven debt, or debt that is repaid on a borrower's behalf, is considered taxable income. However, federal law allows an exclusion for the discharge of student loan debt by the federal, state, or local governments; public benefit corporations that operate a state, county, or municipal hospital;, and qualified educational institutions based on an individual's agreement to work in a certain type of occupation for a specified period of time.

Programs covered by the exclusion include loan forgiveness for teachers and public service employees under the federal direct student loan program, loan forgiveness for teachers under federal guaranteed loan programs, and loan cancelation for public service employees under the federal Perkins Loan program. Certain law school loan repayment programs are also eligible, as are loan payments made on behalf of health professionals who work in shortage areas under the National Health Service Corps Loan Repayment Program or state programs funded by the Public Health Service Act.

PURPOSE: The purpose of the exclusion is to encourage individuals to work in certain high-priority occupations (such as public health or education) or in certain locations (such as health professional shortage areas) by providing student loan forgiveness as an incentive.

IMPACT: Individuals with student loans forgiven under the program benefit from this provision. The industries and geographic areas targeted for the incentive may also benefit. The Congressional Research Service states that, "The value to an individual of excluding the discharge of student loan indebtedness from gross income depends on that individual's marginal tax rate in the tax year in which the benefit is realized ... In many instances, borrowers employed in these types of professions will be in lower tax brackets than if they had taken higher-paying jobs elsewhere."[31] CRS also points out that the impact of loan forgiveness programs and the tax exclusion for discharged student loan debt on occupational choices is not known.[32]

[31] U.S. Senate, Committee on the Budget, pp. 663-664.

[32] U.S. Senate, Committee on the Budget, p. 663.

Income Tax
Exclusions

10. Earnings of Coverdell education savings accounts

Internal Revenue Code Section: 530
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1998

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$127	$127	$253	$380
Total	**$127**	**$127**	**$253**	**$380**

DESCRIPTION: A taxpayer may establish a Coverdell education savings account (ESA) to pay for the qualified education expenses of a named beneficiary.[33] Qualified expenses include tuition, fees, books, supplies, and room and board for elementary, secondary, and higher education. Annual contributions to an account cannot exceed $2,000 and cannot be made after the beneficiary reaches age 18. The annual contribution is not deductible, but any earnings on the contributions are tax-free until they are distributed.

The maximum allowable contribution is reduced for taxpayers with annual incomes over $95,000 and is phased out completely at an annual income level of $110,000 (the comparable thresholds are $190,000 and $210,000 for a joint return). The portion of the distribution attributed to principal is not taxed, but the earnings may be taxed depending on the amount of qualified higher education expenses that the beneficiary has incurred. The tax-free status of distributions for elementary and secondary education is scheduled to expire on December 31, 2012.

A contributor may fund multiple accounts for the same beneficiary (subject to the $2,000 annual limit) and a student may be the designated beneficiary of multiple accounts. With the exception of accounts for special needs beneficiaries, Coverdell ESA balances must be fully distributed by the time the beneficiaries reach the age of 30.

PURPOSE: According to the Congressional Research Service, "These benefits reflect congressional concern that families are having increasing difficulty paying for college. They also reflect an intention to subsidize middle-income families that otherwise do not qualify for much need-based federal student aid."[34]

IMPACT: CRS points out that, "Families that have the wherewithal to save are more likely to benefit. Whether families will save additional sums might be doubted. Tax benefits for Coverdell ESAs are not related to the student's cost of attendance or other family resources, as is most federal student aid for higher education. Higher-income families also are more likely than lower-income families to establish accounts for their children's K-12 education expenses."[35]

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[33] The program is named after the late Senator Paul Coverdell of Georgia, who was the chief sponsor of the authorizing legislation. Coverdell ESAs are sometimes called "Coverdell plans."

[34] U.S. Senate, Committee on the Budget, p. 623.

[35] U.S. Senate, Committee on the Budget, p. 623.

Income Tax
Exclusions

11. Earnings of qualified tuition programs

Internal Revenue Code Section: 529
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1997

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$760	$887	$1,014	$1,186
Total	**$760**	**$887**	**$1,014**	**$1,186**

DESCRIPTION: There are two types of qualified tuition programs (QTPs) that allow people to pay in advance or save for college expenses for designated beneficiaries: (1) prepaid tuition plans, and (2) college savings plans. Prepaid tuition plans allow account owners to make tuition payments for beneficiaries at current prices, thereby providing a hedge against inflation. College savings plans allow account owners to save and invest money on a tax-favored basis that can be used to pay for higher education expenses (tuition and fees, books, supplies, room and board).

The District of Columbia sponsors a college savings plan, but does not offer a prepaid tuition plan. Nevertheless, it is possible to participate in a prepaid tuition plan outside of one's current state of residence. Only states can sponsor college savings accounts, but both states and institutions of higher education offer prepaid tuition plans.

Contributors can fund multiple QTP accounts for the same beneficiary in different states, and an individual may be the designated beneficiary of accounts established by different contributors. Sponsors can establish their own restrictions, and the specifics of each plan vary from state to state. One difference between QTPs and Coverdell education savings accounts (see tax expenditure #10 on the previous page) is that there are no income restrictions or contribution limits for QTPs. Individuals can contribute to QTPs and Coverdell plans during the same year.

Contributions to QTPs are taxable, but the earnings on contributions as well as the distributions from the accounts are free from federal income tax. Non-qualifying distributions are subject to a 10 percent penalty, and the earnings share of a non-qualifying distribution is subject to federal income tax.

PURPOSE: The purpose of the exclusion is to help families save for higher education.

IMPACT: The Congressional Research Service states that the benefits of QTPs are generally limited to higher-income families who have the resources to save for college and face higher marginal tax rates that increase the value of the tax savings.[36] Urban Institute researchers have questioned whether the plans have an impact on college savings because higher-inome families have the resources to set aside funding for higher education without the tax incentives.[37]

[36] U.S. Senate, Committee on the Budget, pp. 635-636.

[37] Elaine Maag and Katie Fitzpatrick, "Federal Financial Aid for Higher Education: Programs and Prospects," Urban Institute discussion paper issued January 2004 (available at www.urban.org), pp. 24-25.

Income Tax
Exclusions

12. Employer-provided education assistance

Internal Revenue Code Section: 127
Federal Law Sunset Date: December 31, 2012
Year Enacted in Federal Law: 1978

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	sunset	sunset
Personal Income Tax Loss	$769	$769	sunset	sunset
Total	**$769**	**$769**	**sunset**	**sunset**

DESCRIPTION: An employee may exclude from income certain amounts paid by his or her employer for education assistance, including tuition, fees, and books. The maximum exclusion is $5,250 per year. Any excess is part of an employee's gross income and is subject both to income and payroll taxes. The exclusion applies regardless of whether the employer pays the expenses, reimburses the employee for expenses, or provides the education directly. The coursework does not have to be job-related, but courses involving sports, games, or hobbies are eligible for the exclusion only if they are job-related.

This exclusion was first enacted in 1978 as a temporary provision and has been renewed more than 10 times. Most recently, the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 extended the exclusion through December 31, 2012.

PURPOSE: The purpose of the exclusion is to encourage employers to offer education assistance to their employees.

IMPACT: The Congressional Research Service states that, "The exclusion allows certain employees, who otherwise might be unable to do so, to continue their education. The value of the exclusion is dependent upon the amount of educational expenses furnished and the marginal tax rate."[38]

CRS adds that, "The availability of employer educational assistance encourages employer investment in human capital, which may be inadequate in a market economy because of spillover effects (i.e., the benefits of the investment extend beyond the individuals undertaking additional education and the employers for whom they work). Because all employers do not provide educational assistance, however, taxpayers with similar incomes are not treated equally."[39] The following groups of employees are much more likely to receive employer-provided educational assistance than other workers: employees in management, professional, and related jobs; full-time employees; employees who belong to labor unions; employees whose wages are in the top half of the earnings distribution; and employees at firms with 100 or more employees.[40]

[38] U.S. Senate, Committee on the Budget, p. 674.

[39] U.S. Senate, Committee on the Budget, p. 675.

[40] U.S. Senate, Committee on the Budget, p. 675.

President Bush's Advisory Panel on Federal Tax Reform recommended repealing this exclusion (as well as several other exclusions for fringe benefits) because, "The favorable tax treatment of fringe benefits results in an uneven distribution of the tax burden as workers who receive the same amount of total compensation pay different amounts of tax depending on the mix of cash wages and fringe benefits."[41]

[41] The President's Advisory Panel on Federal Tax Reform, Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System (November 2005), p. 85.

Income Tax
Exclusions

13. Employer-provided tuition reduction

Internal Revenue Code Sections: 117(d)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$171	$171	$171	$171
Total	**$171**	**$171**	**$171**	**$171**

DESCRIPTION: Tuition reductions for employees of educational institutions may be excluded from federal taxable income if the reductions do not represent payment for services. The exclusion also applies to tuition reductions for an employee's spouse and dependent children.

PURPOSE: The Congressional Research Service states that, "Language regarding tuition reductions was added by the Deficit Reduction Act of 1984 as part of legislation codifying and establishing boundaries for tax-free fringe benefits; similar provisions had existed in regulations since 1956."[42]

IMPACT: CRS notes that, "The exclusion of tuition reductions lowers the net cost of education for employees of educational institutions … Tuition reductions are provided by education institutions to employees as a fringe benefit, which may reduce costs of labor and turnover. In addition, tuition reductions for graduate students providing research and teaching services for the educational institution also contribute to reducing the education institution's labor costs. Both employees and graduate students may view the reduced tuition as a benefit of their employment that encourages education. The exclusion may serve to in effect pass some of the education institutions' labor costs on to other taxpayers."[43]

[42] U.S. Senate, Committee on the Budget, pp. 643-644.

[43] U.S. Senate, Committee on the Budget, pp. 643-644.

Income Tax
Exclusions

14. Interest on education savings bonds

Internal Revenue Code Section: 135
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1988

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$25	$25	$25	$25
Total	**$25**	**$25**	**$25**	**$25**

DESCRIPTION: Part or all of the interest earned on U.S. Series EE or Series I savings bonds can be excluded from taxable income if the bonds are used to finance higher education expenses for the taxpayer, the taxpayer's spouse, or the taxpayer's dependents.[44] The bonds must have been issued after 1989, and the owner must have been at least 24 years old at the time of issuance. The proceeds must be used for qualified higher education expenses (which generally cover tuition and fees, but not room and board) in the same year that they are redeemed.

In tax year 2011, a full exclusion was allowed for taxpayers with income less than $70,100 (single) and $105,100 (married). The exclusion was phased out through incomes up to $85,100 (single) and $135,100 (married). Taxpayers with incomes above those levels did not qualify for any exclusion. The phase-out thresholds are adjusted annually for inflation.

PURPOSE: The purpose of the exclusion is to encourage lower- and middle-income families to save for their children's college education.

IMPACT: The Congressional Research Service states that, "Education savings bonds provide lower- and middle-income families with a tax-favored way to save for higher education that is convenient and familiar. The benefits are greater for families who live in states and localities with high income taxes because the interest income from Series EE and Series I Bonds is exempt from state and local income taxes."[45]

Several restrictions limit the value of education savings bonds as a college savings vehicle. CRS observes that, "Since the interest exclusion for Education Savings Bonds can be limited when the bonds are redeemed, families intending to use them for college expenses must predict their income eligibility far in advance. They must also anticipate the future costs of tuition and fees and whether their children might receive scholarships … In these respects, the bonds may not be as attractive an investment as some other education savings vehicles."[46]

[44] The Series I bond, which provides coupon payments indexed to inflation, was established in 1998.

[45] U.S. Senate, Committee on the Budget, p. 626.

[46] U.S. Senate, Committee on the Budget, p. 627.

Income Tax
Exclusions

15. Interest on state and local private-activity bonds issued to finance education facilities

Internal Revenue Code Sections: 103, 141,142(k), 145, 146, and 501(c)(3)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$583	$648	$648	$684
Personal Income Tax Loss	$2,547	$2,768	$2,879	$3,066
Total	**$3,130**	**$3,416**	**$3,527**	**$3,750**

DESCRIPTION: Interest income on state and local bonds used to finance the construction of non-profit educational facilities (such as classrooms and dormitories) and qualified public educational facilities is tax-exempt. These bonds are classified as private-activity bonds, rather than governmental bonds, because a substantial portion of the benefits accrues to individuals or private organizations instead of the general public.

Bonds issued for non-profit educational facilities are not subject to the state volume cap on private-activity bonds, but there is a cap of $150 million on the amount of bonds any non-profit institution can have outstanding. Public colleges and universities can also issue tax-exempt bonds to finance facilities that are owned by private, for-profit corporations. Tax-exempt bonds issued for qualified public education facilities are subject to a separate state-by-state cap equal to $10 per capita or $5 million per year, whichever is greater.

PURPOSE: The purpose of the education private-activity bonds is to support the construction or substantial rehabilitation of university facilities by subsidizing low-interest loans. Investors purchase the bonds at low interest rates because the income from them is tax-free.

IMPACT: The tax-exempt bonds benefit universities by helping them finance facilities at reduced interest rates. According to the Congressional Budget Office and the Joint Committee on Taxation, education facility bonds accounted for 17 percent of total state and local private-activity bond issuance from 1991 to 2007, growing 11 percent annually during that period.[47]

The Congressional Research Service observes that non-profit universities may be "using their tax-exempt status to subsidize goods and services for groups that might receive more critical scrutiny if they were subsidized by direct federal expenditures."[48] Furthermore, "As one of many categories of tax-exempt bonds, nonprofit educational facilities and public education bonds have increased the financing costs of bonds issued for more traditional public capital stock. In

[47] Congressional Budget Office and the Joint Committee on Taxation, Subsidizing Infrastructure Investment with Tax-Preferred Bonds (Washington, D.C.: Congressional Budget Office and Joint Committee on Taxation, 2009), pp. 19-23.

[48] U.S. Senate, Committee on the Budget, p. 650.

addition, this class of tax-exempt bonds has increased the supply of assets that individuals and corporations can use to shelter income from taxation."[49]

[49] U.S. Senate, Committee on the Budget, pp. 650-651.

Income Tax
Exclusions

16. Interest on state and local private-activity student loan bonds

Internal Revenue Code Sections:	103, 141, 144(b), and 146
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1965 (general exclusion for state and local bonds was enacted in 1913, but student loan bonds were not offered until enactment of the Higher Education Act of 1965)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$65	$130	$130	$194
Personal Income Tax Loss	$443	$443	$443	$443
Total	**$508**	**$573**	**$573**	**$637**

DESCRIPTION: Student loan bonds, which are issued by state and local governments to finance student loans at below-market rates, represent another type of tax-exempt, private-activity bond. These bonds are subject to a state's annual volume cap on private-activity bonds, and therefore msut compete for tax-exempt financing with all other private-activity bonds that are subject to the cap. The tax expenditure represents the revenue loss from the exclusion of interest on the bonds.

In addition, this tax expenditure includes the revenue loss from federal government loan programs (such as Stafford, PLUS, and Consolidation loans) that were carried out through private lenders and financed in part by tax-exempt debt. As of July 1, 2010, the federal government is providing loans directly instead of operating through private lenders. Nevertheless, there is an ongoing revenue loss from loans that have already been issued.

PURPOSE: The purpose of these private-activity bonds is to increase access to higher education by subsidizing low-interest loans. Investors purchase the bonds at below-market interest rates because the income from them is tax-free.

IMPACT: Students benefit from the exclusion, which may also generate spillover benefits to society from a more educated citizenry. The lower interest rate on the bonds may increase the availability of student loans by lowering the cost of government borrowing, but it does not reduce the interest rate charged to students, which is set by federal law. Students present a high credit risk due to their uncertain earning prospects, meaning that the private sector may not supply a sufficient amount of capital for higher education due to the risk. Subsidies can help correct this market failure.[50]

The Congressional Research Service points out that other federal programs, such as subsidized direct loans, may be sufficient to address the market failure. Tax-exempt financing also involves potential costs. CRS states that, "As one of many categories of tax-exempt private-activity bonds, bonds issued for student loans have increased the financing costs of bonds issued for public capital stock, and have increased the supply of assets available to individuals and corporations to shelter their income from taxation."[51]

[50] U.S. Senate, Committee on the Budget, p. 641.

[51] U.S. Senate, Committee on the Budget, p. 641.

Income Tax
Exclusions

17. Scholarship and fellowship income

Internal Revenue Code Section: 117
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,041	$3,168	$3,421	$3,635
Total	**$3,041**	**$3,168**	**$3,421**	**$3,635**

DESCRIPTION: Scholarships and fellowships are excluded from personal taxable income to the extent that they cover tuition and course-related expenses of students enrolled in primary, secondary, or higher education. The exclusion covers awards based on financial need (such as Pell Grants) as well as those based on academic achievement or merit (such as National Merit Scholarships). Eligible educational institutions must maintain a regular teaching staff and curriculum, and have a regularly enrolled student body attending classes where the school carries out its instructional activities.

PURPOSE: This exclusion was orginally enacted to clarify the status of education grants. Until this provision was enacted in 1954, scholarships and fellowships were included in gross income unless it could be proven that the money was a gift. The Congressional Research Service observes that the present rationale for the exclusion, in light of the expansion of need-based grants, "rests upon the hardship that taxation would impose. If the exclusion were abolished, awards could arguably be increased to cover students' additional tax liability, but the likely effect would be that fewer students would get assistance."[52]

IMPACT: CRS states that, "The exclusion reduces the net cost of education for students who receive financial aid in the form of scholarships or fellowships. The potential benefit is greatest for students at schools where higher tuition charges increase the amount of scholarship or fellowship assistance that might be excluded."[53] As a result, students attending private colleges and universities may claim a disproportionate share of the benefits.

CRS adds that, "The exclusion provides greater benefits to taxpayers with higher marginal tax rates. While students themselves generally have low (or even zero) marginal rates, they often are members of families subject to higher rates. Determining what ought to be the proper taxpaying unit for college students complicates assessment of the exclusion."[54]

[52] U.S. Senate, Committee on the Budget, p. 646.

[53] U.S. Senate, Committee on the Budget, p. 646.

[54] U.S. Senate, Committee on the Budget, p. 647.

Income Tax
Exclusions

18. Cafeteria plan benefits

Internal Revenue Code Section: 125
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1974

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$27,597	$30,844	$33,322	$36,787
Total	**$27,597**	**$30,844**	**$33,322**	**$36,787**

DESCRIPTION: Cafeteria plans are employer-sponsored benefit packages that offer employees a choice between taking cash and receiving qualified benefits, such as accident and health coverage, group-term life insurance, dependent care assistance, and adoption assistance. The employee pays no tax on the value of the benefits but does pay tax if he or she chooses the cash.

Most flexible spending accounts (FSAs), which reimburse employees for specific expenses (subject to reimbursement maximums) are governed by cafeteria plan provisions because they involve a choice between cash wages and non-taxable benefits. FSAs allow employees to make pre-tax contributions for the reimbursement of health and/or dependent care expenses. However, these arrangements have a "use or lose" rule. Beginning in 2013, contributions to health care FSAs will be capped at $2,500.

PURPOSE: The purpose of the exclusion is to encourage employers to include a flexible benefit package as part of their compensation package and to encourage employees to use the qualified benefit options.

IMPACT: The Congressional Research Service points out that, "As with other tax exclusions, the tax benefits are greater for taxpayers with higher incomes. Higher income taxpayers may be more likely to choose nontaxable benefits (particularly health care benefits) instead of cash, which would be taxable. Lower income taxpayers may be more likely to choose cash, which they may value more highly and for which the tax rates would be comparatively low."[55]

CRS further states that, "Ability to fine-tune benefits increases the efficient use of resources and may help some employees better balance competing demands of family and work."[56] Still, the exclusion may impair horizontal equity because, "(T)he favorable tax treatment of cafeteria plans leads to different tax burdens for individuals with the same economic income."[57]

[55] U.S. Senate, Committee on the Budget, p. 696.

[56] U.S. Senate, Committee on the Budget, p. 698.

[57] U.S. Senate, Committee on the Budget, p. 698.

Income Tax
Exclusions

19. Employee awards

Internal Revenue Code Sections: 74(c) and 274(j)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$374	$374	$374	$374
Total	**$374**	**$374**	**$374**	**$374**

DESCRIPTION: Certain awards of tangible personal property given to employees for length of service or for safety practices are excluded from personal taxable income, departing from the standard treatment of prizes and awards as taxable income. The amount of the exclusion is limited to $400 but can rise to $1,600 if it is part of a qualified employee achievement award plan that does not discriminate in favor of highly compensated employees. The employer is also allowed to deduct the cost from its taxable income. If the cost of the award to the employer and the fair market value of the award exceed the limits stated above, the employee must include the extra amount in his or her gross income.

There are several other restrictions designed to ensure that the awards do not constitute disguised compensation. Length of service awards cannot be granted to an empoyee in the first five years of service, or to an employee who received a length of service award in any of the prior four years of service. Awards for safety achievement cannot be awarded to a manager, administrator, clerical employee, or other professional employee. In addition, safety awards cannot be granted to more than 10 percent of employees in any year.

PURPOSE: The purpose of the exclusion is to clarify the tax treatment of employee awards and to encourage longevity in employment as well as safety practices on the job.

IMPACT: Employees who receive length-of-service or safety awards and employers who save costs related to training and time lost to injuries benefit from this provision. The Congressional Research Service points out that, "The exclusion recognizes a traditional business practice which may have social benefits. The combination on the limitation of the exclusion as to eligibility for qualifying awards, and the dollar amount of the exclusion not being increased since 1986, keep the exclusion from becoming a vehicle for significant tax avoidance. However, the lack of an increase in the exclusion effectively reduces the tax-free portion of some awards."[58]

[58] U.S. Senate, Committee on the Budget, p. 684.

Income Tax
Exclusions

20. Employee stock ownership plans

Internal Revenue Code Sections: 401(a)(28), 404(a)(9), 404(k), 415(c)(6), 1042, 4975(e)(7), 4978, and 4979A
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1974

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$719	$765	$745	$791
Personal Income Tax Loss	$419	$444	$470	$496
Total	**$1,138**	**$1,209**	**$1,215**	**$1,287**

DESCRIPTION: An employee stock ownership plan (ESOP) is a defined-contribution retirement plan that invests in the stock of a sponsoring employer. ESOPs involve several tax expenditures.

First, employer contributions may be deducted from corporate taxable income as a business expense. An employer may also deduct dividends paid on stock held by an ESOP if the dividends are paid to plan participants. Second, employees are not taxed on employer contributions or the earnings on invested funds until they are distributed. Third, a stockholder in a closely-held company may defer recognition of the gain from the sale of stock to an ESOP if, after the sale, the ESOP owns at least 30 percent of the company's stock and the seller reinvests the proceeds from the sale of stock in a U.S. company.

PURPOSE: The Congressional Research Service states that, "The tax incentives for ESOPs are intended to broaden stock ownership, provide employees with a source of retirement income, and grant employers a tax-favored means of financing."[59]

IMPACT: Employers and employees of participating companies benefit from the tax-favored status of ESOPs. Although most ESOPs are sponsored by private companies, the majority of ESOP participants are employed by public companies with 100 or more participants.[60]

CRS observes that, "These plans are believed to motivate employees by more closely aligning their financial interests with the financial interests of their employers. The distribution of stock ownership in ESOP firms is broader than the distribution of stock ownership in the general population."[61] Nevertheless, "(T)he requirement that ESOPs invest primarily in the stock of the sponsoring employer is consistent with the goal of corporate financing, but it may not be consistent with the goal of providing employees with retirement income … If a firm experiences financial difficulties, the value of its stock and its dividend payments will fall."[62]

[59] U.S. Senate, Committee on the Budget, p. 678.

[60] U.S. Senate, Committee on the Budget, p. 678.

[61] U.S. Senate, Committee on the Budget, p. 680
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[62] U.S. Senate, Committee on the Budget, p. 680

Income Tax
Exclusions

21. Employer-paid meals and lodging (other than military)

Internal Revenue Code Sections: 119 and 132(e)(2)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1918

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$940	$1,025	$1,025	$1,071
Total	**$940**	**$1,025**	**$1,025**	**$1,071**

DESCRIPTION: Employees can exclude from personal taxable income the fair market value of meals provided by employers if the meals are furnished on the employer's business premises and for the convenience of the employer. The fair market value of lodging provided by an employer can also be excluded from personal taxable income, if the lodging is furnished on business premises for the convenience of the employer, and if the employee is required to accept the lodging as a condition of employment (as when an apartment manager must live on the premises). The exclusion does not apply to cases in which an employee is reimbursed by the employer for amounts spent on meals and lodging.

In addition, the fair market value of meals provided to an employee at a subsidized eating facility operated by the employer is excluded from taxable income.

PURPOSE: The purpose of the exclusion is to eliminate a record-keeping burden and to recognize that the fair market value of employer-provided meals and lodging may be difficult to measure.

IMPACT: The Congressional Research Service states that, "The exclusion subsidizes employment in those occupations or sectors in which the provision of meals and/or lodging is common. Both the employees and their employers benefit from the tax exclusion. Under normal market circumstances, more people are employed in these positions than would otherwise be the case and they receive higher compensation (after tax). Their employers receive their services at lower cost. Both sides of the transaction benefit because the loss is imposed on the U.S. Treasury in the form of lower tax collections."[63]

[63] U.S. Senate, Committee on the Budget, p. 688.

Income Tax
Exclusions

22. Housing allowance for ministers

Internal Revenue Code Section: 107 and 265
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$598	$598	$598	$598
Total	**$598**	**$598**	**$598**	**$598**

DESCRIPTION: Ministers can exclude from personal taxable income the fair rental value of a church-owned or church-rented home furnished as part of their compensation, or a cash housing allowance paid as part of their compensation. The church must officially designate the allowance as being for housing before paying it to the minister, and the allowance cannot exceed the fair rental value of the minister's home. In addition, ministers who receive cash housing allowances may also claim them as tax deductions on their individual income tax returns if they are used to pay mortgage interest and real estate taxes on their residences.

PURPOSE: The Revenue Act of 1921 authorized only the exclusion for church-provided housing. Although there was "no stated rationale" for the exclusion, the Congressional Research Service notes that, "Congress may have intended to recognize clergy as an economically deprived group due to their relatively low incomes."[64] Congress added the exclusion for cash housing allowances in 1954, possibly to provide equal treatment among clergy members receiving different types of housing assistance from their churches. In clarifying the tax treatment of housing assistance to clergy members in the "Clergy Housing Allowance Clarification Act of 2002" (P.L. 107-181), Congress stated its desire to "minimize government intrusion into internal church operations and the relationship between a church and its clergy."

IMPACT: Ministers who receive a housing allowance or who live in a church-provided home benefit from this provision. CRS observes that, "The tax-free parsonage allowances encourage some congregations to structure maximum amounts of tax-free housing allowances into their minister's pay and may thereby distort the compensation package. The provision is inconsistent with economic principles of horizontal and vertical equity. Since all taxpayers may not exclude amounts they pay for housing from taxable income, the provision violates horizontal equity principles … Ministers with higher incomes receive a greater subsidy than lower-income ministers because those with higher incomes pay taxes at higher marginal tax rates. The disproportionate benefit of the tax exclusion to individuals with higher incomes reduces the progressivity of the tax sytem, which is viewed as a reduction in equity."[65] In addition, some ministers get a double dose of tax relief by deducting mortgage interest payments that were made with cash housing allowances that they can exclude from taxable income.

[64] U.S. Senate, Committee on the Budget, p. 702.

[65] U.S. Senate, Committee on the Budget, p. 703.

Income Tax
Exclusions

23. Miscellaneous fringe benefits

Internal Revenue Code Sections: 117(d) and 132
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$6,835	$7,006	$7,262	$7,488
Total	**$6,835**	**$7,006**	**$7,262**	**$7,488**

DESCRIPTION: Certain non-cash fringe benefits qualify for an exclusion from an employee's gross income. These benefits include services provided at no additional cost (such as free stand-by flights for airline employees), qualified employee discounts, working condition fringe benefits, certain tuition reductions, and *de minimis* fringe benefits (such as providing coffee to employees or allowing them occasional personal use of an office copy machine).

The benefits must be provided solely to employees, their spouses, and dependent children; retired employees; or the widows or widowers of former employees. Federal law requires that the imputed value of health and other fringe benefits of a domestic partner be included in taxable income. In addition, the provision of the fringe benefits cannot favor highly-paid employees.

PURPOSE: The Congressional Research Service states that, "Congress recognized that in many industries employees receive either free or discount goods and services that the employer sells to the general public. In many cases, these practices had been long established and generally had been treated by employers, employees, and the Internal Revenue Service as not giving rise to taxable income."[66] CRS further points out that, "Employees clearly receive a benefit from the availability of free or discounted goods or services, but the benefit may not be as great as the full amount of the discount. Employers may have valid business reasons, other than simply providing compensation, for encouraging employees to use the products they sell to the public … As with other fringe benefits, placing a value on the benefit in these cases is difficult."[67]

IMPACT: Both employers and employees benefit from this exclusion, which subsidizes employment in those businesses and industries in which ancillary fringe benefits are feasible and commonly offered. CRS states that, "Under normal market circumstances, more people are employed in these businesses and industries than they would otherwise be, and they receive higher compensation (after tax). Their employers receive their services at lower cost. Both sides of the transaction benefit because the loss is imposed on the U.S. Treasury in the form of lower tax collections." In addition, "Because the exclusion applies to practices which are common and may be feasible only in some businesses and industries, it creates inequities in tax treatment among different employees and employers."[68]

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[66] U.S. Senate, Committee on the Budget, p. 716.

[67] U.S. Senate, Committee on the Budget, p. 716.

[68] U.S. Senate, Committee on the Budget, p. 716.

Income Tax
Exclusions

24. Spread on acquisition of stock under incentive stock option plans and employee stock purchase plans

Internal Revenue Code Sections: 422 and 423
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1981

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	-$778	-$907	-$907	-$982
Personal Income Tax Loss	$280	$374	$374	$436
Total	**-$498**	**-$533**	**-$533**	**-$546**

DESCRIPTION: Employees may be granted stock options under an incentive stock option plan (which is capped at $100,000 annually per employee, and can be confined to officers or highly-paid employees) or an employee stock purchase plan (which is capped at $25,000 annually per employee, and must be offered to all full-time employees with at least two years of service). These plans allow employees to exercise the stock options within a specified time frame.

Generally, a stock option or purchase plan allows an employee to buy the stock for less than the current market price. At the time the employee exercises an option, the stock is transferred from the company to the employee, but the difference in value between the market value and the option prices (also known as the spread) is not considered taxable income. The value of this tax expenditure stems from the deferral of the tax until the employee sells the stock. If the stock is held one year from purchase and two years from the granting of the option, the gain is also taxed at the lower long-term capital gain rate.

The employer is not allowed a tax deduction for granting a stock option, but if the stock is not held for the required amount of time the employee is taxed at ordinary income tax rates (rather than lower capital gain rates) and the employer is allowed a deduction.

PURPOSE: According to the Congressional Research Service, the deferral of tax for qualified stock options was re-instituted by the Economic Recovery Tax Act of 1981 "with the justification that encouraging the management of a business to have a proprietary interest in its successful operation would provide an important incentive to expand and improve the profit position of the companies involved."[69] The deferral of taxable gains had been allowed between 1964 and 1976.

IMPACT: CRS describes the complex effects of this provision as follows: "Taxpayers with above average or high incomes are the primary beneficiaries of these tax advantages. Because employers (usually corporations) cannot deduct the cost of stock options eligible for the lower tax rate on long-term capital gains, employers pay higher income taxes. The prevailing view of tax economists is that the corporate income tax falls primarily on shareholders. Because most corporate stock is owned by high income households, these households bear the incidence of this

[69] U.S. Senate, Committee on the Budget, p. 692.

aspect of stock options. These conflicting effects on incidence mean that the overall incidence of qualified stock options is uncertain."[70]

CRS also observes that, "Paying for the services of employees, officers, and directors by the use of stock options has several advantages for the companies. Start-up companies often use this method because it does not involve the immediate cash outlays that paying salaries involves; in effect a stock option is a promise of a future payment, contingent on increases in the value of the company's stock. It also makes the employees' pay dependent on the performance of the company's (or at least the stock's) performance."[71]

[70] U.S. Senate, Committee on the Budget, p. 692.

[71] U.S. Senate, Committee on the Budget, p. 693.

Income Tax
Exclusions

25. Voluntary employees' beneficiary association income

Internal Revenue Code Sections:	419, 419A, 501(a), 501(c)(9) and 4976
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1928

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,588	$3,759	$3,930	$4,119
Total	**$3,588**	**$3,759**	**$3,930**	**$4,119**

DESCRIPTION: A voluntary employees' beneficiary association (VEBA) provides life, sickness, accident, and other insurance, as well as fringe benefits, to its employee members, their dependents, and their beneficiaries. The income earned by a VEBA is generally exempt from federal income taxes,[72] but when the benefits are distributed to individuals, the income is taxable unless there is a specific statutory exclusion. Accident and health benefits are excludable from income, but severance and vacation pay are not.

Most VEBAs are organized as trusts to be legally separate from their employers. VEBAs must meet a number of general requirements. Most importantly, they must be associations of employees who share a common employment-related bond, such as membership in a collective bargaining unit. In addition, membership in a VEBA must be voluntary and the association must be controlled by its members, by an independent trustee such as a bank, or by trustees or fiduciaries at least some of whom are designated by the members or on behalf of the members. Substantially all of the organization's operations must further the provision of life, sickness, accident, and other welfare benefits to employees and their families, and benefit plans (other than collectively-bargained plans) must not discriminate in favor of highly-compensated individuals.

PURPOSE: In describing the original intent of the tax exclusion for VEBAs, the Congressional Research Service states that, "Presumably, VEBAs were seen as providing welfare benefits that served a public interest and normally were exempt from taxation."[73]

IMPACT: There are a number of benefits from the tax-favored treatment of VEBAs. CRS notes that employers can use VEBAs to "earn tax-free investment returns, reduce future contribution requirements by prefunding, create an offsetting asset for an employer liability and meet requirements of rate making bodies and regulatory agencies." [74] CRS also points out that, "(T)he benefits of VEBAs are more likely to accrue in favor of the lower-paid employees, largely because, "VEBAs are used more often for unionized employees who are typically paid less than

[72] Income earned by a VEBA to pre-fund retiree health benefits is normally subject to tax, but an important exception applies to VEBAs that are established through collective bargaining.

[73] U.S. Senate, Committee on the Budget, p. 711.

[74] U.S. Senate, Committee on the Budget, p. 709.

management employees."[75] In addition, in the case of bankruptcy, "(T)he presence of a VEBA with accumulated assets for payment of retiree health benefits offers retirees a measure of protection."[76]

[75] U.S. Senate, Committee on the Budget, p. 711.

[76] U.S. Senate, Committee on the Budget, p. 713.

Income Tax
Exclusions

26. Interest on state and local private-activity bonds issued to support energy facilities

Internal Revenue Code Sections: 103, 141, 142(f), and 146
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1980

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$6	$6	$6	$6
Personal Income Tax Loss	$22	$22	$22	$33
Total	**$28**	**$28**	**$28**	**$39**

DESCRIPTION: Each state receives a certain amount of authority to issue tax-exempt private activity bonds, which are securities issued by a state or local government to finance qualified projects by a private user. Qualified projects, which include energy production facilities such as electric energy or gas, are expected to have a public benefit.

PURPOSE: The purpose of the bonds is to promote the construction of energy production facilities by subsidizing low-interest loans, and thereby expand the energy supply to residential and commercial users. Investors purchase the bonds at low interest rates because the income from them is tax-free.

IMPACT: Energy production companies as well as residential and commercial users of energy benefit from this provision. The Congressional Budget Office and the Joint Committee on Taxation estimate that energy facilities accounted for only 2 percent of total state and local private-activity bond issuance from 1991 to 2007.[77]

The Congressional Research Service observes that, "Even if a case can be made for a federal subsidy of energy production facilities based on underinvestment at the state and local level, it is important to recognize the potential costs. As one of many categories of tax-exempt private-activity bonds, those issued for energy production facilities increase the financing cost of bonds issued for other public capital. With a greater supply of public bonds, the interest rate on the bonds necessarily increases to lure investors. In addition, expanding the availability of tax-exempt bonds increases the range of assets available to individuals and corporations to shelter their income from taxation."[78]

[77] Congressional Budget Office and Joint Committee on Taxation, p. 19.

[78] U.S. Senate, Committee on the Budget, p. 135.

Income Tax
Exclusions

27. Accrued interest on savings bonds

Internal Revenue Code Sections: 454(c)
Federal Law Sunset Date: None for general deduction
Year Enacted in Federal Law: 1951

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$1,124	$1,205	$1,205	$1,248
Total	**$1,124**	**$1,205**	**$1,205**	**$1,248**

DESCRIPTION: Owners of U.S. Treasury Series E, EE, and I savings bonds have the option to include the interest in their taxable income as it accrues, or to defer taxation on the interest until the bond is redeemed. The estimated revenue loss from this tax expenditure represents the difference between the tax that would be due on the interest upon accrual and the tax that is paid using the deferral option.

PURPOSE: The exclusion of accrued interest is intended to encourage people to buy U.S. savings bonds. The Congressional Research Service points out that, "The deferral of tax on interest income on savings bonds provides two advantages. First, the payment of tax on the interest is deferred, delivering the equivalent of an interest-free loan of the amount of the tax. Second, the taxpayer often is in a lower income bracket when the bonds are redeemed. This is particularly common when the bonds are purchased while the owner is working and redeemed after the owner retires."[79]

IMPACT: Savings bonds appeal to small savers because the bonds are available in small denominations, are easy to purchase, and serve as a safe investment. In addition, higher-income individuals cannot devote much of their savings to the bonds because of annual purchase limits.[80] "Because poor families save little and do not pay federal income taxes," CRS states, "the tax deferral of interest on savings bonds primarily benefits middle income taxpayers."[81]

CRS adds that, "The savings bond program was established to provide small savers with a convenient and safe debt instrument and to lower the cost of borrowing to the taxpayer. The option to defer taxes on interest increases sales of bonds. But there is no empirical study that has determined whether or not the cost savings from increased bond sales more than offset the loss in tax revenue from the accrual."[82]

[79] U.S. Senate, Committee on the Budget, pp. 963-964.

[80] Annual cash purchases of both EEI and I bonds are limited to $5,000 in electronic bonds and $5,000 in paper bonds for each series (for an aggregate cap of $20,000 in purchases per year).

[81] U.S. Senate, Committee on the Budget, p. 964.

[82] U.S. Senate, Committee on the Budget, p. 964.

Income Tax
Exclusions

28. Allocation of interest expenses attributable to tax-exempt bond interest by financial institutions

Internal Revenue Code Sections:	141, 265(a), 265(b), and 291(e)
Federal Law Sunset Date:	None (but only applies to bonds issued in 2009 and 2010)
Year Enacted in Federal Law:	2009

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$194	$194	$194	$194
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$194**	**$194**	**$194**	**$194**

DESCRIPTION: Banks are allowed to deduct their interest expenses (the interest they pay to depositors) as a cost of doing business, thereby reducing their tax liability. Nevertheless, banks have to reduce their interest deduction if they invest in tax-exempt bonds. Generally, banks and financial institutions are required to reduce their interest deduction by the same percentage that tax-exempt bonds make up of total assets (i.e., if tax-exempt bonds are 10 percent of the bank's portfolio, then the interest deduction must be reduced by 10 percent). The reason for this rule is to prevent banks from claiming two tax preferences for the same investment.

The American Recovery and Reinvestment Act created new, temporary exceptions to the interest deduction offset rules for bonds issued in 2009 and 2010. First, banks and other financial institutions are not required to reduce their interest deduction if tax-exempt bonds account for less than 2 percent of their investment portfolio. Second, banks and financial institutions can now reduce their interest deduction offset to 20 percent of the interest expense allocable to qualified bonds sold by a municipal government that issues less than $30 million in debt per year (a "small issuer").

PURPOSE: According to the Congressional Research Service, the rationale for the expanded interest deduction for banks and financial institutions investing in tax-exempt bonds is "to encourage public investment infrastructure generally and to assist state and local governments issue debt."[83]

IMPACT: CRS states that, "The temporary elimination of the requirement that banks and financial institutions reduce their interest expense deduction for tax-exempt bond holdings will likely increase demand for these bonds and confer some interest cost savings to issuers. The magnitude of the interest cost saving is unclear and the effectiveness of the provision is uncertain. The increased complexity of the tax code, however, would likely reduce the effectiveness and economic efficiency of the provision."[84]

[83] U.S. Senate, Committee on the Budget, p. 596.

[84] U.S. Senate, Committee on the Budget, p. 596.

Income Tax
Exclusions

29. Interest on public-purpose state and local bonds

Internal Revenue Code Sections: 103, 141, and 146
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$4,988	$5,257	$5,274	$5,544
Personal Income Tax Loss	$21,828	$23,003	$23,077	$23,182
Total	**$26,816**	**$28,260**	**$28,351**	**$28,726**

DESCRIPTION: The interest on state or local bonds that are used to build capital facilities that are owned and operated by government entities and serve the general public interest (such as schools, highways, and bridges) are excluded from federal taxable income.

District policymakers eliminated the exclusion of interest on out-of state bonds acquired after December 31, 2012, from the District of Columbia personal income tax. In other words, the District has "decoupled" from the federal exclusion for state and local bond interest, except for bonds issued by the District. Nevertheless, there will still be a tax revenue loss from the excusion of interest on out-of-state bonds purchased before December 31, 2012.

PURPOSE: According to the Congressional Research Service, the exclusion was based on the belief that state and local interest income was constitutionally protected from federal taxation. In 1988, the U.S. Supreme Court ruled in *South Carolina v. Baker* that federal taxation of state and local interest income was not barred by the Constitution, but the exclusion has remained in place. CRS states that, "(M)any believe the exemption for governmental bonds is still justified on economic grounds, principally as a means of encouraging state and local governments to overcome a tendency to underinvest in public capital formation."[85]

IMPACT: State and local governments benefit from the exclusion because it allows them to offer lower interest rates by increasing the effective rate of return enjoyed by the bondholder. In effect, the federal government pays part of the state or local government's interest cost by providing the exclusion.

Purchasers of state and local bonds also benefit from the exclusion, but the distribution of benefits depends on the interest-rate spread between taxable bonds and the tax-exempt municipal bonds, the percentage of the tax-exempt bond issues purchased by individuals of different income levels, and the range of marginal tax rates. Higher-income taxpayers are more likely to benefit because they are more likely to own bonds and can gain a windfall from the interest-rate spread due to their higher marginal tax rates.

The windfall for higher-income taxpayers is illustrated by the following example. Assume that taxable bonds are paying 7 percent interest and that tax-exempt municipal bonds are paying 5 percent. For someone facing a 25 percent marginal tax rate, the effective return on the taxable

[85] U.S. Senate, Committee on the Budget, p. 954.

bond will be 5.25 percent (7 percent minus the .25 tax), a better deal than the tax-exempt rate of 5 percent. For someone facing a 40 percent marginal tax rate, the effective rate on the taxable bond will be 4.2 percent (7 percent minus the .40 tax), making the tax-exempt bond's 5 percent return a better deal. In fact, the 5 percent interest rate exceeds the amount that the higher-income taxpayer would demand (4.2 percent) to buy a tax-exempt bond rather than a taxable bond. Internal Revenue Service data from 2008 show that 73.1 percent of tax-exempt interest income was earned by tax filers with adjusted gross income of more than $100,000.[86]

The windfall also means that tax-exempt bonds are inefficient: the government loses more revenue by subsidizing tax-exempt bonds than it would cost to provide direct grants to subsidize the same amount of borrowing by state and local governments. According to the Congressional Budget Office and the Joint Committee on Taxation, research suggests that only 80 percent of the tax expenditure from tax-exempt bonds actually translates into lower borrowing costs for state and local governments; the other 20 percent represents a "deadweight loss."[87]

The federal subsidy of state and local borrowing for capital investment may generate spillover benefits for nearby states or localities; for example, a modernized wastewater treatment plant may reduce pollution in nearby rivers and lakes. At the same time, some question the subsidy for promoting capital investment at the expense of labor and argue that there is no evidence that any underproduction or underconsumption of public services in the state and local sector is limited to capital. Finally, the subsidizing of state and local bonds decreases federal control of the budget because the revenue loss results from the decisions of state and local officials.[88]

[86] U.S. Senate, Committee on the Budget, p. 953.

[87] Congressional Budget Office and the Joint Committee on Taxation, p. 34.

[88] U.S. Senate, Committee on the Budget, pp. 954-955.

Income Tax
Exclusions

30. Employer contributions for medical care, medical insurance premiums, and long-term care insurance premiums

Internal Revenue Code Sections: 105, 106, and 125
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1918

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$109,363	$125,939	$137,558	$155,303
Total	**$109,363**	**$125,939**	**$137,558**	**$155,303**

DESCRIPTION: Employer payments for health insurance, other employee medical expenses, and long-term care insurance are not included in the employee's personal taxable income. The exclusion also applies to flexible spending accounts (FSAs), which allow employees to choose a benefit amount at the start of a year and to use the account to pay for medical expenses not covered by employer-provided health insurance. FSAs are funded through wage and salary reductions, or through employer contributions, both of which are exempt from federal income tax.

The exclusion applies to health benefits provided to the employee's family members. Federal law requires that the imputed value of health and other fringe benefits extended to same-sex spouses and domestic partners be included in adjusted gross income (in other words, same-sex spouses and domestic partners are not recognized as family members under federal law).

Although eliminating or capping the exclusion was discussed during the debate over the Patient Protection and Affordable Care Act of 2010 (P.L. 111-147), policymakers decided instead to impose an excise tax of 40 percent on high-cost health insurance plans.

PURPOSE: The exclusion of employer-provided health insurance from taxable income is part of a longstanding policy of excluding fringe benefits from taxation. The exclusion subsidizes the provision of health care to employees through employer-provided group health insurance.

IMPACT: The Congressional Research Service states that, "The tax exclusion for employer contributions to employee health plans benefits only those taxpayers who participate in employer-sponsored plans. Beneficiaries include current employees as well as retirees. In 2009, 58.5 pecent of the U.S. population received health insurance coverage through employers."[89] CRS adds that, "Although the tax exclusion benefits a majority of working Americans, it provides greater benefits to higher-income taxpayers than to lower-income ones. Highly paid employees tend to receive more generous employer-paid health insurance coverage than their lowly paid counterparts. And highly paid employees fall in higher tax brackets" that increase the value of the exclusion.[90]

[89] U.S. Senate, Committee on the Budget, p. 818.

[90] U.S. Senate, Committee on the Budget, p. 818.

Those who are least likely to receive employer-provided health insurance include workers under age 25, workers in firms with fewer than 25 employees, part-time workers, low-wage workers, and workers in the construction, business and personal service, entertainment, and wholesale and retail trade industries.[91]

Experts also points out that the health care exclusion imposes significant efficiency costs on society. Because of the subsidy, employees have an incentive to seek compensation in the form of non-taxable health benefits rather than in taxable wages. As a result, employees may consume more health insurance than they need. As stated by CRS, "Most health economists think the unlimited exclusion for employer-provided health insurance has distorted the markets for both health insurance and health care. Generous health plans encourage subscribers to use health services that are not cost-effective, putting upward pressure on health care costs."[92]

At the same time, CRS points out that, "The exclusion does have some social benefits. Owing to the pooling of risk that employment-based group health insurance provides, one can argue that the exclusion makes it possible for many employees to purchase health insurance plans that simply would not be available on the same terms or at the same cost in the individual market."[93]

[91] U.S. Senate, Committee on the Budget, p. 818.

[92] U.S. Senate, Committee on the Budget, p. 820.

[93] U.S. Senate, Committee on the Budget, p. 820.

Income Tax
Exclusions

31. Interest on state and local private-activity bonds issued to finance non-profit hospital construction

Internal Revenue Code Sections: 103, 141, 145(b), 145(c), 146, and 501(c)(3).
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$389	$454	$454	$491
Personal Income Tax Loss	$1,772	$1,882	$1,993	$2,118
Total	**$2,161**	**$2,336**	**$2,447**	**$2,609**

DESCRIPTION: Interest income on state and local bonds used to finance the construction of non-profit hospitals and nursing homes is tax-exempt. These bonds are classified as private-activity bonds, rather than governmental bonds, because a substantial portion of the benefits accrues to individuals or private organizations instead of the general public. Non-profit hospital bonds are not subject to state volume caps on private-activity bonds.

PURPOSE: The purpose of the bonds is to provide low-cost financing of hospitals and nursing homes owned by non-profit organizations. Investors purchase the bonds at low interest rates because the income from them is tax-free.

IMPACT: Private, non-profit hospitals and the communities they serve benefit from this provision. According to the Congressional Budget Office and the Joint Committee on Taxation, hospital and other health-care facilities accounted for a majority (53 percent) of state and local private-activity bond financing from 1991 to 2007.[94] State and local private-activity bonds are particularly important in the health care sector because the private sector provides almost all (more than 90 percent) of the total investment in hospitals and other health-care facilities.[95]

The Congressional Research Service observes that, "Questions have … been raised about whether nonprofit hospitals fulfill their charitable purpose and if they deserve continued access to tax-exempt bond finance. Even if a case can be made for this federal subsidy for nonprofit organizations, it is important to recognize the potential costs. As one of many categories of tax-exempt private-activity bonds, bonds for nonprofit organizations increase the financing cost of bonds issued for other public capital. With a greater supply of public bonds, the interest rate on the bonds necessarily increases to lure investors. In addition, expanding the availability of tax-exempt bonds increases the assets available to individuals and corporations to shelter their income from taxation."[96]

[94] Congressional Budget Office and Joint Committee on Taxation, p. 19.

[95] Congressional Budget Office and Joint Committee on Taxation, pp. 2-3.

[96] U.S. Senate, Committee on the Budget, pp. 782-783.

Income Tax
Exclusions

32. Medical care and TriCare medical insurance for military dependents, retirees, retiree dependents, and veterans

Internal Revenue Code Sections:	112 and 134
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$2,376	$2,587	$2,746	$2,960
Total	**$2,376**	**$2,587**	**$2,746**	**$2,960**

DESCRIPTION: Active-duty military personnel receive a variety of benefits, such as medical and dental care, that are excluded from taxation. In addition, the following groups are also eligibile for medical and dental care benefits without being subject to taxation: dependents of active-duty personnel; retired military personnel and their dependents; veterans; survivors of deceased veterans; and reservists who have served on active duty since September 11, 2001, and joined the Selected Reserve.

Military dependents and reitrees are allowed to receive medical care in military facilities and from military doctors, if there is sufficient spare capacity. These individuals can also be treated by civilian health-care providers working under contract with the Department of Defense through the TriCare program. TriCare provides medical care through a health maintenance organization, a preferred provider organization, or a fee-for-service option.

PURPOSE: The Congressional Research Service notes that this exclusion has evolved over time through a series of legislative, administrative, and legal actions. Thus, the rationale has not been clearcut. CRS further points out that, "Even if there was no specific statutory exclusion for the health benefits received by military personnel and their dependents, a case for excluding them could be made on the basis of sections 105 and 106 of the Internal Revenue Code. These sections exclude from the taxable income of employees any employer-provided health benefits they receive."[97]

IMPACT: Higher-income individuals gain a disproprortionate share of the benefits of the exclusion because they face higher marginal tax rates that increase the savings from each dollar excluded. Although the tax exclusion of health benefits may create inefficiencies by encouraging individuals to purchase more health care than they would if they bore the full cost, direct care provided in military facilities may be difficult to value for tax purposes. In addition, the exclusion of medical care for service members' dependents and military retirees might hamper military recruitment and retention.[98]

[97] U.S. Senate, Committee on the Budget, p. 827.

[98] U.S. Senate, Committee on the Budget, p. 827.

Income Tax
Exclusions

33. Medicare Part A – hospital insurance benefits

Internal Revenue Code Section:	None (Exclusion was authorized by IRS Revenue Ruling 70-341)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1970

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$19,644	$20,684	$21,833	$23,056
Total	**$19,644**	**$20,684**	**$21,833**	**$23,056**

DESCRIPTION: Part A of Medicare pays most of the cost of in-patient hospital care and as much as 100 days per year of skilled nursing facility care, home health care, and hospice care for individuals who are 65 or older, or who are disabled. Part A is financed primarily by a 2.9 percent payroll tax levied on the earnings of current workers, which is split evenly between the employer and the employee. The expected lifetime value of Part A benefits under current law exceeds the amount of payroll tax contributions by current beneficiaries. This difference, when mutliplied by an individual's marginal tax rate, represents a tax expenditure. The employer's share of the payroll tax is also excluded from an employee's taxable income.

PURPOSE: This exclusion has never been established by statute; rather, it was adopted by an Internal Revenue Service ruling in 1970. The rationale for the ruling was that, "(T)he benefits under Part A of Medicare may be excluded from gross income because they are in the nature of disbursements intended to achieve the social welfare objectives of the federal government. The ruling also stated that Medicare Part A benefits had the same legal status as monthly Social Security payments to an individual"[99] (which were not subject to federal income tax at the time).

IMPACT: The Congressional Research Service states that, "In effect, the tax subsidy for Part A benefits lowers the after-tax cost to the elderly for those benefits. As a result, it has the potential to divert more resources to the delivery of medical care through hospitals than might otherwise be the case."[100] Nevertheless, CRS adds that, "Those who favor curtailing this subsidy, as a means of increasing federal revenue or reducing use of hospital care, would find it difficult to do so in an equitable manner for two reasons. First, Medicare benefits receive the same tax treatment as most other health insurance benefits: they are untaxed. Second, taxing the value of the health care benefits actually received by an individual would have the largest impact on people who suffer health problems that are costly to treat: many of these individuals are elderly and living on relatively small fixed incomes."[101]

Moreover, the dynamics of this tax subsidy will change in the future. The amount by which Medicare Part A benefits exceed payroll tax contributions will decrease for future retirees

[99] U.S. Senate, Committee on the Budget, p. 846.

[100] U.S. Senate, Committee on the Budget, p. 846.

[101] U.S. Senate, Committee on the Budget, pp. 846-847.

because the contribution period will cover more of their work years (early beneficiaries after Medicare was established in 1965 contributed for very little of their working lives). "In addition," CRS states, "the absence of a cap on worker earnings subject to the Medicare (Part A) payroll tax means that today's high-wage earners will contribute more during their working years and consequently receive a smaller (and possibly negative) subsidy once they begin to receive Medicare Part A benefits."[102]

[102] U.S. Senate, Committee on the Budget, p. 847.

Income Tax
Exclusions

34. Medicare Part B – supplementary medical benefits

Internal Revenue Code Section:	None (Exclusion was authorized by IRS Revenue Ruling 70-341)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1970

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$13,352	$14,884	$15,869	$17,360
Total	**$13,352**	**$14,884**	**$15,869**	**$17,360**

DESCRIPTION: Part B of Medicare covers certain physician services, outpatient services, and durable medical equipment for people who are over the age of 65 or who are disabled. Participation in the program is voluntary, unlike Medicare Part A. Premiums cover 25 percent of the cost of Medicare Part B, and regular appropriations cover the other 75 percent. The portion of the program's costs paid by general government revenue is not included in the personal taxable income of recipients and therefore represents a tax expenditure equal to the marginal tax rate of enrollees multiplied by the amount of the exclusion.

PURPOSE: The exclusion has never been established by statute; instead, it was authorized by an Internal Revenue Service ruling in 1970. The IRS determined that Part B benefits (whether funded by premiums or general appropriations) could be excluded from taxable income because they have the same status under the tax code as benefits received through other accident and health insurance.[103] According to the Congressional Research Service, "This treatment is supported by the same rationale used by the IRS to justify the exclusion of Medicare Part A benefits from the gross income of beneficiaries."[104]

IMPACT: CRS states that, "The tax subsidy for Part B reduces the after-tax cost of medical insurance for retirees. One consequence of this reduction is that enrollees are likely to consume more health care than needed to maintain good health. As the subsidy is not means-tested, upper-income Medicare beneficiaries gain more benefit from it than lower-income beneficiaries"[105] because upper-income individuals face higher marginal tax rates. CRS further points out that, "There appear to be no significant administrative barriers" to adding the value of the subsidy to taxable income because, "The value of the subsidy could easily be estimated, assigned to beneficiaries, and reported as income on their tax returns. A drawback to such a proposal is that it would impose an added tax burden on older individuals of moderate or meager means who have little flexibility in their budgets to absorb higher taxes."[106]

[103] U.S. Senate, Committee on the Budget, p. 850.

[104] U.S. Senate, Committee on the Budget, p. 850.

[105] U.S. Senate, Committee on the Budget, p. 851.

[106] U.S. Senate, Committee on the Budget, p. 851.

Income Tax
Exclusions

35. Medicare Part D – prescription drug benefits

Internal Revenue Code Section:	None (Exclusion was authorized by IRS Revenue Ruling 70-341)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	2003

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,666	$4,213	$4,761	$5,470
Total	**$3,666**	**$4,213**	**$4,761**	**$5,470**

DESCRIPTION: Part D of the Medicare program subsidizes the cost of prescription drugs for individuals eligible for Medicare. Participation in Part D is voluntary, except for individuals who are eligible both for Medicare and Medicaid, and certain other low-income Medicare beneficiaries. Part D benefits are offered through stand-alone private prescription drug programs as well as “Medicare Advantage” plans, such as health maintenance organizations, that provide all Medicare benefits including prescription drugs. Part D programs offer either a defined standard benefit or an alternative benefit that is actuarially equivalent; they may also offer enhanced benefits. Enrollees pay monthly premiums that vary among plans and regions.

During 2009, premiums accounted for 10 percent of program income; state transfers accounted for 13 percent; and regular federal appropriations provided the remaining 77 percent. The benefits provided by federal appropriations and state governments are excluded from the taxable income of enrollees, creating a tax expenditure equal to the subsidy (the difference between the value of the benefits received and the premiums that enrollees pay) multiplied by the marginal tax rates faced by enrollees.

PURPOSE: The purpose of the exclusion is to reduce the after-tax cost to enrollees of using prescription drugs and thereby expand access to such drugs among the elderly. Although the exclusion of Medicare benefits from taxable income has never been established by statute, it has been implemented through a regulatory rulings issued by the Internal Revenue Service in 1970. When Part D was created by the “Medicare Prescription Drug, Improvement, and Modernization Act of 2003” (P.L. 108-173), the same exclusion was therefore applicable.

IMPACT: Elderly individuals enrolled in Medicare Part D benefit from this provision. The Congressional Research Service points out that, “For a given subsidy amount, the tax savings from the exclusion are greater for enrollees in the highest tax bracket than for enrollees in the lowest tax bracket.”[107]

[107] U.S. Senate, Committee on the Budget, p. 855.

Income Tax
Exclusions

36. Subsidy payments to employers maintaining prescription drug benefits for retirees eligible for Medicare

U.S. Code Section	42 USC 1395w-132
Federal Law Sunset Date:	December 31, 2012
Year Enacted in Federal Law:	2003

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$324	$194	sunset	sunset
Personal Income Tax Loss	$0	$0	sunset	sunset
Total	**$324**	**$194**	**sunset**	**sunset**

DESCRIPTION: Medicare Part D offers a voluntary outpatient prescription drug benefit. Participants have the choice of purchasing plans offering standard drug coverage or alternative coverage with actuarially equivalent benefits. Coverage is provided by private presciption plans or through comprehensive Medicare plans that also offer hospital and physician benefits and are known as "Medicare Advantage" (see tax expenditure #35, "Medicare Part D – prescription drug benefits").

Under Part D, one option for employers and unions providing presciption drug benefits to their retirees is to receive federal subsidies for continuing the coverage, which must be actuarially equivalent to the standard drug coverage offered by Part D. In 2010 and 2011, the subsidy payments equaled 28 percent of a qualified retiree's allowable presciption drug costs between $310 and $6,300, for a maximum subsidy of $1,764. The lower and upper dollar limits are indexed to annual growth in per-capita spending on prescription drugs by Medicare beneficiaries.

Employers who choose to receive the subsidies are allowed to exclude them from taxable income. In addition, an employer may disregard any subsidy it receives in calculating its deduction for health benefits for current employees and retirees. Beginning in tax year 2013, employers will no longer be able to disregard the subsidy when calculating their deduction for health benefits provided, which will have the effect of taxing the subsidy at the employer's marginal tax rate.

PURPOSE: According to the Congressional Research Service, "The subsidy payments and their preferential tax treatment were mainly intended to keep large numbers of employers and unions from dropping coverage of prescription drugs from their health benefits for Medicare-eligible retirees. Such a step would leave many of them with the choices of enrolling in the Medicare outpatient drug program or having no coverage for outpatient prescription drugs."[108]

IMPACT: The exclusion benefits employers and unions who provide prescription drug benefits to retirees, and also helps retirees by encouraging employers and unions to conntinue the drug coverage. According to CRS, "Large, financially strong employers have long been much more likely than small or medium employers to provide health benefits to retirees."[109] CRS adds that,

[108] U.S. Senate, Committee on the Budget, pp. 861-862.

[109] U.S. Senate, Committee on the Budget, p. 863.

"There is evidence that the typical drug benefit available to retirees through employer health plans is more generous than the standard drug benefit available under Part D. Therefore, a substantial decrease in the number of employers claiming the subsidy in the next few years could adversely affect (retirees') welfare,"[110] which is a likely prospect once the subsidy becomes taxable in 2013.

The subsidy may also benefit the general public, because the estimated cost of the subsidy per retiree ($665) is much less than the estimated federal subsidy ($1,209) for all retirees enrolled in Medicare Part D.[111]

[110] U.S. Senate, Committee on the Budget, p. 863.

[111] U.S. Senate, Committee on the Budget, p. 864.

Income Tax
Exclusions

37. Capital gain on sale of principal residence

Internal Revenue Code Section: 121
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1997

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$17,920	$18,637	$19,456	$20,293
Total	**$17,920**	**$18,637**	**$19,456**	**$20,293**

DESCRIPTION: Homeowners may exclude from personal taxable income up to $250,000 (single taxpayers) or $500,000 (married taxpayers filing joint returns) of capital gains realized on the sale of their principal residence. To qualify, the taxpayer must have owned and occupied the home for at least two of the previous five years. The exclusion applies only to the portion of the property associated with the residence, not to portions of the property used in business activity. The exclusion cannot be used more than once every two years.

PURPOSE: Capital gains arising from the sale of an individual's principal residence have long received preferential tax treatment, as part of an effort to promote homeownership by reducing its after-tax cost. Previously, homeowners were allowed to defer the tax on capital gains from the sale of their principal residence if the proceeds of the sale were used to buy another home of equal or greater value. In addition, homeowners aged 55 and older were allowed a one-time exclusion of a gain up to $125,000 from the sale of their principal residence.

In 1997, Congress modified these provisions to reduce their complexity, creating the current rules that allow all taxpayers to exclude $250,000 (single) or $500,000 (married filing jointly) of capital gains from the sale of their principal residence.

IMPACT: The Congressional Research Service states that, "Excluding the capital gains on the sale of principal residences from tax primarily benefits middle- and upper-income taxpayers. At the same time, however, this provision avoids putting an additional tax burden on taxpayers, regardless of their income levels, who have to sell their homes because of changes in family status, employment, or health. It also provides tax benefits to elderly taxpayers who sell their homes and move to less expensive housing during their retirement years."[112]

With regard to the efficiency impact of the exclusion, CRS states that it "gives homeownership a competitive advantage over other types of investments, since the capital gains from investments in other assets are generally taxed when the assets are sold. Moreover, when combined with other provisions in the tax code such as the deductibility of home mortgage interest, homeownership is an especially attractive investment. As a result, savings are diverted out of other forms of investment and into housing."[113]

[112] U.S. Senate, Committee on the Budget, p. 357-358.

[113] U.S. Senate, Committee on the Budget, p. 359.

Income Tax
Exclusions

38. Income from discharge of principal residence acquisition indebtedness

Internal Revenue Code Sections: 108
Federal Law Sunset Date: December 31, 2012
Year Enacted in Federal Law: 2007

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	sunset	sunset
Personal Income Tax Loss	$467	too small	sunset	sunset
Total	**$467**	**too small**	**sunset**	**sunset**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Mortgage debt cancellation occurs when lenders (1) restructure loans, thereby reducing principal balances, or (2) sell properties, either in advance or as a result of foreclosure proceedings. Historically, if a lender forgives or cancels such debt, tax law has treated the canceled debt as taxable income.

An exception to this rule permits the exclusion of discharged qualified residential debt from gross income. Qualified indebtedness is defined as debt, limited to $2 million ($1 million if married filing separately), incurred in acquiring, constructing, or substantially improving the taxpayer's principal residence. The taxpayer is required to reduce the basis in the principal residence by the amount of the excluded income. This provision applies to discharges made on or after January 1, 2007, and before January 1, 2013. The exclusion is not permitted if the discharge was due to services performed for the lender or any other factor not directly related to a decline in the residence's value or to the taxpayer's financial condition.

PURPOSE: The purpose of the exclusion is to minimize hardship for households in distress. Policymakers have expressed concern that individuals who are experiencing hardship and are in danger of losing their home, presumably as a result of financial distress, should not incur an additional hardship by being taxed on canceled debt income.

IMPACT: Taxpayers who have had debt canceled benefit from this provision. The Congressional Research Service notes that, "The benefits … will be concentrated among middle- and higher-income taxpayers, as these households have likely incurred the largest residential debt and are subject to higher marginal tax rates. To a lesser extent, the benefits also extend to lower-income new homeowners who are in distress as a result of interest rate resets and the slowdown in general economic activity. The residential debt of lower-income households, however, is relatively small, thus limiting the overall benefit accruing to these taxpayers."[114]

Another concern about the provision is that it could encourage homeowners to be less responsible about meeting their debt obligations.

[114] U.S. Senate, Committee on the Budget, p. 402.

Income Tax
Exclusions

39. Interest on state and local private-activity bonds issued to finance housing

Internal Revenue Code Sections: 103, 141, 142, 143, and 146.
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1980

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$389	$454	$454	$491
Personal Income Tax Loss	$1,661	$1,772	$1,882	$2,008
Total	**$2,050**	**$2,226**	**$2,336**	**$2,499**

DESCRIPTION: Each state receives a certain amount of authority to issue tax-exempt private activity bonds, which are securities issued by a state or local government to finance qualified projects by a private user. Qualified projects, which include owner-occupied housing (mortgage revenue bonds, or MRBs), rental housing, and veterans' housing for low and moderate-income families, are expected to have a public benefit. Housing construction must compete with other authorized private activities for bond issuances that are available under a state's volume cap.

PURPOSE: The purpose of the bonds is to finance low-interest mortgages for low- and moderate-income homebuyers, as well as the acquisition, construction, and rehabilitation of multi-family housing for low-income renters. Investors purchase the housing bonds at low interest rates because the income is tax-free. The interest savings made possible by the exclusion should allow issuers to offer housing for sale or rent at a lower cost.

IMPACT: With regard to owner-occupied housing, the Congressional Research Service notes that, "Income, tenure status, and house-price-targeting provisions imposed on MRBs make them more likely to achieve the goal of increased homeownership than many other housing tax subsidies that make no targeting effort, such as is the case for the mortgage-interest deduction. Nonetheless, it has been suggested that most of the mortgage revenue bond subsidy goes to families that would have been homeowners even if the subsidy were not available."[115] Regarding rental housing, CRS states that the bonds promote "equitable treatment for families unable to take advantage of the substantial tax incentives available to those able to invest in owner-occupied housing."[116]

More generally, the private-activity bonds impose costs because they "increase the financing cost of bonds issued for other public capital. With a greater supply of public bonds, the interest rate on the bonds necessarily increases to lure investors. In addition, expanding the availability of

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[115] U.S. Senate, Committee on the Budget, p. 364.

[116] U.S. Senate, Committee on the Budget, p. 369.

tax-exempt bonds increases the assets available to individuals and corporations to shelter their income from taxation."[117]

[117] U.S. Senate, Committee on the Budget, p. 369.

Income Tax
Exclusions

40. Compensatory damages for physical injury or sickness

Internal Revenue Code Section: 104(a)(2) - 104(a)(5)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1918

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$1,495	$1,495	$1,495	$1,495
Total	**$1,495**	**$1,495**	**$1,495**	**$1,495**

DESCRIPTION: Damages paid through a court award or a settlement to compensate for physical injury or illness are excluded from the recipient's taxable income. The exclusion applies both to lump-sum payments and periodic payments, but does not apply to punitive damages except in certain states where only punitive damage awards are allowed. In addition, the exclusion does not apply to compensation for discrimination or emotional distress.

PURPOSE: According to the Congressional Research Service, the exclusion "is based on the reasoning that these payments are compensating for a loss."[118] Noting that the interest component of periodic payments would normally be taxable, CRS adds that, "An argument for the full exclusion of periodic payments was to avoid circumstances where individuals used up their lump-sum payments and might then require public assistance."[119]

IMPACT: CRS states that, "The exclusion benefits individuals who receive cash compensation for injuries and illness. It parallels the treatment of workers' compensation which covers on-the-job injuries. It especially benefits higher-income individuals whose payments would typically be larger, reflecting larger lifetime earnings, and subject to higher tax rates. By restricting tax benefits to compensatory rather than punitive damages, the provision encourages plaintiffs to settle out of court so that the damages can be characterized as compensatory."[120]

[118] U.S. Senate, Committee on the Budget, p. 876.

[119] U.S. Senate, Committee on the Budget, p. 876.

[120] U.S. Senate, Committee on the Budget, pp. 876-877.

Income Tax
Exclusions

41. Disaster mitigation payments

Internal Revenue Code Section: 139
Federal Law Sunset Date: None
Year Enacted in Federal Law: 2005

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	too small	too small	too small	too small
Total	**too small**	**too small**	**too small**	**too small**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Disaster mitigation payments under the Robert T. Stafford Disaster Relief and Emergency Assistance Act or the National Flood Insurance Act are excluded from taxable income. Disaster mitigation grants cover a variety of expenditures such as securing items to reduce potential damage from earthquakes, putting houses on stilts to reduce flood damage, and securing roofs and windows from wind damage.

PURPOSE: According to the Congressional Research Service, the Internal Revenue Service ruled in 2004 that disaster mitigation payments would be taxable, in the absence of a specific exemption in the law. Previously, individuals had not paid taxes on the payments. Congress responded by establishing an explicit statutory exclusion of the payments. CRS states that, "The tax legislation was in response to that ruling and reflected the general view that individuals and businesses should not be discouraged from mitigation activities due to tax treatment of these payments."[121]

IMPACT: CRS observes that, "The tax exemption is most beneficial for higher-income individuals who have higher marginal tax rates. However, even individuals with relatively low incomes could be subject to tax since the mitigation payments can be large when used for major construction projects (such as putting houses in flood plains on stilts). These individuals might not have enough income to pay taxes on these grants and taxation might cause them not to participate in the program."[122]

The fairness and efficiency issues surrounding the exclusion are complex. CRS states that, "An argument can be made that individuals should be responsible for undertaking their own measures to reduce disaster costs since those expenditures would benefit them …Disaster mitigation expenditures for individuals and businesses can also have benefits that spill over to the community at large, and an individual would not take these benefits into account when making an investment decision."[123]

[121] U.S. Senate, Committee on the Budget, p. 868.

[122] U.S. Senate, Committee on the Budget, pp. 867-868.

[123] U.S. Senate, Committee on the Budget, p. 868.

Income Tax
Exclusions

42. Employer contributions for premiums on accident and disability insurance

Internal Revenue Code Sections: 105 and 106
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,076	$3,161	$3,247	$3,338
Total	**$3,076**	**$3,161**	**$3,247**	**$3,338**

DESCRIPTION: Employer payments for employee accident and disability insurance premiums are not included in an individual's personal taxable income.

PURPOSE: According to the Congressional Research Service, in 1954 Congress exempted accident and health benefits from taxation "in an attempt to equalize the tax treatment of benefits through an insurance plan and benefits provided in other ways."[124] This action reversed a 1943 Internal Revenue Service ruling that employer payments to employees due to injury or sickness were subject to taxation.

IMPACT: CRS points out that due to the exclusion, "(T)he employer's cost is less than he would have to pay in wages that are taxable, to confer the same benefit on the employee because the value of this insurance coverage is not taxed. Employers are thus encouraged to buy such insurance for employees."[125] Nevertheless, CRS adds that, "Since public programs (Social Security and workman's compensation) provide a minimum level of disability payments, the justification for providing a subsidy for additional benefits is unclear." [126]

The exclusion may impair both horizontal and vertical equity. In arguing for repeal of the exclusion, President Bush's Advisory Panel on Federal Tax Reform stated that, "Employees who have these employer-provided fringe benefits receive better tax treatment than employees who pay for these expenses out of pocket. Among workers for whom the benefit is available, more of the benefits go to high-income taxpayers, even though they are paid for with higher tax rates for everyone."[127]

[124] U.S. Senate, Committee on the Budget, p. 928.

[125] U.S. Senate, Committee on the Budget, p. 927.

[126] U.S. Senate, Committee on the Budget, p. 928.

[127] The President's Advisory Panel on Federal Tax Reform, p. 85.

Income Tax
Exclusions

43. Employer contributions for premiums on group-term life insurance

Internal Revenue Code Section: 79
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1920

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$1,452	$1,538	$1,623	$1,719
Total	**$1,452**	**$1,538**	**$1,623**	**$1,719**

DESCRIPTION: Employer payments for employee life insurance (up to $50,000 in coverage) and death benefits are not included in an individual's taxable income. In order to qualify for the exclusion, the insurance plan must meet certain requirements including non-discrimination provisions intended to ensure that benefits are spread widely and equitably among employees.

PURPOSE: The exclusion was originally authorized, without any limitation on the amount of coverage, by a legal opinion issued in 1920. The $50,000 limit on the amount that can be excluded was enacted in 1964, based on the view that it "would encourage the purchase of group life insurance and assist in keeping the family unit intact upon death of the breadwinner."[128]

IMPACT: The Congressional Research Service states that, "Encouraging individuals to purchase more life insurance may be justified by concerns that many individuals would fail to buy prudent amounts of life insurance on their own, which could expose surviving family members to financial vulnerabilities. Subsidizing life insurance coverage may help provide a minimum standard of living for surviving dependent individuals."[129] Employers may also benefit from the exclusion, because it allows them to provide this form of compensation at a lower cost than the wages employees would need to buy the same amount of insurance on their own.

Nevertheless, there is uneven access to the benefit, giving rise to horizontal and vertical equity concerns. CRS observes that, "Aside from administrative convenience, the rationale for providing insurance subsidies to employees, but not to the self-employed or those who are not employed, is not obvious. As with many other fringe benefits, higher-income individuals probably receive more benefits from this exclusion because they are more likely to receive group life insurance benefits from their employers. Lower-income individuals, whose surviving dependents are probably more financially vulnerable, probably benefit less from this exclusion."[130] President Bush's Advisory Panel on Federal Tax Reform called for repeal of the exclusion based on similar reasoning.[131]

[128] U.S. Senate, Committee on the Budget, p. 924.

[129] U.S. Senate, Committee on the Budget, p. 925.

[130] U.S. Senate, Committee on the Budget, p. 925.

[131] The President's Advisory Panel on Federal Tax Reform, p. 85.

Income Tax
Exclusions

44. Employer pension contributions and earnings plans

Internal Revenue Code Sections: 401-407, 410-418e, and 457
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$90,652	$106,715	$105,006	$113,301
Total	**$90,652**	**$106,715**	**$105,006**	**$113,301**

DESCRIPTION: Employer contributions to qualified pension, profit-sharing, stock-bonus, and annuity plans are not included in the employee's personal taxable income in the year of contribution. Earnings on these contributions are also tax-free. Withdrawals are included in taxable income.

There are two major types of pension plans: (1) defined-benefit plans, which guaranteee employees a certain benefit level on retirement, and (2) defined-contribution plans, which provide a pension that depends on the employee's contributions and the earnings on those contributions. The estimated revenue impact of this tax expenditure is the revenue that the government does not collect on pension contributions and earnings, offset by the taxes paid on pension withdrawals.

PURPOSE: The purpose of the exclusion is to promote saving for retirement, although the actual effects are unclear. The Congressional Research Service observes that, "Since individuals cannot directly control their contributions to plans in many cases (defined-benefit plans), or are subject to a ceiling, the tax incentives to save may not be very powerful … At the same time, pension plans may force saving and retirement income on employees who otherwise would have total savings less than their pension-plan savings."[132]

IMPACT: CRS states that, "The employees who benefit from this provision consist of taxpayers whose employment is covered by a plan and whose service has been sufficiently continuous for them to qualify for benefits in a company or union-administered plan."[133] Nevertheless, CRS points out that the benefits are likely to accrue disproportionately to high-income households because employees with higher salaries are more likely to receive pension benefits, and the dollar contributions made on behalf of higher-income employees are larger. In addition, higher-income taxpayers derive a larger benefit because their marginal tax rate is higher, increasing the value of the exclusion. Workers are also more likely to be covered by pensions if they work in certain industries, if they are employed by large firms, or if they are unionized.[134]

[132] U.S. Senate, Committee on the Budget, p. 907.

[133] U.S. Senate, Committee on the Budget, p. 904.

[134] U.S. Senate, Committee on the Budget, pp. 904-905.

Income Tax
Exclusions

45. Income of trusts to finance supplemental unemployment benefits

Internal Revenue Code Section: 501(17)(A)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1960

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$34	$43	$51	$60
Total	**$34**	**$43**	**$51**	**$60**

DESCRIPTION: The investment income from a supplemental unemployment benefit trust may be exempt from taxation if it is established by an employer, employees, or both, solely to provide supplemental unemployment compensation when an involuntary loss of employment arises from a reduction in force, discontinuation of a plant or operation, temporary layoff, or other similar circumstance.

The trust must be set forth in a written plan that ensures it does not discriminate in favor of officers, shareholders, supervisors, or highly compensated employees. Benefits must be determined according to objective standards.

Supplemental unemployment trusts were first established in the auto industry in 1955. If an employee leaves a company voluntarily or is discharged for misconduct, he or she is not eligible for a benefit; the employee has no vested interest in the amounts paid into the fund on his or her behalf.

PURPOSE: The purpose of the exclusion is to encourage the creation of supplemental unemployment benefit trusts and to increase income support for laid-off workers.

IMPACT: Employers who sponsor a supplemental unemployment benefit trust and the employees who participate in the plans benefit from this provision.

Income Tax
Exclusions

46. Investment income on life insurance and annuity contracts

Internal Revenue Code Sections: 72, 101, 7702, 7702A
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$1,685	$1,685	$1,750	$1,783
Personal Income Tax Loss	$26,931	$27,648	$28,365	$29,131
Total	**$28,616**	**$29,333**	**$30,115**	**$30,914**

DESCRIPTION: The investment income on life insurance contracts, commonly known as "inside build-up," is typically not included in personal or corporate taxable income as it accrues, or when it is received by beneficiaries upon the death of the insured individual. Moreover, amounts paid as dividends or withdrawn as cash are taxed only when they exceed total premiums paid for the policy, thus allowing tax-free investment income to pay part of the cost of the insurance protection. The investment income that accumulates as part of an annuity policy is also free from taxation, but annuities are taxed on their investment component when paid.

Life insurance policies must follow rules designed to limit the tax-free accumulation of income. If investment income grows faster than is needed to fund the promised benefits, that income will be attributed to the owner of the policy and is subject to current taxation.

PURPOSE: The non-taxable status of life insurance inside build-up, the exclusion of death benefits, and the tax deferral on annuity investment income all date back to the creation of the federal income tax in 1913. The Congressional Research Service suggests that Congress may have decided to exclude death benefits "because they were believed to be comparable to bequests, which also were excluded from the tax base."[135] CRS also notes that the other exclusions "were, in part, based on the general tax principle of constructive receipt. Policyholders, in this view, did not own the interest income because to receive that interest income they would have to give up the insurance protection or the annuity guarantees."[136]

IMPACT: CRS states that, "These provisions … offer preferential treatment for the purchase of life insurance coverage and for savings held in life insurance policies and annuity contracts. Middle-income taxpayers, who make up the bulk of the life insurance market, may reap most of this provision's benefits. Many higher-income taxpayers, once their life insurance requirements are satisfied, generally obtain better after-tax yields from tax-exempt state and local obligations or tax-deferred capital gains."[137]

[135] U.S. Senate, Committee on the Budget, p. 306.

[136] U.S. Senate, Committee on the Budget, p. 307.

[137] U.S. Senate, Committee on the Budget, p. 306.

CRS also points out that the exclusion may create efficiency costs for society because, "This exemption of inside build-up distorts investors' decisions by encouraging them to choose life insurance over competing savings vehicles such as bank accounts, mutual funds, or bonds. The result could be overinvestment in life insurance and excessive levels of life insurance protection relative to what would occur if life insurance products competed on a level playing field with other investment opportunities."[138] Although the exclusion may counteract some families' tendency to underinvest in life insurance, CRS questions whether it "induces families to buy prudent levels of life insurance,"[139] and whether other initiatives, such as better financial education, might prove more effective.

President Bush's Advisory Panel on Federal Tax Reform recommended repealing this exclusion (as well as several other exclusions for fringe benefits) because, "The favorable tax treatment of fringe benefits results in an uneven distribution of the tax burden as workers who receive the same amount of total compensation pay different amounts of tax depending on the mix of cash wages and fringe benefits."[140]

[138] U.S. Senate, Committee on the Budget, p. 307.

[139] U.S. Senate, Committee on the Budget, p. 308.

[140] President's Advisory Panel on Federal Tax Reform, p. 85.

Income Tax
Exclusions

47. Public assistance cash benefits

Internal Revenue Code Section:	N.A. (this exclusion was established through a series of IRS rulings dating back to 1933)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	N.A. (this exclusion was established through a series of IRS rulings dating back to 1933)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$4,604	$5,127	$5,232	$5,588
Total	**$4,604**	**$5,127**	**$5,232**	**$5,588**

DESCRIPTION: Public assistance benefits in the form of cash payments or in-kind benefits (goods or services), whether provided free or partly subsidized, are not included in the personal taxable income of the recipient. Examples include cash benefits provided by the Temporary Assistance to Needy Families and the Supplemental Security Income program for the aged, blind, and disabled, and in-kind benefits provided by Medicaid and the Supplemental Nutrition Assistance Program (Food Stamps).

Nevertheless, the estimates shown above reflect only the forgone revenue from public assistance cash benefits because it is difficult to determine the value of in-kind benefits to recipients.

PURPOSE: The exclusion of public assistance benefits from taxable income is not specifically authorized by law; instead, the exclusion has been established by a series of Internal Revenue Service rulings. The Congressional Research Service states that, "Revenue rulings generally exclude government transfer payments from income because they have been considered to have the nature of 'gifts' in aid of the general welfare. While no specific rationale has been advanced for this exclusion, the reasoning may be that Congress did not intend to tax with one hand what it gives with the other."[141]

IMPACT: CRS notes that, "Exclusion of public assistance cash payments from taxation gives no benefit to the poorest recipients and has little impact on the incomes of many. This is because welfare payments are relatively low and many recipients have little if any non-transfer cash income … If family cash welfare payments were made taxable, most recipients would still owe no tax."[142] Nevertheless, some families with relatively large amounts of cash benefits, as well as those who worked for part of the year and received cash assistance for part of the year, would pay tax if public assistance benefits were taxable; these families therefore benefit from the exclusion.

[141] U.S. Senate, Committee on the Budget, p. 885.

[142] U.S. Senate, Committee on the Budget, p. 884.

Income Tax
Exclusions

48. Roth IRA earnings and distributions

Internal Revenue Code Sections: 219 and 408
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1997

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$4,285	$4,821	$5,625	$6,502
Total	**$4,285**	**$4,821**	**$5,625**	**$6,502**

DESCRIPTION: There are two types of Individual Retirement Accounts (IRAs) that offer tax benefits: the Roth IRA and the traditional IRA. Contributions to a Roth IRA are taxable, but the earnings, as well as qualified distributions made more than five years after the establishment of the IRA, are tax-free. The pattern of benefits for a traditional IRA is the opposite: some contributions to a traditional IRA are tax-deductible for taxpayers below specified income levels, and the earnings on contributions are tax-free, but the qualified distributions are taxable. Participation in IRAs is approximately evenly split between Roth IRAs and traditional IRAs.[143]

Qualified distributions to a Roth IRA are those made after age 59½, upon the death or disability of the individual, or for first-time homebuyer expenses. An individual may contribute up to $5,000 to a Roth IRA ($6,000 for an individual above the age of 50) or an amount equal to earned income, whichever is less, but the tax benefits are limited based on income. The allowable contribution is phased out for single filers with income between $107,000 and $122,000, and for joint filers with income between $169,000 and $179,000, during tax year 2011.

PURPOSE: The purpose of the exclusion is to provide an incentive for taxpayers to save for retirement, and in particular to provide a savings incentive for workers who do not have employer-provided pension plans.

IMPACT: Taxpayers who save for retirement through a Roth IRA benefit from this provision. The Congressional Research Service notes that, "IRAs tend to be less focused on higher-income levels than some types of capital tax subsidies, in part because they are capped at a dollar amount. Their benefits do tend, nevertheless, to accrue more heavily to the upper half of the income distribution. This effect occurs in part because of the low participation rates at lower income levels. Further, the lower marginal tax rates at lower income levels make the tax benefits less valuable."[144]

It is not clear whether Roth IRAs and other tax-favored retirement plans actually increase savings. William Gale and Benjamin Harris of the Urban-Brookings Tax Policy Center point out that, "Savings incentives do not raise private saving to the extent that households finance their

[143] Urban-Brookings Tax Policy Center, The Tax Policy Briefing Book: A Citizens' Guide for the 2008 Election and Beyond, p. II-3-1, available at www.taxpolicycenter.org.

[144] U.S. Senate, Committee on the Budget, pp. 912-913.

contributions by shifting their existing assets into a tax-favored account, or by shifting current-period saving that would have occurred even in the absence of the incentive, or by increasing their debt."[145]

[145] William Gale and Benjamin Harris, "Savings and Retirement: How Does Tax-Favored Retirement Saving Affect National Saving?" in The Tax Policy Briefing Book: A Citizens' Guide for the 2008 Election and Beyond, pp. II-3-13 – II-3-14, available at www.taxpolicycenter.org.

Income Tax
Exclusions

49. Social Security and Railroad Retirement benefits

Internal Revenue Code Section: 86
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1938

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$14,400	$14,960	$15,880	$16,690
Total	**$14,400**	**$14,960**	**$15,880**	**$16,690**

DESCRIPTION: A portion of Social Security and Railroad Retirement Board benefits are not subject to federal income tax. By local law, the District of Columbia has extended the tax exemption to the full amount of benefits (see tax expenditures #127-#130). This description and the estimate of forgone revenue shown above pertain only to the benefits that are exempt due to the District's conformity to the federal income tax rules.

The amount of Social Security benefits and "Tier 1" Railroad Retirement benefits (which are equivalent to Social Security benefits) subject to federal taxation depends on the amount of "provisional income" above certain thresholds. Provisional income is adjusted gross income plus one-half of Social Security benefits and otherwise tax-exempt interest income, such as tax-exempt bonds.

Taxpayers with provisional income under $25,000 (single) or $32,000 (married filing jointly) pay no tax on their Social Security or Railroad Retirement benefits.

If provisional income is above the tax-exempt thresholds but below $34,000 (single) or $44,000 (joint) then the amount of benefits subject to tax is the lesser of: (1) 50 percent of benefits, or (2) 50 percent of income above the tax-exempt thresholds.

If provisional income exceeds $34,000 (single) or $44,000 (joint), then the amount of benefits subject to tax is the lesser of: (1) 85 percent of benefits, or (2) 85 percent of income above the second threshold, plus the smaller of (a) $4,500 for single filers or $6,000 for joint filers, or (b) 50 percent of benefits. The income thresholds described above are not indexed for inflation.

For married people filing separately, taxable benefits are the lesser of 85 percent of benefits or 85 percent of provisional income.

The proceeds from taxation of Social Security and Railroad Retirement benefits at the 50 percent level are credited to the Social Security Trust Fund and the National Railroad Retirement Investment Trust. The proceeds of the taxation of benefits at the 85 percent level are credited to the Medicare Hospital Insurance Trust Fund.

PURPOSE: The purpose of the partial exclusion is to treat Social Security and Railroad Retirement benefits more like other pension income, thereby enhancing horizontal equity. Social Security and Railroad Retirement benefits were tax-free until 1984, unlike other pension benefits which are fully taxable except for the proportion of projected lifetime benefits that can be attributed to the worker's contributions. The Social Security amendments of 1983 (P.L. 98-21) made 50 percent of benefits above threshold amounts taxable, and the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66) created the second level in which 85 percent of benefits above the threshold are subject to taxation.

The Congressional Research Service points out that the exemption level as well as the progressive rates for the taxing of benefits reflect the social welfare goals of Social Security, which differs from a regular pension program in basing its benefits on work history and providing additional benefits to people with lower earnings.[146]

IMPACT: CRS observes that, "Under the current two-level structure, all Social Security beneficiaries have some untaxed benefits. Taxes are imposed on at least half of the benefits for middle- and upper-income beneficiaries, while lower-income beneficiaries have no benefits taxed."[147]

President Bush's Advisory Panel on Federal Tax Reform criticized the two-tiered structure for the taxation of Social Security and railroad retirement benefits for being overly complicated and permitting "bracket creep," which means that more and more recipients cross the income thresholds each year due to inflation and are required to pay more tax.[148]

[146] U.S. Senate, Committee on the Budget, p. 940.

[147] U.S. Senate, Committee on the Budget, p. 941.

[148] The President's Advisory Panel on Federal Tax Reform, p. 88.

Income Tax
Exclusions

50. Survivor annuities paid to families of public safety officers

Internal Revenue Code Section: 101(h)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1997

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	too small	too small	too small	too small
Total	**too small**	**too small**	**too small**	**too small**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: The surviving spouse or child of a public safety officer killed in the line of duty can exclude from gross income a survivor annuity payment under a government pension plan. The annuity must be attributable to the individual's service as a public safety officer.

PURPOSE: According to the Congressional Research Service, "Congress believed that surviving spouses of public safety officers killed in the line of duty should be subject to the same rules as survivors of military service personnel killed in combat."[149]

IMPACT: Surviving family members of officers killed in the line of duty benefit from this provision.

[149] U.S. Senate, Committee on the Budget, p. 936.

Income Tax
Exclusions

51. Workers' compensation benefits

Internal Revenue Code Section: 104(a)(1)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1918

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,332	$3,503	$3,759	$4,000
Total	**$3,332**	**$3,503**	**$3,759**	**$4,000**

DESCRIPTION: Workers' compensation benefits (both medical and non-medical benefits) granted to employees in the case of work-related injury, and to survivors in case of an employee's work-related death, are not taxable. Employers finance the benefits through insurance or self-insurance, and their costs are deductible as a business expense. Benefits are paid regardless of who was at fault, and workers' compensation is treated as the exclusive remedy for work-related injury or death. Workers' compensation programs are administered by the states.

PURPOSE: Although the Congressional Research Service states that no rationale for the exclusion is found in the legislative history (the provision was enacted in 1918), "(I)t has been maintained that workers' compensation should not be taxed because it is in lieu of court-awarded damages for work-related injury or death that, before enactment of workers' compensation laws, would have been payable under tort law for personal injury or sickness and not taxed."[150]

IMPACT: CRS states that, "Exclusion of workers' compensation benefits from taxation increases the value of these benefits to injured employees and survivors, without direct cost to employers, through a tax subsidy. Taxation of workers' compensation would put it on a par with the earned income it replaces. It would also place the 'true' cost of workers' compensation on employers if compensation benefits were increased in response to taxation. It is possible that 'marginal' claims would be reduced if workers knew their benefits would be taxed like their regular earnings."[151]

With regard to equity, CRS notes that the exclusion is "a relatively regressive subsidy because it replaces more income for (and is worth more to) those with higher earnings and other taxable income than for poorer households. While states have tried to correct for this with legislated maximum benefits and by calculating payments based on replacement of after-tax income, the maximums provide only a rough adjustment and few jurisdictions have moved to after-tax income replacement."[152]

[150] U.S. Senate, Committee on the Budget, p. 872.

[151] U.S. Senate, Committee on the Budget, p. 873.

[152] U.S. Senate, Committee on the Budget, p. 873.

Income Tax
Exclusions

52. Active income of controlled foreign corporations

Internal Revenue Code Sections: 11, 882, and 951-964
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1909

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$9,137	$9,655	$10,238	$10,853
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$9,137**	**$9,655**	**$10,238**	**$10,853**

DESCRIPTION: When a U.S. firm earns income through a foreign subsidiary, the income is exempt from U.S. corporate taxes as long as it remains in the hands of the foreign subsidiary. Therefore, federal taxes are deferred until the income is repatriated to the U.S. parent firm as dividends or other income.

When the foreign income is repatriated, the U.S. parent corporation can credit foreign taxes paid by the subsidiary against U.S. taxes owed on the repatriated income. Because U.S. firms can delay paying U.S. taxes by keeping income in the hands of foreign subsidiaries, this provision provides a tax benefit for firms that invest in countries with low tax rates.

PURPOSE: The purpose of this tax deferral is to encourage the purchase and operation of foreign subsidiaries by U.S. firms, thereby increasing U.S. firms' penetration of foreign markets and enhancing the firms' global competitiveness. Proponents also contend that the tax deferral boosts U.S. exports.

IMPACT: U.S. multinational firms with foreign operations in low-tax countries benefit from this provision. The Congressional Research Service observes that, "Economic theory suggests that a tax incentive such as deferral does not promote the efficient allocation of investment. Rather, capital is allocated most efficiently – and world economic welfare is maximized – when taxes are neutral and do not distort the distribution of investment between the United States and abroad. Economic theory also holds that while world welfare may be maximized by neutral taxes, the economic welfare of the United States would be maximized by a policy that goes beyond neutrality and poses a disincentive for U.S. investment abroad."[153]

CRS also points out that deferral probably benefits capital and foreign labor, but may reduce the general U.S. wage level by lowering the stock of capital located in the U.S. CRS states that, "Because the U.S. capital-labor ratio is therefore probably lower it otherwise would be and U.S. labor has less capital with which to work, deferral likely reduces the general U.S. wage level."[154]

[153] U.S. Senate, Committee on the Budget, p. 53.

[154] U.S. Senate, Committee on the Budget, p. 52.

Income Tax
Exclusions

53. Allowances for federal employees working abroad

Internal Revenue Code Section: 912
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1943

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$7,661	$8,086	$8,512	$8,989
Total	**$7,661**	**$8,086**	**$8,512**	**$8,989**

DESCRIPTION: U.S. federal civilian employees working abroad are allowed to exclude from personal taxable income certain special allowances that are provided to offset the costs of living abroad, such as the costs of housing, education, and travel. Like other U.S. citizens, federal employees who work abroad are subject to U.S. taxes and can credit any foreign taxes paid against their U.S. taxes.

PURPOSE: The purpose of this exclusion is to offset the extra costs of working abroad (such as maintaining a home in the U.S. and in the foreign country) and to encourage employees to accept assignments abroad.

IMPACT: Federal civilian employees working abroad benefit from this provision.

Income Tax
Exclusions

54. Income earned abroad by U.S. citizens

Internal Revenue Code Section: 911
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1926

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$6,167	$6,354	$6,634	$6,886
Total	**$6,167**	**$6,354**	**$6,634**	**$6,886**

DESCRIPTION: U.S. citizens who live abroad (except for U.S. government employees, who benefit from a separate exclusion described under tax expenditure #53) were allowed to exclude up to $92,900 in earned income from personal taxable income in 2011. The limit on excludable income is adjusted annually for inflation. A taxpayer must meet foreign residence tests to receive the exclusion. Taxpayers may also exclude a certain amount of foreign housing expenses from taxable income.[155] The combined income and housing exclusion cannot exceed the taxpayer's total foreign earned income for that year.

PURPOSE: The purpose of this exclusion is to compensate U.S. citizens working abroad for the costs of living overseas and the taxes they pay to the foreign country where they live.

IMPACT: U.S. citizens who live and work abroad benefit from this provision. In addition, employers benefit because the exclusion subsidizes the transfer of employees to positions overseas.

[155] The housing exclusion is equal to the amount by which housing costs exceed 16 percent of the earned income exclusion, but cannot exceed 30 percent of the maximum earned income exclusion (which was $91,500 for 2010). In addition, the Treasury Department has the authority to raise the maximum housing exclusion above these levels in high-cost cities.

Income Tax
Exclusions

55. Inventory property sales source rule exception

Internal Revenue Code Sections: 861, 862, 863, and 865
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$4,925	$5,054	$5,054	$5,121
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$4,925**	**$5,054**	**$5,054**	**$5,121**

DESCRIPTION: This provision allows firms to exclude certain export income from the corporate income tax by allocating the income from sales of inventory property to foreign rather than U.S. sources. If the inventory is both manufactured and sold by a firm, it can exempt up to 50 percent of the combined income from U.S. taxes. If the firm earns income only from the sale of the inventory, it can exempt all of the income from U.S. taxes.

This rule on the taxation of inventory property can enable a firm to escape U.S. corporation tax entirely (not just on the portion of income that is attributable to the manufacture or sale of inventory property) because it increases the amount of foreign tax paid, which can be credited against U.S. taxes. Many firms have "excess credits" from prior foreign-source income, so they can reduce their U.S. taxable income by increasing the amount of their income that is attributed to foreign sources. The tax treatment of inventory property represents a tax expenditure because the income from other types of property, such as personal property, cannot be allocated to foreign countries in this way.

PURPOSE: The purpose of the exclusion is to assist U.S. businesses that are engaged in international trade. The Tax Reform Act of 1986 provided that income from the sale of personal property was generally to be attributed to the home country where the seller resides. Nevertheless, Congress was concerned that this rule would create difficulties for U.S. export firms, and therefore made the exemption for inventory property.[156]

IMPACT: Businesses that export goods to other countries are the intended beneficiaries of this provision. Still, the Congressional Research Service notes that, "In the long run … the burden of the corporate income tax (and the benefit from corporate tax exemptions) probably spreads beyond corporate stockholders to owners of capital in general. Thus, the source-rule benefit is probably shared by U.S. capital in general, and therefore probably disproportionately benefits upper-income individuals. To the extent that the rule results in lower prices for U.S. exports, a part of the benefit probably accrues to foreign consumers of U.S. products."[157]

[156] U.S. Senate, Committee on the Budget, p. 59.

[157] U.S. Senate, Committee on the Budget, p. 58.

Income Tax
Exclusions

56. Benefits, allowances, and certain pay for armed forces personnel

Internal Revenue Code Sections: 112 and 134
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1925

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,058	$3,182	$3,557	$3,848
Total	**$3,058**	**$3,182**	**$3,557**	**$3,848**

DESCRIPTION: Compensation received by military personnel for active service in a designated combat zone is not taxable, nor are payments made to families as death gratuities when members of the armed forces die while on active duty or while traveling to or from active duty.[158]

In addition, a range of in-kind benefits received by military personnel are not taxed. These include medical and dental benefits, group life insurance, professional education and dependent education, moving and storage, premiums for survivor and retirement protection plans, subsistence allowances, uniform allowances, housing allowances, overseas cost-of-living allowances, evacuation allowances, family separation allowances, travel for consecutive overseas tours, emergency assistance, family counseling, defense counsel, burial and death services, and travel of dependents to a burial site. Moreover, any cash payments given in lieu of the benefits are also excluded from taxable income.

PURPOSE: The purpose of the exclusion is to recognize the sacrifices made by members of the armed forces, and to establish that the in-kind benefits paid to active personnel are not part of taxable income, partly due to the difficulty of assigning monetary values to the benefits.

IMPACT: District of Columbia residents serving in the military and their families benefit from this provision. The Congressional Research Service observes that, "Some see the provision of compensation in a tax-exempt form as an unfair substitute for additional taxable compensation. The tax benefits that flow from an exclusion do provide the greatest benefits to high- rather than low-income military personnel."[159]

The exclusion may harm efficiency by encouraging the Defense Department to provide members of the armed forces with a greater share of non-cash benefits than they would prefer. According to the U.S. Government Accountability Office, non-cash benefits and deferred compensation accounted for 51 percent of servicemembers' total compensation in 2004, which is much higher than the comparable figure for civilian employment (estimated at less than 33 percent).[160]

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[158] Families of a deceased member of the armed forces receive a $100,000 death gratuity payment.

[159] U.S. Senate, Committee on the Budget, p. 20.

[160] U.S. Government Accountability Office, Military Personnel: DOD Needs to Improve the Transparency and Reassess the Reasonableness, Appropriateness, Affordability, and Sustainability of Its Military Compensation System, GAO-05-798 (July 2005), pp. 21-23.

Income Tax
Exclusions

57. Military disability benefits

Internal Revenue Code Section: 104(a)(4), 104(a)(5), and 104(b)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1942

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$106	$106	$106	$106
Total	**$106**	**$106**	**$106**	**$106**

DESCRIPTION: Service members who become physically unfit to perform military duties can be retired on military disability under certain conditions. Individuals who were members of the armed forces on or before September 24, 1975, may be eligible for the exclusion of disability pay from personal taxable income. The amount of military disability pay is calculated as the greater of (1) the percentage of disability multiplied by the last month of basic pay, or (2) the last month of basic pay multiplied by the number of service years multiplied by 2.5. If the first method is used, the entire amount of disability pay is excludable from taxable income. If the second method is used, only the portion of benefits that would have been paid under the percentage-of-disability method is excludable.

Individuals who joined the armed forces after September 24, 1975, may exclude military disability payments equivalent to disability payments they could have received from the U.S. Department of Veterans Affairs. Otherwise, their disability payments may be excluded only if the disability is directly attributable to a combat-related injury.

Under the Victims of Terrorism Tax Relief Act of 2001, any civilian or member of the military whose disability is attributable to terrorism or military action anywhere in the world may exclude disability income from gross income.

PURPOSE: The purpose of the exclusion is to compensate veterans for economic hardship created by injury or illness. The Congressional Research Service points out that a blanket exclusion for military disability pay was enacted in 1942, based partly on the view that military disability pay was similar to workers' compensation, which was excluded from the federal income tax. In 1976, Congress tightened the exclusion due to concern about abuses by "armed forces personnel who were classified as disabled shortly before becoming eligible for retirement in order to obtain tax-exempt treatment for their pension benefits."[161] However, those who joined the military on or before September 24, 1975, were allowed to continue under the prior rules.

IMPACT: Military veterans who are retired on disability benefit from this exclusion. CRS observes that, "Disability pension payments that are exempt from tax provide more net income than taxable pension benefits at the same level. The tax benefit of the provision increases as the marginal tax rate increases, and is greater for higher-income individuals."[162]

[161] U.S. Senate, Committee on the Budget, p. 24.

[162] U.S. Senate, Committee on the Budget, p. 24.

Income Tax
Exclusions

58. Contributions in aid of construction for water and sewer utilities

Internal Revenue Code Section: 118(c) and 118(d)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1996

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	$0	$0	$0	$0
Total	**too small**	**too small**	**too small**	**too small**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Contributions in aid of construction received by regulated water and sewage disposal utilities are not included in the utilities' gross income if the contributions are spent for the construction of new facilities within two years. Contributions in aid of construction are charges paid by utility customers, usually builders or developers, to cover the cost of expanding, improving, or replacing water or sewage disposal facilities. Contributions that are an advance of funds and require repayment are also excluded from the utilities' income. Connection fees charged to customers for installing lines cannot be excluded from income unless the lines will serve multiple customers. This tax provision allows the utility to treat the contribution as a tax-free addition to its capital rather than treating it as taxable income.

PURPOSE: The purpose of the exclusion is to encourage the modernization of water and sewage facilities. The Tax Reform Act of 1986 repealed a similar subsidy that applied not only to water and sewage facilities, but also to utilities that provided steam, electricity, and gas. Congress reinstated the subsidy for water and sewage facilities in 1996 based on concern that the repeal had inhibited community development and the modernization of water and sewage plants.

IMPACT: Water or sewage disposal utilities are the direct beneficiaries because the utilities are able to attract capital through contributions in aid of construction, in addition to debt or equity financing sources. Nevertheless, the Congressional Research Service notes that the ultimate beneficiaries are unclear because, "To the extent that the lower charges to builders and developers for contributions in aid of construction are passed on to ultimate consumers through lower prices, the benefit from this special tax treatment accrues to consumers. If some of the subsidy is retained by the builders and developers because competitive prices do not require it to be passed forward in lower prices, then the special tax treatment also benefits the owners of the firms." CRS adds that, "Absent a public policy justification, such subsidies distort prices and undermine economic efficiency."[163]

[163] U.S. Senate, Committee on the Budget, pp. 244-245.

Income Tax
Exclusions

59. Earnings of certain environmental settlement funds

Internal Revenue Code Section: 468B
Federal Law Sunset Date: None
Year Enacted in Federal Law: 2005

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	$0	$0	$0	$0
Total	**too small**	**too small**	**too small**	**too small**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Hazardous waste site cleanup is sometimes funded by environmental settlement funds, which serve the same purpose as an escrow account. These funds are established in consent decrees between the U.S. Environmental Protection Agency (EPA) and the parties responsible for contaminating a site, under the jurisdiction of a federal district court. This provision allows businesses that contribute to certain environmental settlement funds to exclude the earnings on those contributions from taxable income. In effect, the provision lowers the after-tax cost to a business of reaching a settlement with the EPA over the clean-up of hazardous wastes identified through the "Superfund" program.

PURPOSE: The purpose of the exclusion is to give parties deemed responsible for hazardous waste sites an incentive to enter into an agreement with the EPA to clean up the sites.

IMPACT: Businesses that establish environmental settlement funds during the eligible period benefit from this provision. There may also be a broader public benefit because the exclusion should encourage those responsible for hazardous wastes to act more quickly to remediate the sites at their own expense, which also saves tax dollars that would otherwise be needed to perform the remediation.

Income Tax
Exclusions

60. Energy conservation subsidies provided by public utilities

Internal Revenue Code Section: 136
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1992

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$6	$6	$6	$6
Personal Income Tax Loss	$196	$196	$187	$187
Total	**$202**	**$202**	**$193**	**$193**

DESCRIPTION: Residential energy customers can exclude from personal taxable income any subsidy they receive from a public utility for purchasing or installing an energy conservation device. If an energy conservation expenditure qualifies for this exclusion, the taxpayer may not claim any other tax benefits for the same expenditure.

PURPOSE: The purpose of the exclusion is to encourage residential customers to participate in conservation programs sponsored by public utilities. These programs would enhance the energy efficiency of dwelling units and encourage energy conservation in residential buildings.

IMPACT: Homeowners who participate in conservation programs and install energy-saving devices benefit from this provision. The Congressional Research Service points out that this tax preference "might be justified on the grounds of conservation, if consumption of energy resulted in negative effects on society, such as pollution. In general, however, it would be more efficient to directly tax energy fuels than to subsidize a particular method of achieving conservation. From an economic perspective, allowing special tax benefits for certain types of investment or consumption results in a misallocation of resources."[164]

CRS also notes that complex incentives are at play in the case of rental housing. Both the tenant and landlord lack a strong financial incentive to invest in energy conservation equipment because the benefits may not accrue entirely to the party paying the cost. Tenants may not occupy a rental property long enough to reap the benefits of energy conservation measures, whereas landlords may not have sufficient control over the behavior of renters to be sure that the investment in energy conservation will pay off. As a result, "These market failures may lead to underinvestment in conservation measures in rental housing and provide the economic rationale for this provision." Nevertheless, the exclusion is available both to owners who occupy their homes and those who rent them out.[165]

[164] U.S. Senate, Committee on the Budget, p. 124.

[165] U.S. Senate, Committee on the Budget, p. 125.

Income Tax
Exclusions

61. Interest on state and local private-activity bonds issued to finance water, sewer, and hazardous-waste facilities

Internal Revenue Code Sections: 103, 141, 142, and 146.
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1968

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$117	$143	$149	$149
Personal Income Tax Loss	$420	$476	$531	$576
Total	**$537**	**$619**	**$680**	**$725**

DESCRIPTION: Interest income on state and local bonds used to finance the construction of sewage facilities, facilities used to supply water, and facilities that dispose of hazardous waste is tax-exempt. The bonds are classifed as private-activity bonds, rather than governmental bonds, when a substantial portion of the benefits accrues to private organizations instead of the general public. The private-activity bonds for these facilities are subject to a state annual volume cap, which was the greater of $90 per capita or $273.775 million in 2010.

In order to qualify for bond financing, water-supply facilities must serve the general public, and must be operated by a governmental unit or have their rates established or approved by a government regulator. The portion of a hazardous waste facility that can be financed with tax-exempt bonds cannot exceed the portion of the facility to be used by entities other than the owner or operator of the facility.

PURPOSE: The purpose of the bonds is to provide low-cost financing of water, sewer, and hazardous-waste facilities. Investors purchase the bonds at low interest rates because the income from them is tax-free.

IMPACT: The Congressional Research Service suggests that tax-exempt financing of water, sewer, and hazardous waste facilities has general public benefits because the subsidy helps correct a market failure that may lead to underinvestment. The benefits of the facilities to the environment and public health cross over state and local borders, but state and local governments may not recognize the spillover benefits when setting spending levels. CRS adds that, "(T)here are significant costs, real and perceived, associated with siting an unwanted hazardous waste facility. The federal subsidy through this tax expenditure may encourage increased investment as well as spread the cost to more potential beneficiaries, federal taxpayers."[166]

CRS also cautions that, "As one of many categories of tax-exempt private-activity bonds, bonds for these facilities increase the financing cost of bonds issued for other public capital. With a greater supply of public bonds, the interest rate on the bonds necessarily increases to lure

[166] U.S. Senate, Committee on the Budget, p. 584.

investors. In addition, expanding the availability of tax-exempt bonds increases the assets available to individuals and corporations to shelter their income from taxation."[167]

[167] U.S. Senate, Committee on the Budget, p. 585.

Income Tax
Exclusions

62. Employer-provided dependent care

Internal Revenue Code Section: 129
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1981

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$1,239	$1,341	$1,444	$1,538
Total	**$1,239**	**$1,341**	**$1,444**	**$1,538**

DESCRIPTION: Employer payments for dependent care through a dependent-care assistance program are not included in an individual's personal taxable income. The maximum annual exclusion is $5,000, and may not exceed the lesser of the employee's earned income or the earned income of the employee's spouse. To qualify, the employer assistance must be provided through a plan that meets certain conditions, such as eligibility requirements that do not discriminate in favor of highly-compensated employees, shareholders, or owners.

Qualifying dependent-care expenses include household services, day care centers, and other similar types of non-institutional care. Dependents must be under the age of 13, except for a physically or mentally incapacitated spouse or dependent who lives with the taxypayer for more than half of the year. Day care centers must comply with state and local laws and regulations for the exclusion of payments to be allowable. Payments to relatives are allowable only if the relatives are not dependents of the taxpayer, or a child of the taxpayer under age 19.

PURPOSE: The Congressional Research Service states that the exclusion was "intended to provide an incentive for employers to become more involved in the provision of dependent care services for their employees."[168]

IMPACT: CRS notes that the exclusion "provides an incentive for employers to provide, and employees to receive, compensation in the form of dependent-care assistance rather than cash … As is the case with all deductions and exclusions, this benefit is related to the taxpayer's marginal tax rate and, thus, provides a greater benefit to taxpayers in high tax brackets than those in low tax brackets."[169] Nevertheless, the $5,000 limit on the exclusion restricts the benefit for upper-income families.

CRS further observes that, "The income tax exclusion violates the economic principle of horizontal equity, in that all taxpayers with similar incomes and work-related child care expenses are not treated equally. Only taxpayers whose employers have a qualified child care assistance program may exclude from income taxes a portion of their work-related child care expenses."

[168] U.S. Senate, Committee on the Budget, p. 738.

[169] U.S. Senate, Committee on the Budget, p. 737.

The horizontal equity problem is one reason why President Bush's Advisory Panel on Federal Tax Refom called for repeal of the exclusion.[170]

On a more positive note, CRS states that, "(I)t is generally believed that the availability of dependent care can reduce employee absenteeism and unproductive work time. The tax exclusion may also encourage full participation of women in the work force as the lower after-tax cost of child care may not only affect labor force participation but hours of work … Those employers that may gain most by the provision of dependent-care services are those whose employees are predominantly female, younger, and whose industries have high personnel turnover."[171]

[170] The President's Advisory Panel on Federal Tax Reform, p. 85.

[171] U.S. Senate, Committee on the Budget, p. 740.

Income Tax
Exclusions

63. Foster care payments

Internal Revenue Code Section: 131
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1982

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$568	$568	$568	$568
Total	**$568**	**$568**	**$568**	**$568**

DESCRIPTION: Payments made by a state, local, or qualified foster-care placement agency to a provider who cares for a foster child in the home are excluded from the personal taxable income of the provider. The exclusion applies both to reimbursements for the general cost of caring for a foster child as well as additional payments provided for the care of a child with physical, mental, or emotional handicaps (the latter are referred to as "difficulty of care" payments).

The exclusion does not cover foster care payments made for more than five children aged 19 or older under the standard benefits, payments for more than 10 children under the age of 19 who are eligible for "difficulty of care" payments, or payments for more than five children aged 19 or older who are eligible for "difficulty of care" payments.

PURPOSE: According to the Congressional Research Service, the exclusion of qualified foster care payments "was made to relieve foster care providers from the detailed record-keeping requirements of prior law," which disallowed any exclusion in excess of the actual expenses paid in caring for a foster child. "Congress feared that detailed and complex record-keeping requirements might deter families from accepting foster children or from claiming the full tax exclusion to which they were entitled."[172]

IMPACT: CRS observes that, "It is generally conceded that the tax law treatment of foster care payments provides administrative convenience for the Internal Revenue Service, and prevents unnecessary accounting and record-keeping burdens for foster care providers. The trade-off is that to the extent foster care providers receive payments over actual expenses incurred, monies which should be taxable as income are provided an exemption for individual income and payroll taxes."[173] Children in foster care may benefit from the exclusion because the reduction in the administrative burden may encourage more people to become foster parents.

[172] U.S. Senate, Committee on the Budget, p. 756.

[173] U.S. Senate, Committee on the Budget, p. 757.

Income Tax
Exclusions

64. Employer-provided parking assistance

Internal Revenue Code Section: 132(f)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,759	$3,930	$4,101	$4,286
Total	**$3,759**	**$3,930**	**$4,101**	**$4,286**

DESCRIPTION: Taxpayers are allowed to exclude up to $240 per month for employer-paid parking in 2012.[174] The maximum monthly exclusion is adjusted annually for inflation.

Employees can use pre-tax dollars, if their employer allows, to pay for parking. A taxpayer who claims a transit benefit can also qualify for mass transit benefits (see tax expenditure #65, "Employer-provided transit assistance," on the next page).

PURPOSE: The exclusion is part of a general policy of excluding employer-provided transportation benefits from taxable income. The exclusion is capped to place a limit on the ability of employers and employees to shift compensation from taxable wages to non-taxable fringe benefits.

IMPACT: The Congressional Research Service states that, "The subsidy benefits both employees, through higher compensation, and their employers, who may face lower wage costs … Higher-income individuals are more likely to benefit from the parking exclusion than the mass transit and vanpool subsidies to the extent that the propensity to drive to work is correlated with income."[175]

CRS adds that, "Subsidies or favorable tax treatment of parking may encourage more employees to drive to work, which may increase traffic congestion and air pollution. One study found that when employees in California firms became able to opt for a cash benefit instead of employer-provided parking benefits, the proportion of employees driving to work fell significantly. Subsidized employee parking may also make finding parking spaces harder, which can affect quality of life in residential neighborhoods near work areas and the flow of customers for retail businesses."[176]

[174] U.S. Department of the Treasury, Internal Revenue Service, Employer's Tax Guide to Fringe Benefits – For Use in 2012 (Publication 15-B, issued December 7, 2011), p. 21.

[175] U.S. Senate, Committee on the Budget, p. 554.

[176] U.S. Senate, Committee on the Budget, p. 556.

Income Tax
Exclusions

65. Employer-provided transit assistance

Internal Revenue Code Section: 132(f)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1992

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$684	$769	$769	$817
Total	**$684**	**$769**	**$769**	**$817**

DESCRIPTION: Taxpayers are allowed to exclude $125 per month for employer-provided transit passes or van-pool benefits in 2012. The maximum monthly exclusion is adjusted annually for inflation. A "transit pass" means any pass, token, farecard, voucher, or similar item that entitles an individual to transportation in a mass-transit system or through a commuter highway vehicle (van pool). Employees can use pre-tax dollars, if their employer allows, to pay for transit passes and vanpool fares. A taxpayer who claims a transit benefit can also qualify for a parking tax benefit (see tax expenditure #64, "Employer-provided parking assistance," on the previous page).

As of March 1, 2009, the American Recovery and Reinvestment Act of 2009 (ARRA) temporarily increased the tax exclusion for transit benefits from $120 to $230 per month, the same amount that employees could exclude for parking benefits at the time. On January 1, 2012, the maximum monthly exclusion for transit benefits returned to the pre-ARRA level, which is now $125 per month due to the inflation adjustment.[177]

PURPOSE: The exclusion is part of a general policy of excluding employer-provided transportation benefits from taxable income. The exclusion is capped to place a limit on the ability of employers and employees to shift compensation from taxable wages to non-taxable fringe benefits.

IMPACT: The Congressional Research Service states that, "The subsidy benefits both employees, through higher compensation, and their employers, who may face lower wage costs."[178] CRS adds that, "Subsidies for mass transit and vanpools encourage the use of mass transportation and may reduce congestion and pollution. Some studies have found that transportation benefit programs can spur non-users of public transportation to become occasional users, and occasional users to become more regular users … If workers commute in ways that reduce traffic congestion, all commuters in an area may enjoy spillover benefits such as lower transportation costs, shorter waiting times in traffic, and improved air quality."[179]

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[177] U.S. Department of the Treasury, Internal Revenue Service, Employer's Tax Guide to Fringe Benefits – For Use in 2012, p. 21.

[178] U.S. Senate, Committee on the Budget, p. 554.

[179] U.S. Senate, Committee on the Budget, p. 555.

Income Tax
Exclusions

66. Interest on state and local private-activity bonds issued to finance airport, dock, and mass commuting facilities

Internal Revenue Code Sections: 103, 141, 142, and 146
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1968

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$130	$194	$194	$243
Personal Income Tax Loss	$664	$775	$775	$839
Total	**$794**	**$969**	**$969**	**$1,082**

DESCRIPTION: Each state receives a certain amount of authority to issue tax-exempt private activity bonds, which are securities issued by a state or local government to finance qualified projects by a private user. These qualified projects, which include the construction of airports, docks, wharves, and mass commuting facilities, are expected to have a public benefit.

Although private-activity mass commuting facility bonds are subject to annual volume caps on private-activity bonds (the cap was $90 per capita or $273.775 million, whichever is greater, in 2010), bonds issued for airports, wharves, or docks are not subject to the caps.

PURPOSE: The purpose of the bonds is to promote the construction of airport, dock, wharf, and mass-transit infrastructure by subsidizing low-interest loans, thereby improving transportation and supporting commerce. Investors purchase the bonds at low interest rates because the income from them is tax-free.

IMPACT: The owners of airport, dock, wharf, and mass-transit infrastructure, as well as the businesses and residents who use these facilities, benefit from this provision. There may also be spillover benefits from such investment. According to the Congressional Research Service, "Economic theory suggests that to the extent these facilities provide social benefits that extend beyond the boundaries of the state or local government, the facilities might be underprovided due to the reluctance of state and local taxpayers to finance benefits for nonresidents."[180]

At the same time, CRS recognizes potential costs of these private activity bonds, stating that, "As one of many categories of tax-exempt private-activity bonds, those issued for airports, docks, and wharves increase the financing cost of bonds issued for other public capital. With a greater supply of public bonds, the interest rate on the bonds necessarily increases to lure investors. In addition, expanding the availability of tax-exempt bonds increases the assets available to individuals and corporations to shelter their income from taxation."[181]

[180] U.S. Senate, Committee on the Budget, p. 565.

[181] U.S. Senate, Committee on the Budget, p. 565.

Income Tax
Exclusions

67. Interest on state and local private-activity bonds issued to finance highway projects and rail-truck transfer facilities

Internal Revenue Code Sections:	103, 141, 142(m), and 146
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	2005

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$39	$39	$32	$32
Personal Income Tax Loss	$199	$188	$177	$166
Total	**$238**	**$227**	**$216**	**$198**

DESCRIPTION: States are authorized to issue tax-exempt private activity bonds, which are securities issued by a state or local government to finance qualified projects by a private user. These qualified projects, which include highway projects and surface freight transfer facilities (truck to rail, or rail to truck) that receive federal aid, are expected to have a public benefit even though a substantial portion of the benefits will accrue to private individuals or businesses.

These bonds are not subject to the federally-imposed annual state volume caps on private-activity bonds, but there is a national limitation of $15 billion on the aggregate value of the bonds, which are allocated by the U.S. Secretary of Transportation.

PURPOSE: According to the Congressional Research Service, in 2005 Congress authorized state and local governments to issue tax-exempt bonds to finance highways and surface freight-transfer facilities in order "to enhance the efficiency of the nation's long-distance freight transport infrastructure. With more efficient intermodal facilities, proponents suggest that long-distance truck traffic will shift from government-financed interstate highways to privately-owned long-distance rail transport."[182] The bonds promote the construction of highways and surface freight-transfer facilities by subsidizing low-interest loans. Investors purchase the bonds at low interest rates because the income from them is tax-free.

IMPACT: Private businesses should benefit from the construction of a more efficient system of long-distance freight transportation, but there may be spillover benefits to society as well in the form of economic development. CRS notes that, "The facilities may be underprovided because state and local taxpayers may be unwilling to finance benefits for nonresidents." At the same time, CRS points out that expanding tax-exempt private-activity bond issuance raises the financing cost of bonds issued for other public capital because, "With a greater supply of public bonds, the interest rate on the bonds necessarily increases to lure investors. In addition, expanding the availability of tax-exempt bonds increases the assets available to individuals and corporations to shelter their income from taxation."[183]

[182] U.S. Senate, Committee on the Budget, p. 542.

[183] U.S. Senate, Committee on the Budget, p. 543.

Income Tax
Exclusions

68. G.I. bill education benefits

U.S. Code Section:	U.S. Code Title 38, Section 5301 (not codified in the Internal Revenue Code)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1917

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$686	$686	$739	$767
Total	**$686**	**$686**	**$739**	**$767**

DESCRIPTION: Higher education benefits that veterans receive under the G.I. bill are excluded from the personal taxable income of recipients (as are all benefits provided by the U.S. Department of Veterans' Affairs).

Veterans who served on active duty for at least three years after September 11, 2001, are eligible for payment of full tuition and fees at all in-state public schools, as well as tuition and fees up to $17,500 per academic year at private or foreign schools. These veterans can also receive an annual stipend of $1,000 for books and supplies. Veterans who served for less than three years can qualify for partial benefits, depending on their length of service.

Veterans who entered active duty before September 11, 2001, are eligible for up to 36 months of education benefits, with the amount of benefits depending on length of service and other factors.

If a veteran qualifies for another education-related tax benefit, such as the Hope Credit or Lifetime Learning Credit, he or she must reduce the value of the other benefit by the amount of any G.I. bill payment made on his or her behalf.

PURPOSE: The purpose of the exclusion is to recognize the service and the sacrifices that veterans made for our country, and to help them prepare for civilian employment.

IMPACT: Veterans receiving education benefits under the G.I. bill benefit from this provision. The U.S. military benefits as well, because the benefits provided under the G.I. bill serve as a valuable recruitment tool.

The tax savings will have greater value for veterans with higher incomes because they are in higher marginal tax brackets.

Income Tax
Exclusions

69. Veterans' benefits and services

U.S. Code Section:	U.S. Code Title 38, Section 5301 (not codified in the Internal Revenue Code)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1917

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$2,904	$3,010	$3,062	$3,145
Total	**$2,904**	**$3,010**	**$3,062**	**$3,145**

DESCRIPTION: All cash payments provided by the U.S. Department of Veterans Affairs are excluded from the personal taxable income of recipients. The payments include veterans' death benefits, disability compensation, and pension payments.

The surviving spouses and parents of servicemembers who die on active duty; veterans who die due to a service-connected illness or condition; and veterans who are totally disabled for 10 or more years before their death due to a non-service-connected illness or condition are eligible for dependency and indemnity compensation payments.

Veterans' service-related disability compensation payments are based on the severity of the disability.

PURPOSE: The purpose of the exclusion is to recognize the service and sacrifices that veterans made for our country, and to provide income support to veterans in their old age.

IMPACT: Individuals receiving veterans' benefits and their families benefit from this provision. The Congressional Research Service observes that, "The exclusion of veterans' benefits alters the distribution of payments and favors higher-income individuals"[184] because those individuals face higher marginal tax rates. CRS adds that, "The rating schedule for veterans disability compensation was intended to reflect the average impact of the disability on the average worker. However, because the rating is not directly rated to the impact of the disability on the veteran's actual or potential earnings, the tax-exempt status of disability compensation payments may reflect a tax exemption for an inaccurate estimate of the veteran's lost earnings because of the disability."[185]

[184] U.S. Senate, Committee on the Budget, p. 949.

[185] U.S. Senate, Committee on the Budget, p. 949.

Income Tax
Adjustments

70. Classroom expenses of elementary and secondary school educators

Internal Revenue Code Section: 62
Federal Law Sunset Date: December 31, 2011
Year Enacted in Federal Law: 2002

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	sunset	sunset	sunset
Personal Income Tax Loss	$187	sunset	sunset	sunset
Total	**$187**	**sunset**	**sunset**	**sunset**

DESCRIPTION: For tax year 2011, a teacher, aide, instructor, counselor, or principal who worked in a public or private school at least 900 hours during the school year and paid for classroom supplies and other materials (such as supplies, materials, books, and software) out of his or her pocket can deduct up to $250 of such expenses. The deduction is limited to elementary and secondary school educators, and must be reduced by the the amount of any interest from an education savings bond, or any distribution from a qualified tuition (section 529) program or a Coverdell education savings account that was excluded from income. Educators in public charter schools are eligible.

This provision expired on December 31, 2011, but there is a revenue loss for FY 2012 because adjustments for tax year 2011 are claimed when people file their tax returns during 2012.

PURPOSE: The purpose of the adjustment is to assist educators in paying for out-of-pocket classroom expenses. According to the Congressional Research Service, a "deduction targeted at educators was considered socially desirable because teachers voluntarily augment school funds by purchasing items thought to enhance the quality of children's education."[186]

IMPACT: CRS observes that, "The availability of the classroom expense deduction may encourage educators who already are doing so to enhance their students' educational experience, and potentially encourages other educators to start doing the same. Alternatively, the deduction may be a windfall to educators."[187]

In tax year 2009, 6,383 District of Columbia tax filers claimed this adjustment. Almost half of the claimants (45 percent) had federal adjusted gross income of less than $50,000.[188]

[186] U.S. Senate, Committee on the Budget, p. 608.

[187] U.S. Senate, Committee on the Budget, p. 608.

[188] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

Income Tax
Adjustments

71. Higher education expenses

Internal Revenue Code Section: 222
Federal Law Sunset Date: December 31, 2011
Year Enacted in Federal Law: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	sunset	sunset	sunset
Personal Income Tax Loss	$634	sunset	sunset	sunset
Total	**$634**	**sunset**	**sunset**	**sunset**

DESCRIPTION: For tax year 2011, certain taxpayers may deduct qualified tuition and related expenses for postsecondary education from their adjusted gross income. This deduction can be taken without itemizing (known as an adjustment or an above-the-line deduction). Taxpayers may claim the deduction for qualified higher education expenses paid for themselves, a spouse, or dependents. Qualified tution and related expenses cover tuition and fees required for enrollment in an institution eligible to participate in U.S. Department of Education student aid programs. Part-time students as well as students in non-degree programs can claim the deduction.

The maximum deduction is $4,000 for single filers with a modified adjusted gross income that does not exceed $65,000 and for joint filers with a modified adjusted gross income that does not exceed $130,000. Taxpayers with income ranging from $65,000 to $80,000 in the case of single filers, or $130,000 to $160,000 for joint filers, may deduct up to $2,000 in qualified higher education expenses. Individuals above these income levels cannot make any deduction.

This provision expired on December 31, 2011, but there is a revenue loss for FY 2012 because adjustments for tax year 2011 are claimed when people file their tax returns during 2012.

The deduction cannot be taken for qualified tuition and related expenses that are covered by the Hope Scholarship Credit or the Lifetime Learning Credit, or by any other tax deduction such as the itemized deduction for education expenses. In addition, any higher education expenses financed by scholarships, Pell Grants, employer-provided educational assistance, veterans' assistance, or by tax-free interest, distributions, or earnings, are not eligible for the deduction.

PURPOSE: The Congressional Research Service states that the deduction "is one additional means that Congress has chosen to help families who are unlikely to qualify for much need-based federal student aid to pay for escalating college expenses."[189]

IMPACT: In tax year 2009, 8,147 District of Columbia tax filers claimed this adjustment. Tax filers with federal adjusted gross income of less than $50,000 comprised 58 percent of the claimants and accounted for 64 percent of the total amount deducted.[190] The relatively high

[189] U.S. Senate, Committee on the Budget, p. 631.

[190] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

percentage of the benefits claimed by low- and moderate-income households reflects the phasing out of benefits at higher income levels.

CRS points out that, "The maximum amount of deductible expenses limits the tax benefit's impact on individuals attending schools with comparatively high tuition and fees."[191] As one of many tax incentives for postsecondary education (including the Hope Scholarship and Lifetime Learning Credits, as well as education savings accounts and qualified tuition plans), the deduction creates additional complexity for taxpayers and the IRS.

[191] U.S. Senate, Committee on the Budget, p. 630.

Income Tax
Adjustments

72. Interest on student loans

Internal Revenue Code Section: 221
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1997

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$507	$634	$634	$713
Total	**$507**	**$634**	**$634**	**$713**

DESCRIPTION: Taxpayers may deduct up to $2,500 in annual interest paid on qualified higher education loans (the maximum deduction is not adjusted for inflation). The deduction can be taken without itemizing (known as an adjustment or above-the-line deduction), but is phased out for taxpayers with modified adjusted gross incomes over $60,000 and $75,000 ($120,000 to $150,000 for joint returns) for tax year 2011.

A qualified education loan represents indebtedness incurred solely to pay for qualified higher education expenses, such as tuition, fees, and room and board, on behalf of a taxpayer, or his or her spouse or dependents. The student must have been enrolled on at least a half-time basis in a program leading to a degree, certificate, or credential at an institution eligible to participate in U.S. Department of Education student aid programs, or at a hospital or health care facility that offers internship or residency programs leading to a certificate or degree.

Interest on loans from relatives or qualified employer plans may not be deducted. The qualifying expenses eligible for deduction must be reduced by the amount of any scholarship or other payment that is excluded from the federal income tax. The deduction is not allowed for individuals who can be claimed as a dependent by another taxpayer.

PURPOSE: According to the Congressional Research Service, the interest deduction "was authorized … as one of a number of benefits intended to make postsecondary education more affordable for middle-income families who are unlikely to qualify for much need-based federal student aid. The interest deduction is seen as a way to help taxpayers repay education loan debt, which has risen substantially in recent years."[192]

IMPACT: In 2009, 31,462 District tax filers claimed the federal student loan adjustment. The bulk of the claimants (59 percent) had federal adjusted gross incomes of less than $50,000,[193] reflecting the phasing out of the benefit at income levels of $60,000 (for individual returns) and $120,000 (for joint returns).

[192] U.S. Senate, Committee on the Budget, p. 618.

[193] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

Researchers from the Urban Institute have pointed out that, "Units that receive the student loan interest deduction differ from units receiving the other tax benefits because benefits accrue to former students who have loans rather than current student and their families."[194]

CRS also discusses the incentives created by the deduction as follows: "The tax deduction can be justified both as a way of encouraging persons to undertake additional education and as a means of easing repayment burdens when graduates begin full-time employment. Whether the deduction will affect enrollment decisions is unknown; it might only change the way families finance college costs. The deduction may allow some graduates to accept public service jobs that pay low salaries, although their tax savings would not be large. The deduction has been criticized for providing a subsidy to all borrowers (aside from those with higher income), even those with little debt, and for doing little to help borrowers who have large loans."[195]

[194] Leonard Burman, Elaine Maag, Peter Orszag, Jeffrey Rohaly, and John O'Hare, "The Distributional Consequences of Federal Assistance for Higher Education: The Intersection of Tax and Spending Programs," Discussion Paper No. 26 of the Urban-Brookings Tax Policy Center, August 2005, p. 8.

[195] U.S. Senate, Committee on the Budget, p. 619.

Income Tax
Adjustments

73. Contributions to health savings accounts

Internal Revenue Code Section: 223
Federal Law Sunset Date: None
Year Enacted in Federal Law: 2003

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$1,367	$1,794	$1,794	$2,074
Total	**$1,367**	**$1,794**	**$1,794**	**$2,074**

DESCRIPTION: Health savings accounts (HSAs) provide a tax-advantaged vehicle for people to pay for medical expenses, such as deductibles and copayments, that are not covered by insurance. Eligible individuals can establish and fund an HSA if they have qualifying high-deductible health insurance (at least $1,200 for single coverage and $2,400 for family coverage in 2011). The minimum deductible levels do not apply to preventive care. Furthermore, qualifying health care plans cannot have limits on out-of-pocket expenditures that exceed $6,050 for single coverage and $12,100 for family coverage in 2011. The goal is to make individuals more conscious of health-care costs while protecting them from catastrophic costs.

For 2010, the annual contribution limit to an HSA was $3,050 for single coverage and $6,150 for family coverage. Individuals who are at least 55 years old but not yet enrolled in Medicare can contribute an additional $1,000 per year. Individuals may deduct their HSA contributions from gross income in calculating their taxable income. An employer can also contribute to an HSA on an employee's behalf, and such contributions are not taxable to the employee or to the employer.

Withdrawals from HSAs are exempt from federal income taxes if they are used for qualified medical expenses. Under the health-care reform act signed by President Obama in 2010, the penalty for an HSA withdrawal that is not used for qualified medical expenses rose from 10 percent to 20 percent in 2011. HSA account earnings are tax-exempt and unused balances may accumulate without limit.

PURPOSE: According to the Congressional Research Service, HSAs were created to (1) slow the growth of health care costs by reducing reliance on insurance and making individuals more aware of the costs of health care, and (2) help individuals finance future health care costs by building up savings. CRS notes that, "Taxpayers can carry their HSAs with them when they change jobs, which, in theory, may help maintain continuity of health care if their new employer offers different or perhaps no health insurance coverage."[196]

IMPACT: A national estimate prepared by the U.S. Government Accountability Office indicated that the average adjusted gross income for an HSA participant was almost $139,000 in 2005, compared to $57,000 for all other filers.[197]

[196] U.S. Senate, Committee on the Budget, p. 777.

[197] U.S. Government Accountability Office, Health Savings Accounts: Participation Increased and Was More Common among Individuals with Higher Incomes, GAO-08-474R, April 30, 2008, p. 6.

CRS observes that, "HSAs could be an attractive option for many people. They allow individuals to insure against large or catastrophic expenses while covering routine and minor costs out of their own pocket. Properly designed, they may encourage more prudent health care use and the accumulation of funds for medical emergencies. For these outcomes to occur, however, individuals will have to put money into their accounts regularly and to refrain from spending it for things other than health care."[198] In addition, it is not clear if individual consumers of health care have the expertise necessary to judge whether they can reduce their usage of health care or purchase lower-cost services without harming their health.

At the same time, HSAs could fracture the health care market. "If HSAs primarily attract young, healthy individuals," CRS states, "premiums for plans without high deductibles are likely to rise since they would disproportionately cover the older and less healthy individuals … If this process continued unchecked, eventually people who need insurance the most would be unable to afford it."[199]

People who finance more of their own health-care costs stand to benefit from HSAs, because they otherwise enjoy a smaller subsidy from the exclusion of employer-provided health care. If an employer-provided health plan switches to a higher deductible, employees would lose out in the absence of an HSA. As CRS states, "HSAs restore this benefit as long as the account is used for health care expenses."[200]

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[198] U.S. Senate, Committee on the Budget, p. 778.

[199] U.S. Senate, Committee on the Budget, p. 778.

[200] U.S. Senate, Committee on the Budget, p. 779.

Income Tax
Adjustments

74. Health insurance premiums and long-term care insurance premiums paid by the self-employed

Internal Revenue Code Section: 162(l)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,925	$4,353	$4,710	$5,181
Total	**$3,925**	**$4,353**	**$4,710**	**$5,181**

DESCRIPTION: Self-employed individuals may deduct amounts paid for health insurance covering themselves, their spouses, or their dependents. In addition, self-employed individuals may also reduce their taxable personal income by the amounts paid for qualified long-term care insurance, subject to annual limits of $200 to $2,500 per individual, depending on the age of the insured person. The deduction is taken "above the line," which means that it can be used regardless of whether the taxpayer itemizes deductions on his or her tax return.

For the purpose of this deduction, a self-employed individual is defined as a sole proprietor, working partner in a partnership, or employee of an S corporation who owns more than 2 percent of the corporation's stock. The following limitations apply: (1) the deduction cannot exceed a taxpayer's net earned income from the trade or business in which the health insurance plan was established, minus deductions for 50 percent of the self-employment tax and any contributions to a qualified pension plan, and (2) the deduction cannot be taken for any month when a self-employed person is eligible to participate in a health insurance plan offered by an employer or a spouse's employer. If a self-employed person claims an itemized deduction for medical expenses, those expenses must be reduced by the amount of this deduction.

PURPOSE: According to the Congressional Research Service, the purpose of the deduction is (1) to provide the self-employed with a tax benefit comparable to the exclusion for employer-provided health benefits, and (2) to improve access to health care by the self-employed.[201]

IMPACT: CRS states that, "The deduction lowers the after-tax cost of health insurance purchased by the self-employed by a factor equal to a self-employed individual's marginal income tax rate. Individuals who purchase health insurance coverage in the non-group market but are not self-employed receive no such tax benefit. There is some evidence that the deduction has contributed to a significant increase in health insurance coverage among the self-employed and their immediate families. As one would expect, the gains appear to have been concentrated in higher-income households."[202]

[201] U.S. Senate, Committee on the Budget, p. 806.

[202] U.S. Senate, Committee on the Budget, p. 806.

That pattern is evident in the District. In 2009, 8,388 District tax filers claimed the federal adjustment for medical insurance premiums. Filers with federal adjusted gross income of $200,000 or more represented 31 percent of the claimants and accounted for more than half (52 percent) of the amount deducted.[203]

CRS also describes some of the efficiency losses to society that may result from the deduction, stating that, "(A) 100-percent deduction is likely to encourage higher-income self-employed individuals to purchase health insurance coverage that leads to wasteful or inefficient use of health care. To reduce the likelihood of such an outcome, some favor capping the deduction at an amount commensurate with a standardized health benefits package, adjusted for regional variations in health care costs."[204]

[203] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

[204] U.S. Senate, Committee on the Budget, p. 807.

Income Tax
Adjustments

75. Contributions to self-employment retirement plans

Internal Revenue Code Sections: 401-407, 410-418E, and 457
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1962

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$12,131	$12,631	$12,988	$13,442
Total	**$12,131**	**$12,631**	**$12,988**	**$13,442**

DESCRIPTION: Self-employed taxpayers who contribute to their own retirement accounts may subtract those contributions from their personal taxable income, up to certain limits. Taxes on the earnings of the retirement accounts are deferred until the funds are distributed during retirement. The withdrawals from the plans are included in personal taxable income. Therefore, the value of the tax expenditure equals the revenue that the government does not collect on the retirement contributions and earnings, offset by the taxes paid on the pensions by those who are currently drawing down the benefits.

One type of self-employment retirement plan is a "simplified employee pension"(SEP). A self-employed taxpayer may deduct SEP contributions of as much as 25 percent of self-employment income (net of any SEP contribution) or $49,000 in 2011 (whichever is less). There are other retirement plan options for the self-employed, including 401(k) plans, other defined contribution plans, and defined benefit plans.

PURPOSE: The purpose of the adjustment is to promote saving for retirement among the self-employed.

IMPACT: In 2009, 5,404 District tax filers claimed this adjustment. The benefits were strongly concentrated among upper-income households. Tax filers with federal adjusted gross income of more than $200,000 represented the majority (57 percent) of the claimants and accounted for 82 percent of the total amount deducted.[205]

The adjustment lowers the after-tax cost of retirement contributions made by the self-employed by a percentage equal to a self-employed individual's marginal income tax rate, which disproprotionately benefits high-income households. The tax-favored treatment of some retirement contributions as well as the earnings on those contributions may encourage individuals to shift their savings from taxable accounts to tax-advantaged accounts without increasing total savings. At the same time, the adjustment also promotes equity among self-employed individuals and individuals who work or public or private-sector organizations.

[205] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

Income Tax
Adjustments

76. Employee contributions to traditional Individual Retirement Accounts

Internal Revenue Code Sections: 219 and 408
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1974

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$6,125	$8,538	$10,022	$13,210
Total	**$6,125**	**$8,538**	**$10,022**	**$13,210**

DESCRIPTION: There are two types of Individual Retirement Accounts (IRAs) that offer tax benefits: the traditional IRA and the Roth IRA. Contributions to a traditional IRA are tax-free for those meeting income requirements, and the earnings on the contributions are tax-free, regardless of income. Qualified distributions from traditional IRAs are taxable. The pattern is inverted for a Roth IRA; the contributions are taxable, while earnings and qualified distributions are tax-free. Participation in IRAs is approximately evenly split between traditional IRAs and Roth IRAs.[206]

Qualified distributions to a traditional IRA are those made after age 59½, upon the death or disability of the individual, or for first-time homebuyer expenses. An individual may contribute up to $5,000 to a traditional IRA ($6,000 for an individual above the age of 50) or an amount equal to earned income, whichever is less, but the tax benefits are limited based on income if a taxpayer is covered by an employer-provided pension plan.

For taxpayers covered by a pension plan, the full deduction is allowed for tax year 2011 if adjusted gross income is less than $56,000 for a single person or $90,000 for a married couple filing jointly. The deduction is phased out over the $56,000 to $66,000 range for single filers and the $90,000 to $110,000 range for joint filers. A taxpayer who is not covered by a pension plan and whose spouse is also not covered is eligible to deduct the full amount of his or her contribution to a traditional IRA, regardless of income.

The estimated value of the tax expenditure reflects the loss of revenue from the exclusion of traditional IRA contributions and earnings, offset by the tax paid on withdrawals from the IRAs.

PURPOSE: The purpose of the exclusion is to provide an incentive for taxpayers to save for retirement, and in particular to provide a savings incentive for workers who do not have employer-provided pension plans.

IMPACT: Taxpayers who save for retirement through a traditional IRA benefit from this provision. However, it is not known whether IRAs benefit society or increase overall levels of saving. It is possible that individuals simply shift existing savings into IRAs because of the tax incentive.

[206] Urban-Brookings Tax Policy Center, The Tax Policy Briefing Book: A Citizens' Guide for the 2008 Election and Beyond, p. II-3-1, available at www.taxpolicycenter.org.

Paul Burham and Larry Ozanne of the Congressional Budget Office state that, "Empirical studies have not been able to resolve the uncertainty about how IRAs affect saving, although many attempts have been made. The evidence for the full population is contradictory, but a limited consensus suggests that IRAs increased saving for nonelderly and less-wealthy families."[207]

The Congressional Research Service points out that, "IRAs tend to be less focused on higher-income levels than some types of capital tax subsidies, in part because they are capped at a dollar amount. Their benefits do tend, nevertheless, to accrue more heavily to the upper half of the income distribution. This effect occurs in part because of the low participation rates at lower income levels. Further, the lower marginal tax rates at lower income levels make the tax benefits less valuable."[208]

In 2009, 4,593 District tax filers claimed this deduction. Approximately half (49 percent) of the claimants had federal adjusted gross income of less than $50,000, and they accounted for 41 percent of the total amount deducted.[209] Although this distribution seems to conflict with CRS' statement that low-income households do not accrue a large share of the benefits, it is possible that in the District the deductions are tilted toward those who are in the upper part of the $0 to $49,999 income category, who would be more able to set aside funds in an IRA.

[207] Paul Burnham and Larry Ozanne, "Individual Retirement Accounts," in *The Encyclopedia of Taxation and Tax Policy*, Second Edition, Joseph Cordes, Robert Ebel, and Jane Gravelle, eds. (Washington, D.C.: The Urban Institute Press, 2005), p. 199.

[208] U.S. Senate, Committee on the Budget, pp. 912-913.

[209] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

Income Tax
Adjustments

77. Overnight travel expenses of National Guard and Reserve members

Internal Revenue Code Section: 62(a)(2)(E) and 162
Federal Law Sunset Date: None
Year Enacted in Federal Law: 2003

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$62	$62	$62	$62
Total	**$62**	**$62**	**$62**	**$62**

DESCRIPTION: A deduction from federal gross income is allowed for all unreimbursed overnight travel, meals, and lodging expenses of National Guard and Reserve members. This deduction can be taken without itemizing (known as an adjustment or above-the-line deduction).

To qualify, members must have traveled more than 100 miles away from home and stayed overnight as part of an activity while on official duty. No deduction is permitted for commuting expenses to and from drill meetings and the amount of expenses may not exceed the general federal government per-diem rate applicable to that locale.

PURPOSE: The purpose of the adjustment is to reimburse members of the National Guard and Reserve for expenses incurred in the line of duty. In enacting the law, Congress noted that more than 157,000 reservists and National Guard members were serving on active duty, most of whom were fighting in Iraq at that time.[210]

IMPACT: National Guard and Reserve members benefit from this provision.

[210] U.S. Senate, Committee on the Budget, p. 28.

Income Tax
Deductions

78. Accelerated depreciation of buildings other than rental housing

Internal Revenue Code Sections: 167 and 168
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$130	$130	$130	$130
Personal Income Tax Loss	$187	$187	$187	$187
Total	**$317**	**$317**	**$317**	**$317**

DESCRIPTION: This provision allows for accelerated depreciation of buildings as a deduction from personal and corporate income tax. The standard method to calculate depreciation is the straight-line method, in which equal amounts are deducted over 40 years. The accelerated method allows buildings used for purposes besides rental housing to be depreciated over 39 years.

The revenue impact of this tax expenditure represents the difference between the tax that would be due under the straight-line method and the tax that is required under accelerated depreciation.

PURPOSE: The purpose of the deduction is to promote investment in buildings. In addition, accelerated depreciation helps to offset any understatement of depreciation that results from use of a historical cost basis to calculate depreciation, which does not account for inflation.

IMPACT: Owners of buildings that are used in a trade or business benefit from this provision. The Congressional Research Service states that, "The direct benefits of accelerated depreciation accrue to owners of buildings, and particularly to corporations … Benefits to capital income tend to concentrate in the higher-income classes."[211]

CRS adds that, "Evidence suggests that the rate of economic decline of rental structures is much slower than the rates allowed under current law, and this provision causes a lower effective tax rate on such investments than would otherwise be the case. This treatment in turn tends to increase investment in nonresidential structures relative to other assets, although there is considerable debate about how responsive these investments are to tax subsidies."[212]

[211] U.S. Senate, Committee on the Budget, p. 431.

[212] U.S. Senate, Committee on the Budget, p. 432.

Income Tax
Deductions

79. Accelerated depreciation of equipment

Internal Revenue Code Sections: 167 and 168
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$4,074	$7,610	$11,473	$14,408
Personal Income Tax Loss	$740	$2,258	$4,110	$5,500
Total	**$4,814**	**$9,868**	**$15,583**	**$19,908**

DESCRIPTION: This provision allows for accelerated depreciation of equipment as a deduction from personal and corporate income tax. The standard method to calculate depreciation is the straight-line method in which equal amounts are deducted in each period. Equipment is currently divided into six categories that are depreciated over 3, 5, 7, 10, 15, and 20 years, respectively. Accelerated depreciation allows for faster write-offs than the straight-line method, using methods such as "double declining balance depreciation," which permits taxpayers to apply twice the straight-line depreciation rate to each year's remaining undepreciated balance.

In addition, Congress and the President have periodically authorized "bonus depreciation," which allows a certain percentage of the cost of machinery and equipment to be deducted immediately. Bonus depreciation is presently in effect under federal law, allowing a 100 percent deduction for equipment placed into service from September 9, 2010, through the end of 2011, and permitting 50 percent expensing through the end of 2012. Nevertheless, in 2008 *the District of Columbia "decoupled" from the federal bonus depreciation rules* (but not from the regular accelerated depreciation rules described in the first paragraph), meaning that taxpayers cannot include the bonus provisions when calculating their District taxes. [213]

As a result, the estimated revenue loss to the District from the tax expenditure reflects only the difference between the tax that would be due under the straight-line method and the tax that is required under the accelerated depreciation provisions described in the first paragraph.

Taxpayers who are eligible for another type of acclerated expensing of the cost of business property (known as the "Section 179 allowance") must calculate their section 179 deduction first and then calculate any additional depreciation from the remaining basis.

PURPOSE: The purpose of this deduction is to promote investment in business machinery and equipment. Proponents of accelerated depreciation contend that the value of machinery and equipment declines faster in the early years, and that depreciation should follow the same pattern.

IMPACT: Owners of machinery and equipment used in a trade or business benefit from this provision. The Congressional Research Service states that, "The direct benefits of accelerated

[213] The statutory provision requiring decoupling was included in D.C. Law 17-219, the "Fiscal Year 2009 Budget Support Act of 2008," which took effect on August 16, 2008. See Title VII-L of the Act.

depreciation accrue to owners of assets and particularly to corporations … Benefits to capital income tend to concentrate in the higher-income classes."[214]

CRS adds that, "Evidence suggests that the rate of economic decline of equipment is much slower than the rates allowed under current law, and this provision causes a lower effective tax rate on such investments than would otherwise be the case. The effects of these benefits on investment in equipment is uncertain, although more studies find equipment somewhat more responsive to tax changes than they do structures. Equipment did not, however, appear to be very responsive to the temporary expensing provisions adopted in 2002 and expanded in 2003."[215]

Another risk is that subsidies for machinery and equipment may encourage the substitution of capital for labor, dampening employment growth.

The Center on Budget and Policy Priorities has urged states to decouple from the federal rules for bonus depreciation, arguing that a substantial portion of the benefits flow to multi-state corporations, which may spend the additional money out-of-state or simply increase their own profit. CBPP also points out that the bonus depreciation provisions include no requirement or incentive for a firm to buy machinery or equipment in state.[216]

[214] U.S. Senate, Committee on the Budget, p. 437.

[215] U.S. Senate, Committee on the Budget, p. 438.

[216] Ashali Singham and Nicholas Johnson, "States Can Avert New Revenue Loss and Protect Their Economies by Decoupling from Federal Expensing Provision," report issued by the Center on Budget and Policy Priorities, April 14, 2011, p. 2.

Income Tax
Deductions

80. Small life insurance company taxable income

Internal Revenue Code Sections: 806
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$65	$65	$65	$65
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$65**	**$65**	**$65**	**$65**

DESCRIPTION: Life insurance companies with gross assets of less than $500 million may take a special deduction on taxable insurance income of as much as $15 million. Specifically, a small life insurance company may deduct 60 percent of the first $3 million of taxable income. for life insurance companies with taxable income between $3 million and $15 million, the deduction equals $1.8 million minus 15 percent of the taxable income above $3 million.

PURPOSE: Although the purpose of the deduction is not clearly stated in the legislative history, the Congressional Research Service posits that the deduction was intended to continue a policy of providing tax-favored treatment to small life insurance companies that dates back to the early 20th century.[217] Policymakers may also have been motivated by a desire to help small businesses and encourage competition in the insurance market.

IMPACT: Small life insurance companies benefit from the tax reduction afforded by this deduction. CRS points out that a company eligible for the maximum deduction of $1.8 million (60 percent of the first $3 million in taxable income) is in effect taxed at a 13.6 percent rate instead of the regular 34 percent corporate rate. CRS adds that, "Determining how benefits for the small life insurance company deduction are distributed is difficult because ownership of these companies may be widely dispersed, either among shareholders in stock companies or policyholders in mutual companies. Competitive pressures may force companies to pass some of these benefits on to life insurance policyholders via lower premiums."[218]

Nevertheless, CRS notes that the deduction violates economic principles and creates costs for society as a whole. First, "The principle of basing taxes on the ability to pay, often put forth as a requisite of an equitable and fair tax system, does not justify reducing taxes on business income for firms below a certain size." In addition, "Imposing lower tax rates on smaller firms distorts the efficient allocation of resources, since it offers a cost advantage based on size and not economic performance. This tax reduction serves no simplification purpose, since it requires an additional set of computations and some complex rules to prevent abuses."[219]

[217] U.S. Senate, Committee on the Budget, p. 312.

[218] U.S. Senate, Committee on the Budget, p. 312.

[219] U.S. Senate, Committee on the Budget, p. 313.

Income Tax
Deductions

81. Amortization of business start-up costs

Internal Revenue Code Section: 195
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1980

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	$1,028	$934	$841	$758
Total	**$1,028**	**$934**	**$841**	**$758**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: This provision allows a taxpayer to deduct from personal or corporate taxable income eligible start-up expenditures of up to $10,000 and to amortize any remaining amount over 15 years. The deduction must be reduced on a dollar-for-dollar basis when the costs exceed $60,000. Therefore, no deduction is allowable for a taxpayer with $70,000 or more of qualified start-up expenditures.

Such expenditures must satisfy two requirements in order to be deducted. First, the expenditures must be paid in connection with creating or investigating a trade or business before the taxpayer begins an active business. Second, the expenditures must reflect costs that would be deductible for an active business.

PURPOSE: The Congressional Research Service states that the deduction was established "to facilitate the creation of new businesses and reduce the frequency of protracted legal disputes over the tax treatment of start-up expenditures." CRS adds that, "The election to deduct and amortize business start-up costs removes an impediment to the formation of new businesses by permitting the immediate deduction of expenses that otherwise could not be recovered until the owner sold his or her interest in the business." [220]

IMPACT: New businesses that incur start-up costs benefit from this provision. As CRS points out, "Benefits to capital income tend to concentrate in the higher income classes."[221] CRS also observes that there are tax administration benefits both to start-up businesses and the IRS, stating that, "In theory, business start-up costs should be written off over the life of the business on the grounds that they are a capital expense. Such a view, however, does pose the difficult challenge of determining the useful life of a business at its outset. Section 195 has two notable advantages as a means of addressing this challenge. First, it makes costly and drawn-out legal disputes involving business taxpayers and the IRS over the tax treatment of start-up costs less likely. Second, it does so at a relatively small revenue cost."[222]

[220] U.S. Senate, Committee on the Budget, p. 450.

[221] U.S. Senate, Committee on the Budget, p. 451.

[222] U.S. Senate, Committee on the Budget, p. 451.

Income Tax
Deductions

82. Completed contract rules

Internal Revenue Code Section: 460
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$454	$454	$518	$555
Personal Income Tax Loss	too small	too small	too small	too small
Total	**$454**	**$454**	**$518**	**$555**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Some taxpayers with construction or manufacturing contracts extending for more than one tax year are allowed to use the completed contract method of accounting. Under this method, income and costs pertaining to the contract are reported when the contract is completed; however, some indirect costs may be deducted from corporate and personal taxable income in the year paid or incurred. This policy has been likened to giving taxpayers an interest-free loan because the speeding up of deductions temporarily provides them with more money.

This deduction is limited to home construction contracts and to other real estate construction contracts if they are in effect for less than two years and the contractor's gross receipts for the previous three years have averaged $10 million or less. The tax expenditure is the revenue loss that results from deferring tax on the contracts covered by the rule, relative to the normal tax treatment of such contracts (which is to capitalize indirect costs and report them at the same time that the income from the contract is reported).

PURPOSE: The purpose of the deduction is to recognize the uncertainities involved in certain contracts, which make it difficult to determine profit or loss until the contract is completed. IRS rules authorized the completed contract method of accounting in 1918, but the use of this method has since been restricted due to concern about perceived abuses by large contractors who were using accrual accounting in their own financial statements (which showed that they could estimate the profit or less before the contract was completed).

IMPACT: The Congressional Research Service states that, "Use of the completed contract rules allows the deferral of taxes through mismatching income and deductions because they allow some costs to be deducted from income in the year incurred, even though the costs actually relate to the income that will not be reported until the contract's completion, and because economic income accrues to the contractor each year he works on the contract but it not taxed until the year the contract is completed. Tax deferral is the equivalent of an interest-free loan from the Government on the amount of the deferred taxes."[223] Although the deduction has minor economic impact, CRS also observes that "it adds some tax advantage to an already heavily-favored" construction sector.[224]

[223] U.S. Senate, Committee on the Budget, p. 472.

[224] U.S. Senate, Committee on the Budget, p. 474.

Income Tax
Deductions

83. Exception from passive loss rules for $25,000 of rental real estate loss

Internal Revenue Code Section: 469(i)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$12,250	$13,857	$15,633	$17,641
Total	**$12,250**	**$13,857**	**$15,633**	**$17,641**

DESCRIPTION: Taxpayers who own rental property and meet specific requirements can deduct up to $25,000 in passive losses from their ordinary income. Passive gains and losses generally arise from ventures such as limited or general partnerships, or other investment-oriented ventures, in which the taxpayer does not actively participate.

Although passive-loss rules usually prohibit deducting rental property losses from income, this tax expenditure involves an exception to those rules. To qualify for the deduction, the taxpayer must play an active role in the rental process, own a stake of at least 10 percent in the property, and have an adjusted gross income of less than $100,000 for a full deduction or $150,000 for a partial deduction.

PURPOSE: The limitations on passive-loss deductions were adopted in the Tax Reform Act of 1986 in order to reduce opportunities for tax sheltering. Many taxpayers had used passive losses in real estate ventures, oil and gas operations, and farming businesses to offset their wage, salary, and active investment income. However, the partial exception for passive losses from rental real estate was established because, "Congress believed that a limited measure of relief … was appropriate in the case of certain moderate-income investors in rental real estate, who otherwise might experience cash flow difficulties with respect to investments that in many cases were designed to provide financial security, rather than to shelter a substantial amount of other income."[225]

IMPACT: Certain owners of rental real estate benefit from this provision. Nevertheless, this exception to the passive-loss rules may create economic distortions and efficiency losses. By extending a tax preference to rental real estate investment, this provision may encourage overinvestment in the real estate sector at the expense of other investments that would otherwise be more productive. Although upper-income households are more likely to own rental properties, the income restrictions curtail the benefits to high-income individuals.

[225] U.S. Congress, Joint Committee on Taxation, General Explanation of the Tax Reform Act of 1986, JCS-10-87 (Washington, D.C.: U.S. Government Printing Office, 1987), p. 230.

Income Tax
Deductions

84. Expensing of depreciable small business property (Section 179 expensing allowance)

Internal Revenue Code Section: 179
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1958

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$369	$270	-$196	-$67
Personal Income Tax Loss	$2,080	$1,702	-$1,056	-$192
Total	**$2,449**	**$1,972**	**-$1,252**	**-$259**

DESCRIPTION: In general, the cost of business property must be deducted from personal and corporate income as it depreciates over its useful life. Section 179 expensing allows certain businesses to deduct the full purchase price of qualified equipment, provided that the amount deducted cannot exceed taxable income from the trade or business in which the property is used. Qualified equipment generally includes new and used machinery, equipment, and off-the-shelf computer software purchased for use in a trade or business. With several exceptions, real property such as buildings and their structural components do not qualify for the deduction.

In recent years, section 179 expensing has been broadened by a series of temporary measures. For tax years 2008 and 2009, the deduction was expanded by the federal Economic Stimulus Act of 2008 and extended by the American Recovery and Re-Investment Act of 2009. The temporary limits allowed a taxpayer to deduct up to $250,000 of the cost of qualifying property (the investment limit) in the year it is purchased. The amount that could be expensed was phased out if the taxpayer purchased more than $800,000 of property during the year. For 2010 and 2011, the limits were even higher: taxpayers could deduct as much as $500,000, with a phaseout beginning at an investment level of $2 million.

The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 set the limit on expensing at $125,000 for 2012, with the phaseout beginning at an investment level of $500,000. The Act also allowed unlimited expensing of equipment placed in service from September 9, 2010, through December 31, 2011. After 2012, the limit on expensing is scheduled to drop to $25,000, with the phaseout starting at $200,000.

In 2008, *the District of Columbia de-coupled from the increases to Section 179 expending*, meaning that individuals and firms were not able to apply the higher expensing levels in calculating their D.C. taxes. [226] The expensing limitation for D.C. taxes equals the lesser of $25,000 (or $40,000 for a qualified high technology company) or the actual cost of the business property during the year it was placed in service. *As a result, the estimated revenue loss to the District from this tax expenditure reflects only this lower expensing limit.*

[226] The statutory provision requiring decoupling was included in D.C. Law 17-219, the "Fiscal Year 2009 Budget Support Act of 2008," which took effect on August 16, 2008. See Title VII-L of the Act.

Taxpayers who are eligible for other types of accelerated depreciation must calculate their section 179 deduction first and then apply any other deductions to the remaining basis.

Accelerated depreciation of any type of property does not change the cumulative amount of depreciation over all years. Therefore, this provision allows a taxpayer to deduct more in the first year of the investment and less in the latter years of the capital life-cycle.

PURPOSE: The expensing allowance, which has been modified and expanded many times since its initial enactment in 1958, was "intended to reduce the tax burden on small firms, give them an incentive to invest more, and simplify their tax accounting," according to the Congressional Research Service.[227]

IMPACT: CRS states that, "In the absence of section 179, the cost of qualified assets would have to be recovered over longer periods. Thus, the provision greatly accelerates the depreciation of relatively small purchases of those assets. This effect has significant implications for business investment. All other things being equal, expensing boosts the cash flow of firms able to take advantage of it, as the present value of taxes owed on the stream of income earned by a depreciable asset is smaller under expensing than other depreciation schedules. Expensing is equivalent to taxing the income earned from affected assets at a marginal effective tax rate of zero."[228] The lower cost of capital and the resulting increase in cash flow are in turn intended to stimulate the economy by spurring capital investment and employment.

CRS also points out that, "(B)ecause the allowance has a phase-out threshold, its benefits are confined to firms that are relatively small in asset, employment, or revenue size. Benefits to capital income tend to concentrate in the higher income classes."[229]

With regard to efficiency effects, CRS states that, "Some argue that investment by smaller firms should be supported by government subsidies because they create more jobs and develop and commercialize more new technologies than larger firms. The evidence on this issue is inconclusive. In addition, economic analysis offers no clear justification for targeting investment tax subsidies at such firms. In theory, taxing the returns to investments made by all firms at the same effective tax rate does less harm to social welfare than granting preferential tax treatment to the returns earned by many small firms."[230]

Another risk is that subsidies for machinery and equipment may encourage the substitution of capital for labor, dampening employment growth.

[227] U.S. Senate, Committee on the Budget, p. 445.

[228] U.S. Senate, Committee on the Budget, pp. 444-445.

[229] U.S. Senate, Committee on the Budget, p. 445.

[230] U.S. Senate, Committee on the Budget, p. 447.

Income Tax
Deductions

85. Expensing of magazine circulation expenditures

Internal Revenue Code Section: 173
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1950

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	too small	too small	too small	too small
Total	**too small**	**too small**	**too small**	**too small**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: This provision allows publishers of periodicals to deduct expenditures to establish, maintain, or increase circulation in the year that the expenditures are made. The revenue impact of this tax expenditure is the difference between the current deduction of costs and the recovery that would have been allowed if these expenses were capitalized and deducted over time.

The expenditures that are eligible for deduction do not include purchases of land and depreciable property, or the expansion of circulation through the purchase of another publisher or its list of subscribers.

PURPOSE: According to the Congressional Research Service, "Congress wanted to eliminate some of the difficulties associated with distinguishing between expenditures to maintain circulation, which had been treated as currently deductible, and those to establish or develop new circulation, which had to be capitalized."[231] There had been numerous disputes between publishers and the IRS, dating back to the late 1920s, about how to make this distinction.

IMPACT: Publishers of periodicals benefit from this provision, but the IRS also benefits from the administrative simplification that results. CRS states that, "Section 173 provides a significant tax benefit for publishers in that it allows them to expense the acquisition of an asset (i.e., lists of subscribers) that seems to yield returns in more years than one. At the same time, it simplifies tax compliance and accounting for them and tax administration for the IRS. Without such treatment, it would be necessary for the IRS or Congress to clarify how to distinguish between expenditures for establishing or expanding circulation and expenditures for maintaining circulation."[232]

CRS adds that, "Like many other business tax expenditures, the benefit tends to accrue to high-income individuals."[233]

[231] U.S. Senate, Committee on the Budget, p. 464.

[232] U.S. Senate, Committee on the Budget, p. 464.

[233] U.S. Senate, Committee on the Budget, p. 464.

Income Tax
Deductions

86. Film and television production costs

Internal Revenue Code Sections: 181
Federal Law Sunset Date: December 31, 2011
Year Enacted in Federal Law: 2004

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$13	$6	sunset	sunset
Personal Income Tax Loss	$9	$0	sunset	sunset
Total	**$22**	**$6**	**sunset**	**sunset**

DESCRIPTION: Generally, the cost of producing films and television programs must be depreciated over a period of time using the income forecast method, which allows deductions based on the pattern of expected earnings. Nevertheless, companies were allowed to deduct immediately the first $15 million of production costs (the amount rises to $20 million for films and TV programs produced in designated low-income areas), provided that at least 75 percent of the compensation associated with the project is for services performed in the United States. Only the first 44 episodes of a TV program qualified for this tax expenditure, and sexually-explicit productions were not eligible.

This provision expired on December 31, 2011, but there will still be a revenue loss in FY 2012 and FY 2013 as deductions from tax year 2011 are claimed.

PURPOSE: According to the Congressional Research Service, the purpose of this deduction was to discourage the movement of film and TV productions to other countries, which often offer tax and other incentives.[234]

IMPACT: Film and TV producers benefit from this provision, because it allows for earlier expensing of costs. CRS points out that, "The benefit is greatest per dollar of investment for those productions whose expected income is spread out over a long period of time and whose production period is lengthy."[235] The cap on the amount that can be expensed focuses the benefits on smaller productions.

CRS adds that, "In general, special subsidies to industries and activities tend to lead to inefficient allocation of resources. Moreover, in the long run, providing subsidies to counter those provided by other countries will not necessarily improve circumstances, unless they induce both parties to reduce or eliminate their subsidies."[236]

[234] U.S. Senate, Committee on the Budget, p. 494.

[235] U.S. Senate, Committee on the Budget, p. 494.

[236] U.S. Senate, Committee on the Budget, p. 495.

Income Tax
Deductions

87. Gain on non-dealer installment sales

Internal Revenue Code Sections: 453 and 453A(b)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$2,657	$3,629	$3,758	$4,536
Personal Income Tax Loss	$1,101	$1,321	$1,046	$1,020
Total	**$3,758**	**$4,950**	**$4,804**	**$5,556**

DESCRIPTION: People who do not deal regularly in selling property (non-dealers) are allowed to report some sales of property for personal and corporate tax purposes under a special method of accounting called the installment method. This method allows the taxpayer to pro-rate the gross profit from the sale over a period in which payments are received. The taxpayer gets the advantage of deferring some of the taxes to future years, rather than paying the taxes in full. The tax expenditure is the difference between what the tax liability would be under year-of-sale reporting and tax liability under installment reporting.

Non-dealers must pay interest to the government on the deferred taxes attributable to the portion of the installment sales that arise during and remain outstanding at the end of the tax year in excess of $5 million. A transaction with a sales price of less than $150,000 does not count toward the $5 million threshold. Because the interest payments offset some of the value of the tax deferral, the tax expenditure reflects only the revenue loss from transactions that give rise to interest-free deferrals.

PURPOSE: The purpose of the deduction is to match the timing of tax payments to the timing of the cash flow generated by the sale of the property. The Congressional Research Service points out that, "It has usually been considered unfair, or at least impractical, to attempt to collect the tax when the cash flow is not available, and some form of installment sale reporting has been permitted since at least the Revenue Act of 1921."[237]

IMPACT: Infrequent sellers of property who sell on an installment basis benefit from this provision. CRS notes that, "The deferral of taxation permitted under the installment sale rules essentially furnishes the taxpayer an interest-free loan equal to the amount of tax on the gain that is deferred." CRS adds that, "(T)he primary benefit probably flows to sellers of farms, small businesses, and small real estate investments."[238]

A fair method of taxing such property sales is difficult to structure. CRS states that, "The installment sales rules have always been pulled between two competing goals: taxes should not be avoidable by the way a deal is structured, but they should not be imposed when the money to pay them is not available. Allowing people to postpone taxes by taking a note instead of cash in a

[237] U.S. Senate, Committee on the Budget, p. 422.

[238] U.S. Senate, Committee on the Budget, p. 422.

sale leaves obvious room for tax avoidance … After having tried many different ways of balancing these goals, lawmakers have settled on a compromise that denies the advantage to taxpayers who would seldom have trouble raising the cash to pay their taxes (retailers, dealers in property, investors with large amounts of sales) and permits its use to small, non-dealer transactions (with 'small' rather generously defined)."[239]

[239] U.S. Senate, Committee on the Budget, p. 423.

Income Tax
Deductions

88. Life insurance company reserves

Internal Revenue Code Sections: 803(a)(2), 805(a)(2), and 807
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$1,555	$1,685	$1,750	$1,859
Personal Income Tax Loss	$0	$0	$0	$0
Total	$1,555	$1,685	$1,750	$1,859

DESCRIPTION: Life insurance companies can deduct net additions to their reserves and must add net subtractions to their reserves when calculating income, subject to certain requirements set forth in section 807 of the Internal Revenue Code. The ability to deduct the net additions to reserves may allow life insurance companies to defer paying some taxes, thus reducing their tax burden by allowing them to offset current income with future expenses. In most years, insurance companies increase their reserves.

PURPOSE: The purpose of the deduction is to make tax rules consistent with standard industry accounting practices. In the insurance industry, it is common practice to use some form of reserve accounting in estimating net income.

Insurance companies have been allowed to deduct any additions to their reserves required by law since the corporate income tax was adopted in 1909. Before Congress adopted the Deficit Reduction Act of 1984 (P.L. 98-369), reserves were required by state law. Because Congress concluded that state rules allowed for a significant overstatement of deductions, it established federal rules for allowable reserves in P.L. 98-369.

IMPACT: The Congressional Research Service observes that, "When life insurance companies can deduct additions to the reserve accounts when computing taxable income, they can purchase assets using tax-free (or tax-deferred) income. Reserve accounting shelters both premium and investment income from tax because amounts added to reserves include both premium income and the investment income earned by the invested assets."[240]

The benefits from the deduction may extend beyond the life insurance companies. CRS points out that, "Competition in the life insurance market could compel companies to pass along corporate tax reductions to policyholders. Thus, this tax expenditure may benefit life insurance consumers as well as shareholders of private stock insurance companies. For mutual life insurance companies, policyholders may benefit either through lower insurance premiums, better service, or higher policyholder dividends."[241]

[240] U.S. Senate, Committee on the Budget, p. 316.

[241] U.S. Senate, Committee on the Budget, p. 316.

Income Tax
Deductions

89. Loss from sale of small business corporation stock

Internal Revenue Code Section: 1244
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1958

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$56	$56	$56	$56
Total	**$56**	**$56**	**$56**	**$56**

DESCRIPTION: Taxpayers may deduct a loss on the sale or exchange of qualifying small business corporation stock as an ordinary loss, rather than a capital loss. The deduction as an ordinary loss is more valuable because ordinary income is taxed at a higher rate than capital income.

The eligibility requirements for a small business corporation include a limit of $1 million on the amount of money and property received for its stock. For any taxable year, the aggregate amount that a taxpayer may treat as an ordinary loss shall not exceed $50,000 for single filers or $100,000 for joint filers. This write-off is much greater than the $3,000 deduction allowed to other corporations. Both C corporations and S corporations are eligible for the deduction.

PURPOSE: The purpose of the deduction is to encourage investment in small businesses. Because small businesses are often unproven and have a high failure rate, the deduction may encourage entrepreneurs to invest in small businesses by offering them some protection against investment losses.

IMPACT: Individuals with losses from small business corporation stock benefit from this provision. Nevertheless, there may be an efficiency loss associated with the deduction, because it channels resources (in the form of tax relief) to businesses based on their size rather than on their productivity and ability to respond to market forces.

Income Tax
Deductions

90. Property and casualty insurance company reserves

Internal Revenue Code Section: 832(b)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$259	$259	$259	$259
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$259**	**$259**	**$259**	**$259**

DESCRIPTION: A property and casualty insurance company's taxable income during a tax year is its underwriting income (i.e., premiums minus incurred losses and expenses) plus investment income and certain other income items minus allowable deductions. Additions to loss reserves held to pay future claims can also be deducted from taxable income under certain conditions.

The Tax Reform Act of 1986 imposed a 15 percent pro-ration provision, due to Congressional concern that the use of tax-exempt investments to finance additions to loss reserves needed to be regulated. Therefore, the allowable deduction for additions to loss reserves was reduced to 15 percent of the sum of (1) the insurer's tax-exempt interest, (2) the deductible portion of dividends received (with special rules for dividends from affiliates), and (3) the increase in the cash value of life insurance, endowment or annuity contracts for the taxable year.

PURPOSE: The Congressional Research Service states that Congress adopted this provision because members concluded that "it is not appropriate to fund loss reserves on a fully deductible basis out of income which may be, in whole or in part, exempt from tax. The amount of the reserves that is deductible should be reduced by a portion of such tax-exempt income to reflect the fact that reserves are generally funded in part from tax-exempt interest or from wholly or partially deductible dividends."[242]

IMPACT: CRS observes that, "The 15 percent pro-ration provision allows property and casualty insurance companies to fund a substantial portion of their deductible reserves with tax-exempt or tax-deferred income. Life insurance companies, banks and brokerage firms, and other financial intermediaries, face more stringent proration rules that prevent or reduce the use of tax-exempt or tax-deferred investments to fund currently deductible reserves or deductible interest expense. Allowing property and casualty insurance companies an advantageous tax status, based on the ability to use tax-exempt income to reduce tax liabilities, may allow those insurers to attract economic resources from other sectors of the economy, thus creating economic inefficiencies." At the same time, CRS points out that, "A more stringent allocation rule could reduce insurance companies' demand for tax-exempt bonds issued by state and local governments, which could raise financing costs for those governments."[243]

[242] U.S. Senate, Committee on the Budget, p. 332.

[243] U.S. Senate, Committee on the Budget, pp. 332-333.

Income Tax
Deductions

91. Research and development expenditures

Internal Revenue Code Section: 174
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$2,851	$3,758	$4,471	$5,741
Personal Income Tax Loss	$93	$93	$93	$93
Total	**$2,954**	**$3,851**	**$4,564**	**$5,834**

DESCRIPTION: This provision allows research and development (R&D) expenditures to be fully deducted as an expense in the first year for purposes of computing corporate and personal taxable income. This policy stands in contrast to the tax treatment of other investments with long-term benefits, in which the expenditures would be depreciated over the useful life of the asset. The deduction for R&D is reduced by the amount of credit that a taxpayer receives for increasing qualified research expenditures under section 41 of the Internal Revenue Code.

PURPOSE: The purpose of deduction is to encourage investment in R&D, and to avoid the difficulty of determining the useful life of any asset created through the research and development process. Many economists contend that society as a whole will underinvest in R&D because private organizations and individuals do not account for the spillover benefits to society when they make decisions to pursue R&D. Therefore, it may be appropriate for the government to encourage greater expenditure on R&D in order to realize its full benefits.

IMPACT: Firms with qualified research and development expenditures benefit from this provision.[244] The Congressional Research Service states that, “The main beneficiaries of the (R&D deduction) are larger manufacturing corporations primarily engaged in developing, producing, and selling technically advanced products. As a corporate tax deduction, the benefits of expensing any capital cost are likely to accrue mainly to upper-income individuals.”[245]

Acknowledging that there is “considerable evidence that the social returns to R&D exceed the private returns,” CRS also points out that there are other methods of subsidizing R&D that “do not necessarily call for the use of a tax preference.” CRS adds that, “A principal shortcoming with tax subsidies like section 174 is that they do not target the R&D investments that are likely to generate the largest social benefits.”[246]

[244] IRS regulations define expenditures eligible for the deduction as “research and development costs in the experimental or laboratory sense,” including all costs related to “the developmetn of an experimental or pilot model, a plant process, a product, a formula, an invention, or similar proeprty, and the improvement of already existing property.

[245] U.S. Senate, Committee on the Budget, p. 85.

[246] U.S. Senate, Committee on the Budget, p. 86.

Income Tax
Deductions

92. Amortization of certified pollution control facilities

Internal Revenue Code Sections: 169(d)(5)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 2005

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$130	$130	$65	$49
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$130**	**$130**	**$65**	**$49**

DESCRIPTION: Coal-fired electric generation plants that invested in pollution control equipment placed in service after April 11, 2005, are eligible for more rapid (seven-year) amortization of costs than would ordinarily be allowed under the modified accelerated cost recovery system. The seven-year amortization applies only to plants that began operation on or after January 1, 1976. Depending on the type of equipment, the normal depreciation rules would allow for depreciation over 15 or 20 years.

Plants that began operating before January 1, 1976, are eligible for five-year amortization if the pollution control equipment has a useful life of 15 years or less. Qualifying pollution control equipment refers to any technology, such as a scrubber system, that is installed by a qualifying facility to reduce the air emissions of any pollutant regulated by the U.S. Environmental Protection Agency under the the Clean Air Act.

PURPOSE: According to the Congressional Research Service, the accelerated depreciation for pollution control equipment "targets electric utilities, a major source of air pollution … The incentive will facilitate utilities in meeting a new suite of EPA mandates to reduce emissions of sulfur dioxide (SO_2), nitrous oxide (NO_2), and mercury (Hg)."[247]

IMPACT: CRS observes that, "Because of the time value of money, the earlier deduction is worth more in present value terms, which reduces the cost of capital and the effective tax rates on the investment returns. This should provide an incentive for power plant companies … to invest in pollution control equipment."[248] At the same time, CRS notes a possible perverse consequence of this subsidy, stating that, "The Clean Air Act's 'New Source Review' provisions require the installation of state-of-the-art pollution-control equipment whenever an air-polluting plant is built or when a 'major modification' is made on an existing plant. By creating a more favorable (in some cases much more favorable) regulatory environment for existing facilities than new ones, grandfathering creates an incentive to keep old, grandfathered facilities up and running."[249]

[247] U.S. Senate, Committee on the Budget, p. 224.

[248] U.S. Senate, Committee on the Budget, p. 224.

[249] U.S. Senate, Committee on the Budget, p. 225.

Income Tax
Deductions

93. Depreciation recovery periods for specific energy property

Internal Revenue Code Sections: 168(e)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$130	$130	$65	$49
Personal Income Tax Loss	too small	too small	too small	too small
Total	**$130**	**$130**	**$65**	**$49**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Federal law allows more rapid depreciation of certain types of tangible energy property than would otherwise be allowed under the Modified Accelerated Cost Recovery System, which provides the standard rules for depreciation. The accelerated depreciation of specific types of energy property, described in the next paragraph, represents a tax expenditure.

The recovery period for certain renewable energy equipment, including solar, wind, geothermal, fuel cell, combined heat and power, and microturbine property is five years. Renewable energy generation property that is part of a "small electric power facility" and certain biomass property are also depreciated over five years. Natural gas gathering lines are subject to seven-year depreciation if the original use commenced after April 11, 2005. A qualified smart meter or smart electric grid system has a recovery period of 10 years. Finally, certain transmission property and natural gas distribution lines placed in service after April 11, 2005, are depreciated over 15 years.[250]

PURPOSE: According to the Congressional Research Service, a detailed legislative history for these provisions (which were contained in separate bills enacted in 1986, 2005, and 2008) is lacking, but the rationale was "presumably to encourage alternative energy sources that are less polluting than conventional fuels."[251]

IMPACT: Commercial property owners who purchase the energy property listed above benefit from the tax subsidy, but there may be efficiency costs to society. CRS points out that, "Economic theory suggests that capital investments should be treated in a neutral fashion to maximize economic efficiency. Permanent investment subsidies, such as accelerated depreciation, may distort the allocation of capital in the long run." Nevertheless, externalties such as the pollution associated with conventional fossil fuels may justify a tax subsidy for alternative energy sources. CRS also observes that, "Economic efficiency may be enhanced by taxing energy sources believed to impose negative external costs, rather than subsidizing renewable alternatives."[252]

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[250] This description is based on U.S. Senate, Committee on the Budget, pp. 107-108.

[251] U.S. Senate, Committee on the Budget, p. 108.

[252] U.S. Senate, Committee on the Budget, p. 109.

Income Tax
Deductions

94. Energy-efficient commercial building property

Internal Revenue Code Section: 179D
Federal Law Sunset Date: December 31, 2013
Year Enacted in Federal Law: 2005

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$65	$65	$65	$65
Personal Income Tax Loss	$93	$93	$93	$93
Total	**$158**	**$158**	**$158**	**$158**

DESCRIPTION: A deduction is available for expenditures on energy-efficient commercial property occurring after December 31, 2005, and before January 1, 2014. The deduction is based on a formula with a maximum of $1.80 per square foot of commercial building space. The deduction is reduced by any amount deducted in prior years (in other words, the limit of $1.80 per square foot is cumulative rather than annual).

A qualified professional must certify that the energy-saving improvements reduce the total energy and power costs of the building by a certain percentage (usually 50 percent) when compared to the costs associated with a similar reference builiding. The building owner must receive a certificate from a licensed professional engineer or contractor before claiming the deduction.

PURPOSE: The purpose of the deduction is to promote energy efficiency by encouraging businesses to retrofit their buildings with energy-conserving equipment. The commercial sector in the United States uses almost as much energy as the residential sector but has generally not been the target of energy conservation incentives.[253] The Energy Tax Act of 1978 targeted the industrial energy sector, but the tax credits authorized by this law have expired.

IMPACT: Businesses that make investments in energy-efficient property are the direct beneficiaries, but there could be spillover benefits to society. The Congressional Research Service points out that, “If consumption of energy results in negative effects on society, such as pollution, the deduction … might be justified. In general, however, it would be more economically efficient to directly tax energy fuels than to subsidize a particular method of achieving conservation.” In addition, CRS notes that there may be market failures in energy conservation for commercial property that is rented out; both landlord and tenant may underinvest in energy conservation equipment because each party is not sure that it will be able to realize the savings needed to offset the up-front cost.[254] The tax deduction may help to correct the market failure.

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[253] U.S. Senate, Committee on the Budget, p. 102.

[254] U.S. Senate, Committee on the Budget, pp. 102-103. For example, the tenant might not occupy the property long enough to realize the benefits, while the landlord might not be certain if the tenant will properly or consistently use the energy-saving equipment in order to generate the required level of savings.

Income Tax
Deductions

95. Blue Cross and Blue Shield companies

Internal Revenue Code Sections: 833
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$259	$259	$324	$365
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$259**	**$259**	**$324**	**$365**

DESCRIPTION: Blue Cross and Blue Shield and other smaller health insurance providers which operated on August 16, 1986, as well as other non-profit health insurers that meet certain community service and medical loss ratio standards, qualify for special tax treatment. A medical loss ratio (MLR) equals total health benefits paid divided by premium income, and is used as an indicator of profitability and administrative efficiency.

This deduction has two main features. First, Blue Cross/Blue Shield and other eligible health insurers are allowed to fully deduct unearned premiums,[255] unlike other property and casualty insurance companies (which is how Blue Cross/Blue Shield and the other insurers are classified under tax law). Second, Blue Cross/Blue Shield and the other insurers may deduct 25 percent of the year's health-related claims and expenses minus their accumulated surplus at the beginning of the year. The special deductions apply only to net taxable income for the year and cannot be used in alternative minimum tax calculations. The health care reform law enacted in 2010 ties the special deduction tax benefits to an MLR threshold of 85 percent for tax years beginning in 2010.

PURPOSE: In the Tax Reform Act of 1986, Congress repealed a tax exemption that Blue Cross/Blue Shield had enjoyed since the 1930s, after finding that the company was engaged in inherently commercial activities and that its tax-exempt status provided an unfair competitive advantage. At the same time, Congress enacted the special deduction to recognize the role of Blue Cross/Blue Shield and other health insurers in providing community-rated health insurance,[256] which is more risky and expensive because it is offered without restrictions based on age, health status, claims history or other factors.

IMPACT: Although the preferential tax treatment presumably benefits Blue Cross/Blue Shield, the other insurers, and the people who receive the insurance, the Congressional Research Service notes that the insurers have moved away from their traditional role of covering smaller, high-risk groups. As a result, "Some have argued that these tax preferences have benefited their managers and their affiliated hospitals and physicians more than their communities."[257]

[255] An unearned premium refers to an insurance premium that has been collected in advance by an insurance company, but must be returned to the client if the coverage ends before the term covered by the insurance is complete (if the client exercises an option to cancel, for example).

[256] U.S. Senate, Committee on the Budget, pp. 321-322.

[257] U.S. Senate, Committee on the Budget, p. 321.

Income Tax
Deductions

96. Medical and dental care expenses

Internal Revenue Code Section: 213
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1942

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$24,420	$26,544	$29,729	$32,970
Total	**$24,420**	**$26,544**	**$29,729**	**$32,970**

DESCRIPTION: Taxpayers who itemize their deductions can deduct from their taxable personal income any medical and dental expenses in excess of 7.5 percent of adjusted gross income (the threshold will rise to 10 percent in 2013). The deduction includes amounts that are paid for health insurance, and covers the medical expenses of the taxpayer, his or her spouse, and dependents.

PURPOSE: The purpose of the deduction is to compensate for large medical bills that are viewed as involuntary expenses and therefore reduce an individual's ability to pay taxes. Still, the Congressional Research Service observes that, "(T)he deduction is not limited to strictly involuntary expenses. It also covers some costs of preventive care, rest cures, and other discretionary expenses."[258]

IMPACT: CRS states that low- to middle-income households claim a large share of the benefits of the deduction because, "Lower-income taxpayers have relatively low rates of health insurance coverage, because they cannot afford health insurance coverage or their employers do not offer it. As a result, many of these taxpayers are forced to pay out of pocket for the health care they and their immediate families receive. In addition, medical spending constitutes a larger fraction of household budgets among low-income taxpayers than it does among high-income taxpayers, making it easier for low-income taxpayers to exceed the 7.5 percent AGI threshold in a given year."[259]

CRS also observes that the deduction does not completely establish horizontal equity among those who receive employer-sponsored health care and those who pay for health care costs out of pocket, stating that, "Employer-paid health care is excluded from income and payroll taxes, whereas the cost of health insurance bought in the non-group market can be deducted from taxable income only to the extent it exceeds 7.5 percent of AGI."[260]

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[258] U.S. Senate, Committee on the Budget, p. 810.

[259] U.S. Senate, Committee on the Budget, p. 810.

[260] U.S. Senate, Committee on the Budget, pp. 810-811.

Income Tax
Deductions

97. Accelerated depreciation of rental housing

Internal Revenue Code Sections: 167 and 168
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$324	$259	$259	$233
Personal Income Tax Loss	$3,924	$3,644	$3,738	$3,596
Total	**$4,248**	**$3,903**	**$3,997**	**$3,829**

DESCRIPTION: Rental housing that was placed in service after 1986 benefits from accelerated depreciation that is calculated on a straight-line basis over 27.5 years. This tax expenditure measures the revenue loss due to the rental housing deductions in excess of those allowed under the 40-year straight-line depreciation allowed under the alternative minimum tax.

Rental housing that was placed in service before 1986 continues to depreciate according to the method in effect when it came on the market, which may allow the property to depreciate faster than under a straight-line method.

PURPOSE: The purpose of accelerated depreciation is to promote investment in rental housing by effectively deferring taxes paid on such investment.

IMPACT: The Congressional Research Service states that, "The direct benefits of accelerated depreciation accrue to owners of rental housing. Benefits to capital income tend to concentrate in the higher-income classes."[261]

With regard to the economic impact of accelerated depreciation, CRS notes that, "Evidence suggests that the rate of economic decline of residential structures is much slower than the rates allowed under current law, and this provision causes a lower effective tax rate on such investments than would otherwise be the case. This treatment in turn tends to increase investment in rental housing relative to other assets, although there is considerable debate about how responsive these investments are to tax subsidies.[262]

In addition, "Much of the previous concern about the role of accelerated depreciation in encouraging tax shelters in rental housing has faded because the current depreciation provisions are less rapid than those previously in place, and because there is a restriction on the deduction of passive losses."[263]

[261] U.S. Senate, Committee on the Budget, p. 376.

[262] U.S. Senate, Committee on the Budget, p. 377.

[263] U.S. Senate, Committee on the Budget, p. 378.

Income Tax
Deductions

98. Mortgage interest on owner-occupied residences

Internal Revenue Code Section: 163(h)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$87,024	$91,093	$98,769	$105,386
Total	**$87,024**	**$91,093**	**$98,769**	**$105,386**

DESCRIPTION: Taxpayers may take an itemized deduction for interest paid on debt secured by a principal or second residence. Although some restrictions apply, most taxpayers can deduct the full amount of their mortgage interest. Mortgage interest is deductible on up to $1 million of debt used to buy, build, or improve a principal or second residence. The deduction is limited to $100,000 in home equity debt. The sum of the acquisition indebtedness and home equity debt cannot exceed the fair market value of the home.

The deduction is considered a tax expenditure because homeowners are allowed to deduct their mortgage interest even though the implicit rental income from the home (the money they could earn by renting to someone else) is not subject to tax. There were no limits on the home mortgage interest deduction until the current restrictions were enacted in 1986 and 1987.

PURPOSE: The home mortgage interest deduction was part of a larger deduction for all interest paid that was established when the personal income tax was first enacted in 1913. The Congressional Research Service states that, "There is no evidence in the legislative history that the interest deduction was intended to encourage home ownership or to stimulate the housing industry at that time."[264]

Proponents of the deduction contend that it encourages homeownership, which in turn is seen as a way to encourage neighborhood stability and civic responsibility by giving people a stronger stake in their communities.

IMPACT: In 2009, 82,417 District tax filers claimed the mortgage interest deduction. Taxpayers with federal adjusted gross income of $100,000 or more comprised 45 percent of the beneficiaries and claimed 60 percent of the total amount deducted.[265] CRS reports that the households with annual income over $100,000 also claimed the bulk (69.2 percent) of the benefits nationwide.[266] Higher-income households can afford to spend more on housing and can qualify to borrow more.

[264] U.S. Senate, Committee on the Budget, p. 337.

[265] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

[266] U.S. Senate, Committee on the Budget, p. 337.

Urban Institute researchers also point out that the mortgage interest deduction "is not a cost-effective tool for increasing homeownership because its main beneficiaries are not individuals on the margin between renting and owning. The deduction is available only to itemizing taxpayers and its value rises with an individual's tax rate."[267] As a result, eliminating the deduction would reduce after-tax income by the largest percentage for those in the 80th to 99th percentiles of the income distribution (those in the top 1 percent would not lose as much because their mortgage costs are lower as a percentage of income).[268]

CRS also describes the economic inefficiencies that may result from the deduction, stating that, "The preferential tax treatment of owner-occupied housing relative to other assets is also criticized for encouraging households to invest more in housing and less in other assets that might contribute more to increasing the Nation's productivity and output … the rate of homeownership in the United States is not significantly higher than in countries such as Canada that do not provide a mortgage interest deduction under their income tax. The value of the U.S. deduction may be at least partly capitalized into higher prices at the middle and upper end of the market."[269]

The home mortgage interest deduction also impairs horizontal and vertical equity. Renters do not receive a comparable tax benefit, while landlords may deduct mortgage interest paid for rental properties, but must pay tax on the rental income (homeowners don't pay any tax on the imputed rental value of their homes). Finally, many elderly individuals do not have home mortgages (they own their homes outright) and therefore do not benefit from the mortgage interest deduction.[270]

[267] Eric Toder, Margery Austin Turner, Katherine Lim, and Liza Getsinger, "Reforming the Mortgage Interest Deduction," April 2010 (available at www.urban.org), p. 3.

[268] Toder, Turner, Lim, and Getsinger, p. 16.

[269] U.S. Senate, Committee on the Budget, p. 338.

[270] Richard Green, "Mortgage Interest Deduction," in The Encyclopedia of Taxation and Tax Policy, Joseph Cordes, Robert Ebel, and Jane Gravelle, eds. Washington, D.C.: The Urban Institute Press, 2005), p. 260.

Income Tax
Deductions

99. State and local property taxes on owner-occupied residences

Internal Revenue Code Section: 164
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$14,586	$15,191	$16,017	$16,801
Total	**$14,586**	**$15,191**	**$16,017**	**$16,801**

DESCRIPTION: Taxpayers may take an itemized deduction for real estate taxes paid on an owner-occupied residence.

PURPOSE: When the U.S. personal income tax was first enacted in 1913, all federal, state, and local taxes were deductible, based on the premise that tax payments reduce disposable income and therefore should not be included in a measure of the taxpayer's ability to pay. Today, proponents argue that the deduction promotes fiscal federalism by helping state and local governments raise revenue to support public services.

IMPACT: In 2009, 85,292 District tax filers claimed the deduction for property taxes paid. Taxpayers with federal adjusted gross income of $100,000 or more comprised 47 percent of the claimants and accounted for 67 percent of the total amount deducted.[271]

As stated by the Congressional Research Service, "Like all personal deductions, the property tax deduction provides uneven tax savings per dollar of deduction. The tax savings are higher for those with higher marginal tax rates, and those homeowners who do not itemize deductions receive no direct tax savings. Higher-income groups are more likely to itemize property taxes and to receive larger average benefits per itemizing return. Consequently, the tax expenditure benefits of the property tax are concentrated in the upper-income groups."[272]

CRS further contends that the deduction "is not an economically efficient way to provide federal aid to state and local governments in general, or to target aid on particular needs, compared with direct aid. The deduction works indirectly to increase taxpayers' willigness to support higher state and local taxes by reducing the net price of those taxes and increasing their income after federal taxes."[273] Nevertheless, a counter-argument is that state and local governments may underinvest in infrastructure or services that spill over beyond their borders; the deduction for state and local taxes may help correct that underinvestment.

[271] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

[272] U.S. Senate, Committee on the Budget, p. 342.

[273] U.S. Senate, Committee on the Budget, p. 344.

A possible unintended consequence is that, "(T)he value of the property tax deduction may be capitalized to some degree into higher prices for the type of housing bought by taxpayers who can itemize."[274] Like the mortgage interest deduction, the property tax deduction may also impair horizontal and vertical equity. Renters cannot deduct their rent payments from the federal income tax, while landlords are able to deduct the property taxes on their rental properties but must pay tax on the rental income (homeowners don't pay any tax on the imputed rental value of their homes).

President Bush' Advisory Panel on Federal Tax Reform called for repeal of deductions for state and local taxes, arguing that, "(T)hese expenditures should be treated like any other nondeductible personal expense, such as food or clothing, and that the cost of these services should be borne by those who want them – not by every taxpayer in the country … As with many other tax benefits, the state and local tax deduction requires higher tax rates for everyone, but the benefits of the deduction are not shared equally among taxpayers."[275]

[274] U.S. Senate, Committee on the Budget, p. 344.

[275] The President's Advisory Panel on Federal Tax Reform, pp. 83-84.

Income Tax
Deductions

100. Casualty and theft losses

Internal Revenue Code Section: 165(c)(3), 165(e), 165(h) - 165(k)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$331	$331	$331	$331
Total	**$331**	**$331**	**$331**	**$331**

DESCRIPTION: Taxpayers who itemize deductions may subtract from taxable income their non-business casualty and theft losses that are not reimbursed through insurance, subject to the following limitations: (1) total losses during the tax year must exceed 10 percent of adjusted gross income, and (2) losses must exceed $100 per event in order to be counted. Eligible losses include those arising from fire, storm, shipwreck or other casualty, or from theft. Congress has removed the 10 percent of AGI threshold and the $100 per-event threshold for calamities such as Hurricanes Katrina, Wilma, and Rita.

PURPOSE: The purpose of the deduction is to reduce the tax burden for those who experience large casualty and theft losses. The $100 floor per-event, which was established in 1964, was intended to reduce the number of small and often improper claims, reduce the costs of record-keeping and audits, and focus the deduction on extraordinary losses.[276]

IMPACT: As stated by the Congressional Research Service, "The deduction grants some financial assistance to taxpayers who suffer substantial casualties and itemize deductions. It shifts part of the loss from the property owner to the general taxpayer and thus serves as a form of government coinsurance. Use of the deduction is low for all income groups."[277]

The benefits may be tilted toward more affluent taxpayers because, "A dollar of deductible losses is worth more to taxpayers in higher income tax brackets because of their higher marginal tax rates," [278] and because the deduction is available only to those who itemize.

Finally, the deduction may protect people who failed to purchase insurance at the expense of those who did. CRS further points out that, "It similarly discriminates against people who take preventive measures to protect their property but cannot deduct their expenses. No distinction is made between loss items considered basic to maintaining the taxpayer's household and livelihood versus highly discretionary personal consumption."[279]

[276] U.S. Senate, Committee on the Budget, p. 900.

[277] U.S. Senate, Committee on the Budget, p. 900.

[278] U.S. Senate, Committee on the Budget, p. 900.

[279] U.S. Senate, Committee on the Budget, p. 901.

Income Tax
Deductions

101. Deduction of foreign taxes instead of a credit

Internal Revenue Code Sections: 901
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$194	$194	$194	$194
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$194**	**$194**	**$194**	**$194**

DESCRIPTION: Taxpayers may elect to claim a deduction against taxable income or a credit against taxes due for any taxes paid on income that was earned abroad. Generally, the credit is more advantageous than the deduction because the credit reduces taxes on a dollar-for-dollar basis, whereas the deduction only reduces the amount of income subject to taxation. Nevertheless, if the taxpayer has reached the foreign tax credit limit, then he or she will benefit from claiming the deduction, which also represents a tax expenditure.

PURPOSE: According to the Congressional Research Service, the rationale for this almost 100-year-old deduction "could have been to recognize foreign taxes, like state taxes, as a possible cost associated with earning income. As such, the provision would help correct for mismeasurement of adjusted gross income and be justified on ability to pay or horizontal equity arguments."[280]

IMPACT: The deduction benefits those who earn income abroad by treating foreign taxes as a business expense. CRS points out that, "This results in the foreign return net of foreign tax equaling the domestic before-tax return and a nationally efficient allocation of capital. While this maximizes the income or output in the domestic market, it also alters the division of income between capital and labor, shifting income towards labor and away from capital. Because national neutrality distorts the location of investment, it produces an inefficient 'deadweight' reduction in world economic welfare."[281]

[280] U.S. Senate, Committee on the Budget, p. 66.

[281] U.S. Senate, Committee on the Budget, p. 66.

Income Tax
Deductions

102. Financing income of certain controlled foreign corporations

Internal Revenue Code Sections: 953 and 954
Federal Law Sunset Date: December 31, 2011
Year Enacted in Federal Law: 1962

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$2,592	sunset	sunset	sunset
Personal Income Tax Loss	$0	sunset	sunset	sunset
Total	**$2,592**	**sunset**	**sunset**	**sunset**

DESCRIPTION: Under the U.S. method of taxing overseas investment, income earned abroad by foreign-chartered subsidiary corporations that are owned and controlled by U.S. investors or firms is generally not taxed if it is reinvested abroad. Instead, U.S. taxes are deferred until the income is repatriated to the U.S. parent firm as dividends or other income.

Subpart F of the U.S. Internal Revenue Code disallows the deferral of tax on foreign income by certain firms known as "controlled foreign corporations."[282] In general, the types of income that fall under subpart F and are therefore subject to current taxation include passive investment, such as interest, dividends, and gains from the sale of stock and securities, as well as certain types of income whose geographic source is thought to be shifted easily.

Ordinarily, income from banking and insurance would often be covered by Subpart F and therefore subject to immediate taxation. Nevertheless, Congress provided a temporary exception from Subpart F for income derived in the active conduct of a banking, financial, or similar business, and for the investment income of an insurance company earned on risks located in its country of incorporation. These exceptions to Subpart F constitute a tax expenditure. This provision expired on December 31, 2011, but there will still be a revenue loss for FY 2012 (which began on October 1, 2011).

PURPOSE: According to the Congressional Research Service, Subpart F was enacted in 1962 to "curtail the use of tax havens by U.S. investors who sought to accumulate funds in countries with low tax rates – hence Subpart F's emphasis on passive income and income whose source can be manipulated."[283] The stated rationale for the banking and insurance exception from Subpart F was that, "(I)nterest, dividends, and like income were not thought to be 'passive' income in the hands of banking and insurance firms."[284]

IMPACT: U.S. firms conducting financial business abroad benefited from this provision. CRS notes that, "(B)anks and insurance firms present an almost insoluble technical problem" in the

[282] A "controlled foreign corporation" is a firm that is at least 50 percent owned by U.S. stockholders, each of whom owns at least 10 percent of the corporation's stock.

[283] U.S. Senate, Committee on the Budget, p. 63.

[284] U.S. Senate, Committee on the Budget, p. 63.

implementation of Subpart F because, "(T)he type of income generated by passive investment and income whose source is easily manipulated are also the types of income financial firms earn in the course of their active business. The choice confronting policymakers, then, is whether to establish an approximation that is fiscally conservative or one that places most emphasis on protecting active business income from Subpart F."[285]

More generally, tax incentives for investment abroad can reduce economic efficiency both for the capital-exporting country (the U.S. in this case) and the world economy. CRS states that, "Economic theory instead recommends a policy known as 'capital export neutrality' under which marginal investments face the same tax burden at home and abroad. From that vantage, then, the exceptions to Subpart F likewise impair efficiency."[286]

[285] U.S. Senate, Committee on the Budget, p. 64.

[286] U.S. Senate, Committee on the Budget, p. 64.

Income Tax
Deductions

103. Charitable contributions

Internal Revenue Code Sections: 170 and 642(c)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1917 (individuals) and 1935 (corporations)

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$2,138	$2,203	$2,268	$2,336
Personal Income Tax Loss	$52,398	$54,930	$57,242	$59,875
Total	**$54,536**	**$57,133**	**$59,510**	**$62,211**

DESCRIPTION: Subject to certain limitations, charitable contributions may be deducted by individuals, corporations, estates, and trusts. The contributions must be made to religious, educational, or scientific institutions; public charities; non-profit hospitals; and federal, state, or local governments. Only individuals who itemize their deductions can claim this deduction.

Individuals may deduct charitable contributions of as much as 50 percent of gross income (30 percent for gifts of capital gain property). Corporations may deduct charitable contributions up to 10 percent of their pre-tax income. Contributions made in the form of property are subject to different rules depending on the type of donor, recipient, and purpose.

PURPOSE: According to the Congressional Research Service, the deduction was originally established for individual taxpayers during World War I in response to concern that high wartime tax rates would curtail charitable contributions.[287] The deduction was extended to corporations in 1935. Proponents argue that the deduction for private donations reduces demand for government services, and that the services provided by voluntary, non-profit organizations may be more efficient and better tailored to people's needs than public services.

IMPACT: In 2009, 103,908 District tax filers claimed this deduction. While 59 percent of the claimants have federal adjusted gross incomes of less than $100,000, they accounted for only 37 percent of the total amount deducted. Those with annual incomes of $200,000 or more recorded 44 percent of the total amount deducted.[288]

The unavailability of the deduction to taxpayers who claim the standard deduction is one reason why the benefits of the charitable contribution deduction are tilted to higher-income individuals; in addition, the higher marginal tax rates faced by higher-income taxpayers mean that each dollar they deduct translates into a larger reduction in tax. To make the deduction more equitable, President Bush's Advisory Panel on Federal Tax Reform proposed making it available to all taxpayers who contribute more than 1 percent of their income to charity, regardless of whether they itemize their deductions.[289]

[287] U.S. Senate, Committee on the Budget, p. 667.

[288] These data are from the Internal Revenue Service's Statistics of Income Tax Stats, Historic Table 2, available at www.irs.gov/taxstats/index.html.

[289] President's Advisory Panel on Federal Tax Reform, pp. 75-76.

CRS states that households at the lower end of the income scale are more likely to claim deductions for donating to religious institutions, whereas higher-income households are more likely to claim deductions for giving to hospitals, the arts, and educational institutions.[290]

Society as a whole may benefit from the deduction because it supports activities, such as education and scientific innovation, that can have large spillover effects. On the other hand, critics "claim that the present system allows wealthy taxpayers to indulge special interests and hobbies. To the extent that charitable giving is independent of tax considerations, federal revenues are lost without having provided any additional incentive for charitable gifts."[291] However, recent research by Jon Bakija of Williams College and Bradley Heim of the U.S. Treasury Department found that the estimated permanent price elasticity of charitable giving is about -0.7 and is higher for high-income individuals. As a result, they conclude there is "fairly robust evidence that charitable giving is fairly responsive to persistent changes in tax incentives."[292]

William Randolph of the U.S. Treasury Department points out that a deduction may not be the most effective to way to promote charitable giving because, "An efficient subsidy would vary with the amount of external benefits, whereas the tax subsidy rate provided by a charitable deduction varies only with the giver's tax rate … Some argue that a tax credit would be a fairer and more efficient form of subsidy because the subsidy rate would not depend as much on the giver's level of income."[293] Moreover, researchers at the Center on Philanthropy at Indiana University have found that economic growth plays a more important role in spurring charitable giving than do changes in tax rates or preferences.[294]

[290] U.S. Senate, Committee on the Budget, p. 762.

[291] U.S. Senate, Committee on the Budget, pp. 762-763.

[292] Jon Bakija and Bradley Heim, "How Does Charitable Giving Respond to Incentives and Income? Dynamic Panel Estimates Accounting for Predictable Changes in Taxation," National Bureau of Economic Research Working Paper 14237, August 2008, p. 41.

[293] William Randolph, "Charitable Deductions," in The Encyclopedia of Taxation and Tax Policy, Joseph Cordes, Robert Ebel, and Jane Gravelle, eds. Washington, D.C.: The Urban Institute Press, 2005), p. 52.

[294] The Center on Philanthropy at Indiana University, "How Changes in Tax Rates Might Affect Itemized Charitable Deudctions" (March 2009), research paper available at www.philanthropy.iupui.edu.

Income Tax
Deductions

104. Costs of removing architectural and transportation barriers to the disabled and elderly

Internal Revenue Code Section:	190
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	1976

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	$93	$93	$93	$93
Total	**$93**	**$93**	**$93**	**$93**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: Business taxpayers may deduct up to $15,000 in annual expenses for the removal of physical barriers to the elderly or persons with disabilities in qualified facilities or public transportation vehicles that the taxpayer owns or leases. Any costs associated with constructing a new facility or vehicle, or undertaking a complete renovation of an existing facility to make it more accessible to the elderly or persons with disabilities, qualifies for the deduction. In the case of a partnership, the $15,000 limit applies separately to the partnership and its individual members.

The tax expenditure associated with this deduction reflects the additional tax savings from the deduction, relative to the regular depreciation rules that would otherwise apply.

PURPOSE: According to the Congressional Research Service, the "likely goal" of the deduction "was to engage the private sector in expanding employment opportunities and improving access to goods and services for the elderly and disabled. Supporters of the provision have long contended that without it, most firms would be unlikely to remove physical barriers to the elderly and disabled from their facilities and transport systems."[295]

IMPACT: CRS states that, "Like all accelerated depreciation allowances, the provision defers a small portion of the tax on any income earned by firms making the requisite improvements. In effect, the provision increases the present value of the depreciation allowances a firm may claim for making the eligible investment."[296]

CRS also questions the impact of the deduction because, "It is not even clear from the business tax data published by the Internal Revenue Service to what extent firms have taken advantage of the section 190 expensing allowance. No studies of the efficacy of the allowance … appear to have been done … Because the allowance covers only a fraction of the expenses a firm incurs in accommodating the needs of disabled employees, it can be argued that its incentive effect is too small to have much of an impact on employment levels for the disabled."[297]

[295] U.S. Senate, Committee on the Budget, p. 503.

[296] U.S. Senate, Committee on the Budget, p. 502.

[297] U.S. Senate, Committee on the Budget, p. 504.

Income Tax
Special Rules

105. 60-40 rule for gain or loss from section 1256 contracts

Internal Revenue Code Sections: 1256
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1981

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	too small	too small	too small	too small
Personal Income Tax Loss	$748	$748	$841	$894
Total	**$748**	**$748**	**$841**	**$894**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: A "section 1256 contract" is any regulated futures contract, foreign currency contract, non-equity option, dealer equity option, or dealer securities futures contract that is traded on a qualified board of exchange with a "mark-to-market" accounting system. Under a mark-to-market system, gains and losses must be reported on an annual basis for tax purposes.

A tax expenditure arises under section 1256 contracts because the capital gain or loss from applicable contracts are treated as consisting of 60 percent long-term and 40 percent short-term gain or loss. The "60-40 rule" removes the one-year holding period requirement for long-term capital gains tax treatment, allowing some gains to be taxed at a lower rate.

The "60-40 rule" does not apply to hedging transactions, which are transactions done by a business in its normal operation with the primary purpose of reducing risks, or to limited partnerships.

PURPOSE: The purpose of this special rule is to provide consistent tax treatment for economically similar contracts, according to the Congressional Research Service.[298]

IMPACT: CRS points out that the use of mark-to-market accounting for section 1256 contracts eliminates the deferral that would result under usual tax rules that recognize gains only when they are realized, rather than when they accrued. At the same time, this accounting method aremoves the one-year holding requirement for long-term capital gains treatment, conferring a benefit to the owners of these assets. According to CRS, this special rule "often results in lower taxes for traders."[299]

[298] U.S. Senate, Committee on the Budget, p. 534.

[299] U.S. Senate, Committee on the Budget, p. 534.

Income Tax
Special Rules

106. Interest rate and discounting period assumptions for reserves of property and casualty insurance companies

Internal Revenue Code Sections: 831, 832(b), and 846
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$454	$518	$454	$454
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$454**	**$518**	**$454**	**$454**

DESCRIPTION: Property and casualty insurance companies may gain a tax advantage from the rules for calculating the present value of future losses. A present value is the current equivalent value of a given cash flow, and is calculated using interest rates or discount factors and information about the timing of income and losses. Most businesses calculate taxable income by deducting expenses when the business becomes liable for paying them. However, property and casualty companies pay out a significant portion of losses years after premiums were collected. Therefore, it is necessary to discount losses in future years to prevent the insurer from gaining a tax advantage from deferring loss payments.

Each year, the U.S. Treasury Department specifies discount factors for various lines of property and casualty insurance that are used to compute present value of future losses for tax purposes. If Treasury uses long-term market interest rates, that will tend to overstate the present value of losses paid in the near future while underestimating the present value of losses paid further into the future. A tax expenditure arises if the net present value of losses calculated by the insurers for tax purposes is greater than the true net present value of the losses based on efficient financial strategies.

PURPOSE: According to the Congressional Research Service, "Requiring most property and casualty companies to calculate the present value of future losses … using discount rates specified by the Treasury may simplify the calculation of tax liability for those insurers. In addition, the relative simplicity of the methods may help ensure that the tax treatment of property and casualty companies is uniform."[300]

IMPACT: Although the provision should benefit property and casualty insurance companies, doing so shifts the tax burden to other taxpayers or results in a loss of federal revenue. CRS points out that, "Allowing property and casualty insurance companies an advantageous tax status, based on the potential mismatch between simple tax rules and actual financial management practices, may allow those insurers to attract economic resources from other sectors of the economy, thus creating economic inefficiencies."[301]

[300] U.S. Senate, Committee on the Budget, p. 329.

[301] U.S. Senate, Committee on the Budget, p. 329.

Income Tax
Special Rules

107. Inventory accounting

Internal Revenue Code Sections: 475, 491-492
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1938

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$2,851	$3,046	$3,175	$3,356
Personal Income Tax Loss	$654	$654	$748	$801
Total	**$3,505**	**$3,700**	**$3,923**	**$4,157**

DESCRIPTION: Businesses that sell goods generally must maintain inventory records to determine the cost of the goods sold. Businesses can account for inventory on an item-by-item basis, but may also use rules such as first-in, first-out (FIFO) accounting, which assumes that the most recent item sold is the earliest one that was purchased, and last-in, first-out (LIFO) accounting, which assumes that the most recent item sold is the last one purchased. In connection with FIFO, businesses may choose the lower of cost or market (LCM) method, which allows them to deduct losses on goods that have fallen in value below their original cost while in inventory. LIFO can only be used if it is also used for financial reporting, although it is not allowable for securities dealers.

The use of the LCM method under FIFO, as well as the LIFO method more generally, are considered tax expenditures because basic FIFO is seen as the appropriate method of accounting for costs by matching the order of purchase with the order of sale. LIFO provides more favorable tax treatment because increases in price over time will increase the amount of the deduction. LCM also provides a tax benefit because it allows firms to recognize losses when prices drop but does not require any corresponding recognition of gain when prices rise in value.

PURPOSE: According to the Congressional Research Service, LIFO was originally adopted "to allow a standard accounting practice." Because price inflation was very low, LIFO originally had a very minor impact. CRS also notes that LCM was "considered a conservative accounting practice which reflected the loss in value of inventories."[302] President Obama's FY 2010 and FY 2011 budget requests included a proposal to repeal both LIFO and LCM.

IMPACT: One study found that LIFO is most heavily used by the chemical, furniture, general merchandise, and metal industries, while another study concluded that LIFO is most often used by the petroleum industry and by motor vehicle, food and beverage, and general merchandise retailers.[303] LIFO allows firms to lower their tax burden by reducing the difference between the sales price and the cost of inventory, and may even encourage firms expecting a high tax bill to purchase more inventory before the year ends to reduce taxable income. CRS notes that small firms may benefit by using LSM for both tax and financial purposes.[304]

[302] U.S. Senate, Committee on the Budget, p. 518.

[303] U.S. Senate, Committee on the Budget, p. 518.

[304] U.S. Senate, Committee on the Budget, p. 519.

Income Tax
Special Rules

108. Ordinary gain or loss treatment for sale or exchange of Fannie Mae and Freddie Mac preferred stock by certain financial institutions

U.S. Code Section:	Section 301 of P.L. 110-343 (Not codified in Internal Revenue Code)
Federal Law Sunset Date:	None
Year Enacted in Federal Law:	2008

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Corporate Income Tax Loss	$65	-$65	-$65	-$65
Personal Income Tax Loss	too small	too small	too small	too small
Total	**$65**	**-$65**	**-$65**	**-$65**

Note: "Too small" means that the nationwide federal revenue impact was estimated as $50 million or less.

DESCRIPTION: This tax expenditure allows capital gains or losses from the sale or exchange of preferred stock of Fannie Mae and Freddie Mac to be treated as ordinary income or loss by applicable financial institutions, including banks, cooperative banks, and savings and loan associations, among others. This means that losses can be directly used by the financial institutions to reduce taxable income.

For sales or exchanges of Fannie Mae and Freddie Mac preferred stock occurring between January 1, 2008 and September 6, 2008, the taxpayer must have been an eligible financial institution at the time of the sale. For sales or exchanged after September 6, 2008, the taxpayer had to be an eligible financial institution at all times between September 6, 2008 and the date of sale or exchange, and the preferred stock had to be held by the institution on September 6, 2008.

PURPOSE: According to the Congressional Research Service, the enactment of this provision was motivated by concern about the precarious condition of financial institutions in 2008. After the government seized control of Fannie Mae and Freddie Mac that year, it suspended dividends on the preferred stock of both organizations and made their preferred stock subordinate to the senior preferred stock issued to the U.S. Treasury. As a result, the value of Fannie Mae and Freddie Mac's preferred stock plummeted. By allowing financial institutions to treat the losses incurred as ordinary income, the institutions could use the losses to reduce taxable income for 2008. Therefore, "The basic idea behind this tax relief was to reduce the need of banks 'to obtain additional capital from the (Federal Deposit Insurance Corporation) or investors.'"[305]

IMPACT: Financial institutions owning Fannie Mae or Freddie Mac preferred stock benefit from this rule. CRS points out that the rule may have prevented some community banks from becoming insolvent.[306]

[305] U.S. Senate, Committee on the Budget, p. 516.

[306] U.S. Senate, Committee on the Budget, p. 516.

Income Tax
Special Rules

109. Special alternative tax on small property and casualty insurance companies

Internal Revenue Code Sections: 321(a), 501(c)(15), 832, and 834
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$65	$65	$65	$65
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$65**	**$65**	**$65**	**$65**

DESCRIPTION: Insurance companies that are not classified as life insurance companies (mostly property and casualty insurance companies) enjoy tax-exempt status if their annual gross receipts are $600,000 or less and if premiums account for 50 percent or less of their gross receipts. Mutual insurance companies may enjoy tax-exempt status if their annual gross receipts are $150,000 or less, and if more than 35 percent of the receipts consist of premiums.

Slightly larger insurance companies that are not classified as life insurance companies may elect to be taxed only on their taxable investment income, provided that net written premiums and direct written premiums each do not exceed $1.2 million.

PURPOSE: Small insurance companies have enjoyed tax advantages for more than a century, dating back to a time when tax-exempt fraternal beneficiary societies provided life insurance to about 30 percent of the population. The Congressional Research Service states that, "These provisions may have been included to encourage formation of small insurance companies to serve specific groups of individuals or firms that could not easily obtain insurance through existing insurers."[307]

IMPACT: Due to this provision, "Some very small non-life insurance companies are exempted from taxation entirely, while slightly larger non-life insurance companies may choose a potentially advantageous tax status instead of being taxed at the regular corporate tax rate of 34 percent." It is difficult to determine how the benefits of the deduction are distributed because "ownership of some of these companies may be widely dispersed. Competitive pressures may force companies to pass some of these benefits on to insurance policyholders via lower premiums. In other cases, a set of companies may set up a 'captive' or 'minicaptive' insurance company, which provides insurance policies in exchange for premiums. In these cases, stakeholders in the parent companies benefit from the tax exemption."[308]

Still, CRS notes that the deduction violates economic principles and creates costs for society as a whole. First, "The principle of basing taxes on the ability to pay, often put forth as a requisite of an equitable and fair tax system, does not justify reducing taxes on business income for firms

[307] U.S. Senate, Committee on the Budget, p. 324.

[308] U.S. Senate, Committee on the Budget, p. 324.

below a certain size." In addition, "Imposing lower tax rates on smaller firms distorts the efficient allocation of resources, since it offers a cost advantage based on size and not economic performance. This tax reduction serves no simplification purpose, since it requires an additional set of computations and some complex rules to prevent abuses."[309]

[309] U.S. Senate, Committee on the Budget, p. 325.

Income Tax
Special Rules

110. Apportionment of research and development expenses for determining foreign tax credits

Internal Revenue Code Sections: 861-863 and 904 (also see IRS Regulation 1.861-17)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1977

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$259	$259	$259	$259
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$259**	**$259**	**$259**	**$259**

DESCRIPTION: This tax expenditure arises from a complicated set of rules governing the allocation of research and development (R&D) expenses by multinational corporations. These rules allow some corporations to claim larger foreign tax credits that can be used to offset U.S. corporate tax liability.

When foreign-source income is repatriated to the U.S. in the form of dividends, royalties, or other income, the U.S. parent corporation can claim a credit against its U.S. tax liability for any foreign taxes the subsidiary has paid on that income, in order to avoid double taxation of the income. The credit cannot exceed the U.S. tax due on the foreign-source income. Multinational corporations must allocate deductible expenses between foreign and domestic income, but this is difficult in the case of R&D because of its long-term nature.

IRS regulations that were most recently revised in 1995 require U.S.-based multinational corporations to allocate a portion of R&D expenditures to foreign countries even if the research was performed entirely in the U.S. Because most foreign governments do not allow a tax deduction for R&D, the required allocation of R&D expenses to these countries raises the amount of foreign tax paid and therefore increases foreign tax credits against U.S. taxable income.[310]

PURPOSE: According to the Congressional Research Service, the relevant IRS regulations were "guided by the notion that if R&D conducted in the United States often contributes to the development of goods and services sold in foreign markets, then the accurate measurement of foreign income for U.S. multinational companies requires that part of their domestic R&D expenses be deducted from foreign income."[311]

IMPACT: The effects of the R&D apportionment rules are unclear. Supporters of the regulations contend that allocating all R&D expenses to U.S. income would be equivalent to allowing a double deduction in cases where foreign countries provide a deduction. Critics argue that the regulations discourage R&D and encourage U.S. companies to transfer some of their R&D to foreign locations with higher tax rates.[312]

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[310] This description is based on U.S. Senate, Committee on the Budget, pp. 39-42.

[311] U.S. Senate, Committee on the Budget, p. 42.

[312] U.S. Senate, Committee on the Budget, pp. 44-46.

Income Tax
Special Rules

111. Interest-charge domestic international sales corporations

Internal Revenue Code Sections: 991-997
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Loss	$65	$65	$65	$65
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$65**	**$65**	**$65**	**$65**

DESCRIPTION: An "Interest-Charge Domestic Sales Corporation" (IC-DISC) is a domestic corporation, usually formed as a tax-exempt subsidiary of another corporation or trust, that exports U.S. products. The parent company pays the IC-DISC a tax-deductible commission for its qualified export sales. Because the IC-DISC is tax-exempt, distributions to IC-DISC shareholders are taxed only once at the lower individual dividend and capital gains tax rates. As a result, the shareholders enjoy a preferred after-tax return which represents a tax expenditure.

IC-DISC shareholders may also defer up to $10 million in income that is attributable to qualified export sales. An interest charge is imposed on shareholders, however, based on the distribution that would have occurred without the deferral. The $10 million deferral limit was intended to limit the benefit of IC-DISC activity to smaller businesses.

PURPOSE: According to the Congressional Research Service, "IC-DISC was intended to increase U.S. exports and provide an incentive for U.S. firms to operate domestically rather than abroad. Additionally, IC-DISC was adopted as a way to partially offset export subsidies offered by foreign countries."[313]

IMPACT: Although IC-DISCs are intended to strengthen the U.S. economy by increasing exports and discouraging U.S. corporations from establishing subsidiaries in foreign countries, CRS highlights a number of negative consequences. For example, "With flexible exchange rates, an increase in U.S. exports resulting from IC-DISC likely causes an appreciation of the U.S. dollar relative to foreign currencies. In response, U.S. citizens could be expected to increase their consumption of imported goods, possibly at the expense of domestically produced substitutes. As a result, no improvement in the balance of trade occurs and domestic employment could decrease."

CRS also points to "inefficiencies that IC-DISC may introduce into the allocation of productive economic resources within the U.S. economy, as only domestic exporters benefit from the subsidy. Additionally, because the tax benefit is related to the production of exported goods and services, domestic consumers receive no direct consumption benefit. Foreign consumers, on the other hand, benefit from lower-priced goods."[314]

[313] U.S. Senate, Committee on the Budget, p. 72.

[314] U.S. Senate, Committee on the Budget, p. 73.

PART II: LOCAL TAX EXPENDITURES

INCOME TAX
(LOCAL BUSINESS AND PERSONAL INCOME TAX)

Income Tax
Exemptions

112. Additional personal exemption for the blind

District of Columbia Code: D.C. Official Code § 47-1806.02(d)
Sunset Date: None
Year Enacted: 1987

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$96	$103	$106	$109
Total	**$96**	**$103**	**$106**	**$109**

DESCRIPTION: All District of Columbia taxpayers may claim a personal exemption, which amounts to $1,675 for tax year 2011. An additional exemption of equal value ($1,675) is available for a blind taxpayer, and for the blind spouse or domestic partner of a taxpayer, if the spouse or partner has no gross income and is not the dependent of another taxpayer.

The District provides a larger additional exemption for the blind than Maryland ($1,000) or Virginia ($800).[315] The federal government provides an additional standard deduction for the blind equal to $1,450 for single filers and $1,150 for married individuals.

Although the D.C. Code provides that the exemption shall be adjusted annually to reflect changes in the cost of living,[316] in 2010 the adjustments were suspended until January 1, 2013, to help close the budget gap created by the economic recession.[317]

PURPOSE: The purpose of this provision is to reduce the tax burden of taxpayers who are blind or who have blind spouses or domestic partners, based on the assumption that someone who is blind faces additional expenses that make it harder to maintain an adequate standard of living.

IMPACT: Taxpayers who are legally blind, or have a legally blind spouse or domestic partner, benefit from this provision. In tax year 2009, the exemption was claimed on behalf of 890 individuals and 69 percent of the benefits (in terms of reduced tax liability) went to filers with income at or below $75,000 (see table on the next page).

[315] Wisconsin Legislative Fiscal Bureau, "Individual Income Tax Provisions in the States," Informational Paper 4 (January 2011), p. 2.

[316] See D.C. Official Code § 47-1806.02(i).

[317] The suspension of the cost-of-living adjustments was made by Title VII-V of D.C. Law 18-111, the "Fiscal Year 2010 Budget Support Act of 2009." Under current law, once the suspension ends the exemption was to be adjusted to make up for the three years of forgone inflation adjustments. In his FY 2013 budget, Mayor Gray proposed basing the inflation adjustment only on the past year's change in the price level, but the proposal had not yet become law at the time this was written.

The additional personal exemption for the blind violates the principle of horizontal equity. As stated by the Congressional Budget Office in discussing the additional federal deduction for the blind, "(N)o analogous relief is provided to deaf people or to those with other disabiltiies who confront other, similar, expenses."[318] Moroever, the additional personal exemption does not benefit blind people who have no tax liability before taking the exemption.

Additional Personal Exemption for the Blind -- 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	43	5%	$0	0%
$1 to $25,000	312	35%	$27	28%
$25,001 to $50,000	205	23%	$24	24%
$50,001 to $75,000	117	13%	$17	17%
$75,001 to $100,000	69	8%	$10	10%
$100,001 to $150,000	67	8%	$10	10%
$150,001 to $200,000	24	3%	$3	3%
Over $200,000	53	6%	$8	8%
Total	890	100%	$98	100%

[318] Congressional Budget Office, Budget Options, Vol. 2 (August 2009), p. 198.

Income Tax
Exemptions

113. Additional personal exemption for the elderly

District of Columbia Code: D.C. Official Code § 47-1806.02(e)
Sunset Date: None
Year Enacted: 1987

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$4,346	$4,670	$4,800	$4,930
Total	**$4,346**	**$4,670**	**$4,800**	**$4,930**

DESCRIPTION: All District of Columbia taxpayers may claim a personal exemption, which amounts to $1,675 for tax year 2009. An additional exemption of equal value ($1,675) is available for an elderly taxpayer (someone who has reached the age of 65 before the end of the taxable year), and another exemption is available for the elderly spouse or domestic partner of the taxpayer, provided that the spouse or partner has no gross income and is not the dependent of another taxpayer.

The District provides a larger additional exemption for the elderly than Maryland ($1,000) or Virginia ($800).[319] The federal government provides an additional standard deduction for the elderly equal to $1,450 for single filers and $1,150 for married individuals.

Although the D.C. Code provides that the exemption shall be adjusted annually to reflect changes in the cost of living,[320] in 2010 the adjustments were suspended until January 1, 2013, to help close the budget gap created by the economic recession.[321]

PURPOSE: The purpose of this provision is to reduce the tax burden of elderly taxpayers and their families. The additional exemption reflects the assumption that the elderly face additional expenses, such as medical bills, that make it harder to maintain an adequate standard of living.

IMPACT: Elderly taxpayers, as well as taxpayers with an elderly spouse or domestic partner, benefit from this provision. During tax year 2009, the exemption was claimed on behalf of 40,177 individuals, and 66 percent of the benefits (in terms of reduced tax liability) went to filers with income at or below $75,000 (see table on the next page).

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[319] Wisconsin Legislative Fiscal Bureau, p. 2.

[320] See D.C. Official Code § 47-1806.02(i).

[321] The suspension of the cost-of-living adjustments was made by Title VII-V of D.C. Law 18-111, the "Fiscal Year 2010 Budget Support Act of 2009." Under current law, once the suspension ends the exemption was to be adjusted to make up for the three years of forgone inflation adjustments. In his FY 2013 budget, Mayor Gray proposed basing the inflation adjustment only on the past year's change in the price level, but the proposal had not yet become law at the time this was written.

The additional personal exemption for the elderly violates the principle of horizontal equity. Non-elderly taxpayers with the same economic income do not receive an equivalent exemption. In discussing the additional federal standard deduction for the elderly, the Congressional Budget Office also points out that the poverty rate among the elderly is now the lowest of all age groups.[322]

Additional Personal Exemption for the Elderly -- 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	1,314	3%	$0	0%
$1 to $25,000	12,453	31%	$1,085	24%
$25,001 to $50,000	10,135	25%	$1,188	26%
$50,001 to $75,000	5,296	13%	$754	16%
$75,001 to $100,000	3,150	8%	$448	10%
$100,001 to $150,000	3,189	8%	$454	10%
$150,001 to $200,000	1,620	4%	$231	5%
$200,001 to $500,000	2,301	6%	$328	7%
Over $500,000	719	2%	$102	2%
Total	40,177	100%	$4,590	100%

[322] Congressional Budget Office, Budget Options, Vol. 2, p. 198.

Income Tax
Subtractions

114. Qualified high-technology companies: capital gains

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(Q)
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$0**	**$0**	**$0**	**$0**

DESCRIPTION: Qualified high-technology companies are allowed to exclude the capital gain from the sale or exchange of an asset held for more than five years, subject to certain limitations. Specifically, in the case of a sale or exchange of an interest in a partnership or the stock of an S corporation, the amount of the excludable capital gain may not include any gain that (1) is attributable to real property or an intangible asset which is not an integral part of the company, and (2) occurs before January 1, 2001, and after December 31, 2007.

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies. The capital gains exclusion is part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[323]

Although Maryland does not offer a comparable capital gains provision, the state provides several types of financial assistance to information and technology firms, including the Maryland Venture Fund, a state-funded seed and early-stage equity fund that has invested 60 percent of its resources in technology companies; the Challenge Investment Program, which helps "seed-stage" companies defray some of the initial costs involved in bringing new products to market; and the Enterprise Investment Fund Program, which makes direct equity investments in emerging technology companies.[324] In addition, Maryland provides tax credits for those who invest at least $25,000 in qualified Maryland biotechnology companies.

Virginia permits technology businesses to deduct long-term capital gains (as defined in federal law) from taxable income, provided that the business has gross revenues of $3 million or less in the most recent year, has its principal office in Virginia, and does at least 80 percent of its business in Virginia. Virginia also offers a Qualified Equity and Subordinated Debt Investments Credit to corporate and individual taxpayers who invest in a pre-qualified small business venture

[323] The other incentives, which include increased expensing of capital assets, a reduced corporate tax rate, employment credits, property tax abatements, sales tax exemptions, and personal property tax exemptions, are discussed later in this report.

[324] Maryland Department of Business and Economic Development, "Business in Maryland: Information & Technology," available at www.choosemaryland.org, p. 13.

that is primarily engaged in certain technology fields. Finally, Virginia authorizes localities to offer reduced user and permit fees, local tax incentives, special zoning treatment, and other benefits to qualifying firms located in designated "technology zones." Arlington County, which is the only neighboring Virginia jurisdiction to create a technology zone, offers reduced gross receipts tax rates to certain firms with 100 or more employees.[325]

PURPOSE: The purpose of the subtraction is to encourage the growth of high-technology firms in the District of Columbia and thereby expand the District's economy and employment base.

IMPACT: Qualified high-technology companies in the District of Columbia are the intended beneficiaries of this provision. Nevertheless, there have been no claimants in recent years.

[325] This information is from the Internet site of the Virginia Department of Technology (www.technology.virginia.gov), the Virginia Department of Taxation (www.tax.virginia.gov), and the Economic Development Partnership's Ally Information Exchange (www.virginiaallies.org).

Income Tax
Subtractions

115. Qualified high-technology companies: depreciable business assets

District of Columbia Code: D.C. Official Code § 47-1803.03(a)(18)
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	no estimate	no estimate	no estimate	no estimate
Personal Income Tax Loss	$0	$0	$0	$0
Total	**no estimate**	**no estimate**	**no estimate**	**no estimate**

DESCRIPTION: Qualified high-technology companies benefit from more generous rules regarding the franchise tax deduction for personal property expenses. Whereas other businesses can subtract the lesser of $25,000 or the actual cost of the property for the year the property is placed in service, a qualified high-technology company can subtract the lesser of $40,000 or the actual cost of the property for the year the property is placed in service.

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies. The expensing rules are part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[326]

Maryland and Virginia offer a variety of incentives targeted at the technology industry. Those incentives are described under tax expenditure #114, "Qualified high-technology companies: capital gains."

PURPOSE: The purpose of this provision is to encourage the growth of high-technology companies in the District of Columbia and thereby expand the District's economy and employment base.

IMPACT: High-technology companies in the District of Columbia benefit from this provision. There is no estimate of the forgone revenue because the subtraction is reported on the same line on the business tax forms as other subtractions; therefore, relevant data were unavailable. The provision violates the principle of horizontal equity because companies in other industries with similar levels of income and personal property expenses cannot subtract the same amount.

[326] The other incentives, which include the exclusion of certain capital gains, a reduced corporate tax rate, employment credits, property tax abatements, sales tax exemptions, and personal property tax exemptions, are discussed elsewhere in this section.

Income Tax
Subtractions

116. College savings plan contributions

District of Columbia Code: D.C. Official Code § 47-4501 - § 47-4512
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$881	$881	$881	$881
Total	**$881**	**$881**	**$881**	**$881**

DESCRIPTION: The District of Columbia College Savings Program allows residents to create college savings accounts to benefit from incentives provided for qualified tuition programs under section 529 of the U.S. Internal Revenue Code. Contributions to a college savings account must be spent on "qualified higher education expenses," which include tuition, fees, books, supplies, and equipment.[327] Anyone can open a college savings account on behalf of a particular child.

The earnings in a college savings account are exempt from federal income tax, as is the distribution of funds in the account to pay for qualified higher education expenses. The District of Columbia conforms to those federal rules when applying the local income tax (see tax expenditure #11, "Earnings of qualified tuition programs").

The District of Columbia also allows account owners to take a local income tax deduction of as much as $4,000 each year for single filers, or $8,000 for joint filers. If the account owner contributes more than the maximum amount in a tax year, the excess amount may be carried forward, subject to the annual limit, for five years. The estimate of forgone revenue shown above reflects the loss resulting from the local income tax deduction.

College savings plans are offered in 49 states, 34 of which offer state tax deductions or credits to those who contribute to the plans, in addition to the federal tax incentives.[328] In Maryland, a taxpayer can deduct up to $2,500 in account contributions *per* child, while in Virginia a taxpayer can deduct up to $4,000 in account contributions *per* child.

PURPOSE: The purpose of this provision to increase access to higher education by helping individuals and families save for higher education on a tax-favored basis.

IMPACT: Families and others who pay for higher education benefit from the subtraction, as do the students whose educations are financed, at least in part, by the tax-favored college savings accounts. Moreover, there may be a general benefit to society from having a more educated citizenry and productive workforce.

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[327] See Section 529(c)(3) of the Internal Revenue Code for the statutory definition of "qualified higher education expenses."

[328] National Association of State Treasurers, "College Savings Plans Network Finds Average 529 Plan Account Balance Increased 26 Percent over Twelve-Month Period," press release issued September 29, 2011, p. 2.

During tax year 2008, 2,404 tax filers claimed this subtraction. As shown in the table below, tax filers with income above $100,000 claimed 86 percent of the benefits of this provision.

Higher-income families stand to benefit more from college savings plans because they have the resources to save for college and face higher marginal tax rates that increase the value of the tax deductions and exclusions. Urban Institute researchers have questioned whether the plans have an impact on college savings because higher-income families would likely set aside funding for higher education even without the tax incentives.[329]

College Savings Program - 2008				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	11	0.5%	$0	0%
$1 to $25,000	84	3%	$11	1%
$25,001 to $50,000	141	6%	$22	2%
$50,001 to $75,000	168	7%	$40	5%
$75,001 to $100,000	202	8%	$53	6%
$100,001 to $150,000	425	18%	$133	15%
$150,001 to $200,000	364	15%	$137	15%
$200,001 to $500,000	788	33%	$378	42%
Over $500,000	221	9%	$124	14%
Total	2,404	100%	$897	100.0%

[329] Maag and Fitzpatrick, pp. 24-25.

Income Tax
Subtractions

117. Public school teacher expenses

District of Columbia Code: D.C. Official Code § 47-1803.03(b-2)
Sunset Date: None
Year Enacted: 2007

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$92	$92	$92	$92
Total	**$92**	**$92**	**$92**	**$92**

DESCRIPTION: An individual who has served as a classroom teacher in a traditional public school or a public charter school for an entire tax year may subtract the following expenses from District of Columbia gross income: (1) the amount paid for basic classroom materials and supplies needed for teaching, up to $500 per year, and (2) the amount paid as tuition and fees for post-graduate education, professional development, or licensing and certification requirements, up to $1,500 per year. If the taxpayer claimed a deduction for classroom materials and supplies, or tuition and fees on his or her federal income tax return, then those expenses may not be claimed as a deduction from District of Columbia gross income.

PURPOSE: The purpose of the subtraction is to defray the costs that teachers often absorb for classroom supplies, materials, and professional development, and to enhance the public schools' ability to recruit and retain highly qualified teachers.

IMPACT: Classroom teachers are the direct beneficiaries of the subtraction, but there may be spillover benefits for society if the provision helps public schools in the District of Columbia schools attract and retain skilled teachers. On the other hand, the subtraction may violate the principle of horizontal equity because other professionals such as child welfare workers do not receive a similar deduction. Decision-makers might also consider whether it makes more sense to pursue the policy goals through direct spending for school supplies and professional development, rather than through a tax provision.

During tax year 2008, 2,338 tax filers claimed the subtraction, which is squarely focused on middle-income earners. As shown in the table on the next page, taxpayers with incomes between $25,000 and $75,000 claimed 57 percent of the benefits for tax year 2008.

Public School Teacher Expenses - 2008				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	26	1%	$0	0%
$1 to $25,000	385	16%	$10	10%
$25,001 to $50,000	800	34%	$28	26%
$50,001 to $75,000	535	23%	$34	32%
$75,001 to $100,000	234	10%	$20	19%
$100,001 to $150,000	223	10%	$9	9%
$150,001 to $200,000	83	4%	$3	3%
Over $200,000	52	2%	$2	2%
Total	2,338	100%	$107	100%

Income Tax
Subtractions

118. Health insurance premiums paid for a same-sex spouse or domestic partner (business income tax)

District of Columbia Code: D.C. Official Code § 47-1803.03(a)(15)
Sunset Date: None
Year Enacted: 1992

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$550	$577	$606	$636
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$550**	**$577**	**$606**	**$636**

DESCRIPTION: A corporation, unincorporated business, or partnership can deduct from gross income all health insurance premiums paid on behalf of an employee's family members or a domestic partner, provided that the benefits are offered to all full-time employees who are District of Columbia residents.

In practice, this provision amounts to a local business deduction for health insurance premiums paid on behalf of a same-sex spouse or a domestic partner (the latter does not have to be a same-sex partner). Corporations and other businesses can also deduct from gross income the health insurance premiums they pay on behalf of other family members of an employee, but that deduction is provided in federal law, to which the District conforms (see tax expenditure #30, "Employer contributions for medical insurance premiums and medical care"). The federal government does not allow any deductions on behalf of same-sex spouses or domestic partners, so those deductions are based only in local law. The estimated revenue loss shown above is the cost of extending the deduction in local law to same-sex spouses and domestic partners.

D.C. law defines a "domestic partner" as a person with whom an individual maintains a committed relationship characterized by mutual caring and the sharing of a mutual residence; who is at least 18 years of age and competent to contract; who is the sole domestic partner of the other person; and is not married.

Neither Maryland nor Virginia offers employers a similar tax deduction. In March 2012, Maryland Governor Martin O'Malley signed legislation authorizing same-sex marriage, but the law had not taken effect at the time of this writing. Virginia law bans same-sex marriage and domestic partnerships among persons of the same sex.

PURPOSE: The purpose of this provision is to make the tax treatment of health insurance benefits for same-sex spouses and domestic partners (of either gender) more equitable by providing businesses with the same deduction from local business taxes that they receive for providing health benefits to other family members of an employee.

IMPACT: Businesses that pay health insurance premiums on behalf of same-sex spouses or domestic partners benefit from this provision. Same-sex spouses and domestic partners also benefit indirectly because the provision lowers the price to businesses of providing health benefits to domestic partners and therefore may increase the availability and affordability of the benefits.

Income Tax
Subtractions

119. Health insurance premiums paid for a same-sex spouse or domestic partner (personal income tax)

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(W) and § 46-401(b)
Sunset Date: None
Year Enacted: 2006

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Corporate Income Tax Impact	$0	$0	$0	$0
Personal Income Tax Impact	$56	$55	$56	$59
Total	**$56**	**$55**	**$56**	**$59**

DESCRIPTION: A taxpayer may subtract from gross income the amount of any health insurance premium paid by his or her employer for a same-sex spouse, or a domestic partner of either gender.

Individuals can also exclude from gross income the health insurance premiums that employers pay for themselves and other family members, but that deduction is provided in federal law, to which the District conforms (see tax expenditure #30, "Employer contributions for medical insurance premiums and medical care"). The federal government does not allow any tax exclusions on behalf of same-sex spouses or domestic partners, so those provisions are based only in local law. The estimated revenue loss shown above is the cost of providing the deduction to same-sex spouses and domestic partners for the D.C. personal income tax.

D.C. law defines a "domestic partner" as a person with whom an individual maintains a committed relationship characterized by mutual caring and the sharing of a mutual residence; who is at least 18 years of age and competent to contract; who is the sole domestic partner of the other person; and is not married.

Neither Maryland nor Virginia offers a similar provision. In March 2012, Maryland Governor Martin O'Malley signed legislation authorizing same-sex marriage, but the law had not taken effect as of the time of this writing. Virginia law bans same-sex marriage and domestic partnerships among persons of the same sex.

PURPOSE: The purpose of the subtraction is to promote tax equity for same-sex spouses and domestic partners, and to expand their access to health insurance. The health insurance premiums paid by employers on behalf of opposite-sex spouses or children are not counted in District of Columbia gross income as a result of federal conformity; this provision offers the same treatment to same-sex spouses and to domestic partners of either gender. The provision also makes health insurance more affordable to same-sex spouses and domestic partners .[330]

IMPACT: Same-sex spouses, domestic partners, and their families benefit from the subtraction. During tax year 2008, 380 taxpayers claimed the subtraction. Slightly more than half of the

[330] Council of the District of Columbia, Committee on Finance and Revenue, Report on Bill 16-495, the "Domestic Partner Health Care Benefits Tax Exemption Act of 2005," October 12, 2005.

benefits (in terms of reduced tax liability) were claimed by tax filers with incomes over $100,000, as shown in the table below.

Health Insurance Premiums Paid for a Same-Sex Spouse or Domestic Partner -- 2008				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	11	3%	$0	0%
$1 to $25,000	67	18%	$3	5%
$25,001 to $50,000	78	21%	$10	15%
$50,001 to $75,000	62	16%	$10	15%
75,001 to $100,000	32	8%	$8	13%
$100,001 to $150,000	54	14%	$14	22%
$150,001 to $200,000	40	11%	$8	13%
$200,001 to $500,000	31	8%	$9	15%
Over $500,000	5	1%	$1	2%
Total	380	100%	$65	100%

Income Tax
Subtractions

120. Health professional loan repayments

District of Columbia Code: D.C. Official Code § 7-751.11
Sunset Date: None
Year Enacted: 2006

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$58	$58	$58	$58
Total	**$58**	**$58**	**$58**	**$58**

DESCRIPTION: The District of Columbia Health Professional Recruitment Program was established to serve as a recruitment tool for health professionals in the District. Subject to the availability of funds, the program repays the outstanding principal, interest, and related expenses for government or commercial loans obtained by an individual for the tuition, fees, and reasonable educational expenses incurred while obtaining a health professional degree. The loan repayments made by the District government are taxable under the federal income tax, but are not considered income for purposes of District of Columbia income tax.

In return for the loan repayment, the health professional must work for at least two years and a maximum of four years at a non-profit facility located in a "health professional shortage area" or "medically underserved area" in the District of Columbia designated by the U.S. Department of Health and Human Services. The non-profit facility must offer primary care, mental health, or dental services to District of Columbia residents regardless of their ability to pay.

Physicians, dentists, and nurses are among the health professionals who are eligible to apply for the program. Participants are selected based on professional qualifications and relevant experience, professional achievements, and other indicators of competency. The Department of Health administers the program.

PURPOSE: The purpose of this provision is to "recruit community-based providers to our neediest neighborhoods by creating an incentive for those health professionals who choose to work where a health care shortage exists."[331]

IMPACT: Health professionals who agree to work in health professional shortage or medically underserved areas in the District of Columbia benefit from this provision. Low-income residents who receive health care from non-profit entities in the targeted areas should also benefit from this provision.

During tax year 2008, 100 taxpayers claimed the subtraction. As shown in the table on the next page, almost 80 percent of the benefits (in terms of reduced tax liability) flow to tax filers with income at or below $100,000.

[331] Council of the District of Columbia, Committee on Health, Report on Bill 16-420, the "District of Columbia Health Professional Recruitment Program Act of 2005," October 14, 2005, p. 1.

Health Professional Loan Repayments -- 2008				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	1	1%	$0	0%
$1 to $25,000	25	25%	$6	11%
$25,001 to $50,000	17	17%	$8	16%
$50,001 to $75,000	24	24%	$17	32%
$75,001 to $100,000	17	17%	$11	20%
$100,001 to $150,000	10	10%	$7	12%
$150,001 to $200,000	3	3%	$2	5%
Over $200,000	3	3%	$2	4%
Total	100	100%	$54	100%

Income Tax
Subtractions

121. Long-term care insurance premiums

District of Columbia Code: D.C. Official Code § 47-1803.03(b-1)
Sunset Date: None
Year Enacted: 2005

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$186	$186	$186	$186
Total	**$186**	**$186**	**$186**	**$186**

DESCRIPTION: An individual may subtract from District of Columbia gross income the amount paid annually in premiums for long-term care insurance, up to a limit of $500 per year, per individual, whether he or she is filing individually or jointly.

According to the AARP Public Policy Institute, 26 states and the District offered long-term care tax incentives as of 2007.[332] Maryland offers a long-term care insurance non-refundable credit, rather than a deduction. The credit equals the amount of premiums paid, up to a maximum of $340 for each insured person aged 40 or younger, and a maximum of $500 for each insured person aged 41 or older. Virginia offers both a non-refundable credit equal to 15 percent of long-term care insurance premiums paid during the tax year and a tax deduction for premiums paid, but taxpayers cannot claim any credits for payments that have already been deducted.

PURPOSE: The purpose of the subtraction is threefold: (1) to encourage people to purchase long-term care insurance policies, (2) to protect people's assets as they age or become disabled and rely on long-term care, and (3) to relieve a burden on the District's general fund by avoiding Medicaid expenditures for long-term care.[333]

IMPACT: Individuals purchasing long-term care insurance benefit from this provision. During tax year 2008, 4,016 tax files claimed this subtraction. As shown in the table on the next page, more than half of the benefits (54 percent) were claimed by tax filers with income of more than $100,000. Nevertheless, it is not known if beneficiaries would have purchased long-term care insurance in the absence of the subtraction, and there are no benefits for those without tax liability. In 2007, the average annual premium for long-term care insurance was $2,207, rising to $3,026 for those aged 70 or older.[334]

[332] David Baer and Ellen O'Brien, "Federal and State Income Tax Incentives for Private Long-Term Care Insurance," AARP Public Policy Institute (November 2010), pp. 9-10.

[333] Council of the District of Columbia, Committee on Finance and Revenue, Report on Bill 15-136, the "Long-Term Care Insurance Tax Deduction Act of 2004," December 6, 2004, pp. 2-3.

[334] Baer and O'Brien, p. 3.

Long-Term Care Insurance Premiums - 2008				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	40	1%	$1	0%
$1 to $25,000	365	9%	$8	5%
$25,001 to $50,000	649	16%	$21	12%
$50,001 to $75,000	625	16%	$26	14%
$75,001 to $100,000	558	14%	$25	14%
$100,001 to $150,000	811	20%	$40	22%
$150,001 to $200,000	347	9%	$20	11%
$200,001 to $500,000	520	13%	$33	18%
Over $500,000	101	3%	$6	3%
Total	4,016	100%	$182	100%

Income Tax
Subtractions

122. Housing relocation assistance

District of Columbia Code: D.C. Official Code § 47-1803.2(a)(2)(R) and § 42-2851.05
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$0**	**$0**	**$0**	**$0**

DESCRIPTION: The "Housing Act of 2002" (D.C. Law 14-114) authorizes the Mayor to provide relocation services to the tenants of a building that discontinues its participation in a federal housing assistance program. The relocation services include not only information about available housing and relevant assistance programs, but also relocation assistance payments of as much as $500 per tenant. Relocation assistance payments are excluded from the definition of District of Columbia gross income.

PURPOSE: The purpose of this exclusion is to protect low-income tenants who must leave federally-subsidized housing to find new housing.

IMPACT: Tenants receiving relocation assistance payments are the intended beneficiaries of this provision. Nevertheless, the D.C. government has never implemented the relocation assistance payments, and there are no plans to do so at this time.[335]

[335] The authorizing statute provides that, "The Mayor *may* provide relocation assistance payments of up to $500 per tenant, based on need and pursuant to regulations promulgated by the Mayor" (emphasis added). Thus, the Mayor has discretion about whether to implement the program.

Income Tax
Subtractions

123. D.C. and federal government pension income

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(N)
Sunset Date: None
Year Enacted: 1987

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$4,361	$4,305	$4,419	$4,612
Total	**$4,361**	**$4,305**	**$4,419**	**$4,612**

DESCRIPTION: Taxpayers who are 62 years of age or older may subtract from District of Columbia gross income the lesser of $3,000 or the actual amount of pension, military retired pay, or annuity income received from the District of Columbia or the federal government during the tax year. In order for an individual to qualify for this benefit, his or her pension, military retired pay, or annuity must otherwise be subject to the D.C. income tax.

Maryland provides a pension exclusion (which covers federal, state, local, military, and private pensions) equal to $26,300 minus Social Security and railroad retirement benefits for tax year 2011. Virginia does not provide a pension exclusion, but rather provides a broader "age deduction" of $12,000 for single filers and $24,000 for married couples filing jointly. Virginia's age deduction is phased out beginning at income levels of $50,000 for single taxpayers and $75,000 for married couples regardless of filing status.[336]

PURPOSE: The purpose of the subtraction is to shield from taxation a portion of the pension income earned by the elderly through public employment, thereby enhancing the economic self-sufficiency of senior citizens on fixed incomes.

IMPACT: Taxpayers aged 62 or older who have District of Columbia or federal pension income benefit from this provision. During tax year 2009, 15,894 tax filers claimed this subtraction. As shown in the table on the next page, the bulk of the benefits (71 percent) were claimed by tax filers with income of $75,000 or less.

The subtraction of federal and D.C. government pension income violates the principle of horizontal equity, because those with private pension income do not receive the same exclusion.

[336]These data are from National Conference of State Legislatures, "State Personal Income Taxes on Pensions and Retirement Income: Tax Year 2010" (February 2011), available at www.ncsl.org.; http://individuals.marylandtaxes.com; and www.tax.virginia.gov.

D.C. and Federal Government Pension Income -- 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	363	2%	$45	1%
$1 to $25,000	4,773	30%	$752	21%
$25,001 to $50,000	4,910	31%	$1,099	31%
$50,001 to $75,000	2,309	15%	$655	18%
$75,001 to $100,000	1,278	8%	$390	11%
$100,001 to $150,000	1,117	7%	$331	9%
$150,001 to $200,000	482	3%	$145	4%
$200,001 to $500,000	575	4%	$162	4%
Over $500,000	87	1%	$24	1%
Total	15,894	100%	$3,603	100%

Income Tax
Subtractions

124. D.C. and federal government survivor benefits

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(N)
Sunset Date: None
Year Enacted: 1987

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,928	$3,877	$3,980	$4,154
Total	**$3,928**	**$3,877**	**$3,980**	**$4,154**

DESCRIPTION: Taxpayers may exclude from their District of Columbia taxable income the amount of any survivor benefits they received from the D.C. government or federal government if they are 62 years of age or older by the end of the tax year. Neither Maryland nor Virginia has an income exclusion for survivor benefits.

This provision does not affect Social Security survivor benefits, which are excluded from taxation under another provision of D.C. law (see tax expenditure # 129, "Social Security benefits for survivors and dependents").

PURPOSE: The purpose of the exclusion is to promote income security among elderly survivors of D.C. government or federal government workers by shielding their benefits from taxation.

IMPACT: Individuals over the age of 62 who are receiving survivor benefits from the D.C. government or federal government benefit from this provision. In 2009, 2,706 tax filers claimed this subtraction. The bulk of the benefits (77 percent) of the benefits were claimed by filers with income at or below $50,000, as shown in the table on the next page.

The exclusion of federal and D.C. government survivor benefits violates the principle of horizontal equity, because those with private-sector survivors' benefits do not receive the same exclusion.

D.C. and Federal Government Survivor Benefits -- 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	363	13%	$276	10%
$1 to $25,000	1271	47%	$1,098	40%
$25,001 to $50,000	689	25%	$759	27%
$50,001 to $75,000	211	8%	$324	12%
75,001 to $100,000	67	2%	$126	5%
$100,001 to $150,000	63	2%	$113	4%
$150,001 to $200,000	25	1%	$40	1%
$200,001 to $500,000	15	1%	$23	1%
Over $500,000	2	0%	$3	0%
Total	2,706	100%	$2,762	100%

Income Tax
Subtractions

125. Disability payments for the permanently and totally disabled

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(M)
Sunset Date: None
Year Enacted: 1985

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$72	$71	$73	$76
Total	**$72**	**$71**	**$73**	**$76**

DESCRIPTION: Taxpayers may exclude from adjusted gross income up to $5,200 in disability payments, provided that (1) they were permanently and totally disabled when they retired, (2) they had not reached the age required to retire under their employer's regular (non-disability) retirement program as of the first day of the taxable year, and (3) their other income was less than $15,000.

This provision does not apply to Social Security disability benefits, which are are excluded from taxation under another provision of D.C. law (see tax expenditure # 130, "Social Security benefits for the disabled").

Virginia allows permanently and totally disabled taxpayers to exclude up to $20,000 in disability plan income. Virginia taxpayers who claim the state's age deduction for those over the age of 62 are not eligible for the exclusion.

PURPOSE: The purpose of the subtraction is to maintain in D.C. law a provision of the U.S. Internal Revenue Code that was abolished by the Social Security Amendments of 1983, thereby maintaining a tax benefit to certain individuals with disability income.[337]

IMPACT: Permanently and totally disabled individuals who receive disability payments, are not eligible for their employer's regular retirement plan, and meet the income standards benefit from this provision. In tax year 2008, 126 taxpayers claimed the subtraction.

Because of the income limit, the subtraction assists only low-income individuals and households. At the same time, the real value of the benefit has declined over time because the amount that can be excluded ($5,200) and the limitation on other income ($15,000) have not been adjusted for inflation or income growth.

[337] Specifically, the federal government replaced a disability income exclusion with a new credit for the permanently and totally disabled. Because a credit is not automtically mirrored in the D.C. income tax system, D.C. policymakers apparently decided to retain the disability income exclusion in local law.

Income Tax
Subtractions

126. Income of persons with a permanent and total disability

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(V)
Sunset Date: None
Year Enacted: 2005

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$457	$451	$463	$484
Total	**$457**	**$451**	**$463**	**$484**

DESCRIPTION: A taxpayer who has been determined to have a permanent and total disability by the U.S. Social Security Administration may exclude up to $10,000 from District of Columbia gross income, if he or she (1) is receiving Supplemental Security Income or Social Security Disability, railroad retirement disability, or federal or District of Columbia government disability payments, and (2) has a household adjusted gross income of less than $100,000.

PURPOSE: The purpose of this exclusion is to provide income support to people who cannot work due to a permanent and total disability.

IMPACT: People with a permanent and total disability benefit from this provision. During tax year 2008, 680 taxpayers claimed this subtraction. As shown in the table below, the benefits accrue almost entirely to low- and moderate-income taxpayers: 85 percent of the benefits were claimed by taxpayers with income of $50,000 or less.

Income of Persons with a Total and Permanent Disability -- 2008				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	136	20%	$46	15%
$1 to $25,000	308	45%	$133	42%
$25,001 to $50,000	159	23%	$90	28%
$50,001 to $75,000	61	9%	$40	13%
Over $75,000	16	2%	$8	2%
Total	680	100%	$318	100%

Income Tax
Subtractions

127. Railroad retirement system benefits

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(L)
Sunset Date: None
Year Enacted: 1985

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$82	$81	$83	$87
Total	**$82**	**$81**	**$83**	**$87**

DESCRIPTION: The District of Columbia exempts all railroad retirement benefits from the local income tax, a policy that goes beyond the federal policy of exempting a portion of railroad retirement benefits from the federal income tax (see tax expenditure #49, "Social Security and Railroad Retirement benefits"). Maryland and Virginia also exempt all railroad retirement benefits from income tax. The estimate of forgone revenue shown above represents the incremental revenue loss resulting from the District's decision to exempt the railroad retirement benefits that are subject to federal taxation.

At the federal level, the amount of railroad retirement benefits equivalent to the benefit that a retiree would have received under the Social Security system is taxable in the same way that Social Security benefits are taxed.

PURPOSE: The purpose of the subtraction is to help protect railroad retirement benefits as a source of income support, and to ensure equitable tax treatment of railroad retirement and Social Security benefits. Under D.C. law, all Social Security benefits are also exempt from the local income tax (see tax expenditure #128, "Social Security benefits for retired workers").

IMPACT: Individuals receiving railroad retirement payments benefit from this subtraction. According to the Railroad Retirement Board, in the District of Columbia there are approximately 500 current beneficiaries of the railroad retirement program, who receive average benefits of $565 per month.[338]

Because D.C. taxpayers report their railroad retirement and Social Security income on the same line of the income tax form, there are no data on the railroad retirement subtraction by income level.

[338] U.S. Railroad Retirement Board, "Table B27: Retirement and Survivor Benefits in Current-Payment Status on September 30, 2010, by Class and State," available at www.rrb.gov.

Income Tax
Subtractions

128. Social Security benefits for retired workers

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(L)
Sunset Date: None
Year Enacted: 1985

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$14,763	$14,574	$14,959	$15,613
Total	**$14,763**	**$14,574**	**$14,959**	**$15,613**

DESCRIPTION: The District exempts all Social Security benefits from taxation, a policy that is more generous than the federal treatment of Social Security benefits (see tax expenditure #49, "Social Security and Railroad Retirement Benefits"). Under federal law, between 50 and 85 percent of the Social Security benefits of taxpayers whose "provisional income" is $25,000 or more for single filers and $32,000 or more for joint filers are subject to federal income tax. Provisional income consists of federal adjusted gross income, tax-exempt interest, some foreign-source income, and one-half of Social Security benefits.

The estimate of forgone revenue shown above represents the incremental revenue loss resulting from the District's decision to exempt the Social Security benefits of retired workers that are subject to federal taxation.

There are 27 other states that provide a full exemption of Social Security benefits from taxation,[339] including Maryland and Virginia.[340]

PURPOSE: The purpose of the subtraction is to shield Social Security benefits from taxation and ensure that Social Security provides adequate income support to the elderly during their retirement.

IMPACT: Retired Social Security recipients benefit from this provision. Because D.C. taxpayers report railroad retirement and all types of Social Security income (for retirees, survivors and dependents, and the disabled) on the same line of the income tax form, there are no data on the subtraction for Social Security retirement benefits by income level.

The table on the following page shows the aggregate distribution of Social Security *and* railroad retirement subtractions by income group. Nevertheless, because almost two-thirds of the Social Security recipients in the District are retired workers[341] and the number of railroad retirement

[339] Joseph Cordes and Jason Juffras, "State Personal Income Taxes," in *The Oxford Handbook of State and Local Finance* (Oxford: Oxford University Press, 2012), p. 317.

[340] Wisconsin Legislative Fiscal Bureau, pp. 32, 55.

[341] U.S. Social Security Administration, OASDI Beneficiaries by State and County, 2010 (Washington, D.C.: June 2011), SSA Publication No. 13-11954, p. 2.

beneficiaries in the District is small (approximately 500), the distribution suggests that taxpayers with incomes of $100,000 or less claim the bulk of the benefits of the subtraction.

Social Security and Railroad Retirement Benefits -- 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	267	1%	$109	1%
$1 to $25,000	3798	18%	$872	5%
$25,001 to $50,000	6985	33%	$4,301	23%
$50,001 to $75,000	3389	16%	$3,796	20%
75,001 to $100,000	1962	9%	$2,453	13%
$100,001 to $150,000	1945	9%	$2,774	15%
$150,001 to $200,000	917	4%	$1,485	8%
$200,001 to $500,000	1296	6%	$2,387	13%
Over $500,000	381	2%	$780	4%
Total	20,940	100%	$18,957	100%

Note: The table shows the income levels of Social Security beneficiaries (old-age, survivors and dependents, and disaiblity benefits) as well as Railroad Retirement beneficiaries in 2009. Approximately two-thirds of these beneficiaries are Social Security old-age (retired worker) beneficiaries.

Income Tax
Subtractions

129. Social Security benefits for survivors and dependents

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(L)
Sunset Date: None
Year Enacted: 1985

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$2,074	$2,047	$2,101	$2,193
Total	**$2,074**	**$2,047**	**$2,101**	**$2,193**

DESCRIPTION: The District exempts all Social Security benefits from taxation, a policy that is more generous than the federal treatment of Social Security benefits. Under federal law, between 50 and 85 percent of the Social Security benefits of taxpayers whose "provisional income" is $25,000 or more for single filers and $32,000 or more for joint filers are subject to federal income tax. Provisional income consists of federal adjusted gross income, tax-exempt interest, some foreign-source income, and one-half of Social Security benefits.

The estimate of forgone revenue shown above represents the incremental revenue loss resulting from the District's decision to exempt the Social Security benefits of survivors and dependents that are subject to federal taxation.

There are 27 other states that provide a full exemption of Social Security benefits from taxation,[342] including Maryland and Virginia.[343]

PURPOSE: The purpose of the exclusion is to shield Social Security benefits from taxation and ensure that Social Security provides adequate income support to dependents and survivors.

IMPACT: Survivors and dependents who receive Social Security benefit from this provision. Because D.C. taxpayers report railroad retirement and all types of Social Security income (for retirees, survivors and dependents, and the disabled) on the same line of the income tax form, there are no data on the subtraction for Social Security survivors' and dependents' benefits by income level.

[342] Cordes and Juffras, p. 317.

[343] Wisconsin Legislative Fiscal Bureau, pp. 32, 55.

Income Tax
Subtractions

130. Social Security benefits for the disabled

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(L)
Sunset Date: None
Year Enacted: 1985

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$3,614	$3,567	$3,662	$3,822
Total	**$3,614**	**$3,567**	**$3,662**	**$3,822**

DESCRIPTION: The District exempts all Social Security benefits from taxation, a policy that is more generous than the federal treatment of Social Security benefits. Under federal law, between 50 and 85 percent of the Social Security benefits of taxpayers whose "provisional income" is $25,000 or more for single filers and $32,000 or more for joint filers are subject to federal income tax. Provisional income consists of federal adjusted gross income, tax-exempt interest, some foreign-source income, and one-half of Social Security benefits.

The estimate of forgone revenue shown above represents the incremental revenue loss resulting from the District's decision to exempt the Social Security disability benefits that are subject to federal taxation.

There are 27 other states that provide a full exemption of Social Security benefits from taxation,[344] including Maryland and Virginia.[345]

PURPOSE: The purpose of the exclusion is to shield Social Security benefits from taxation and ensure that Social Security provides adequate income support to the disabled.

IMPACT: Disabled Social Security recipients benefit from this provision. Because D.C. taxpayers report railroad retirement and all types of Social Security income (for retirees, survivors and dependents, and the disabled) on the same line of the income tax form, there are no data on the subtraction for Social Security disability benefits by income level.

[344] Cordes and Juffras, p. 317.

[345] Wisconsin Legislative Fiscal Bureau, pp. 32, 55.

Income Tax
Subtractions

131. Environmental savings account contributions and earnings

District of Columbia Code: D.C. Official Code § 8-637.03
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	minimal	minimal	minimal	minimal
Personal Income Tax Loss	minimal	minimal	minimal	minimal
Total	**minimal**	**minimal**	**minimal**	**minimal**

Note: "Minimal" means that the forgone revenue is estimated as less than $50,000 per year, although precise data are lacking.

DESCRIPTION: An individual, partnership, corporation, trust, or government agency may establish an environmental savings account (ESA) in order to accumulate funds for the cleanup or redevelopment of brownfields, which are defined as "abandoned, idled property or industrial property where expansion or redevelopment is complicated by actual or perceived environmental contamination."[346] Funds deposited in an ESA, and the interest earned on the funds, are exempt from District of Columbia income tax. Any funds that are withdrawn and not used for the cleanup and redevelopment of a contaminated property will be subject to the income tax and a 10 percent penalty.

A review did not identify similar income tax incentives offered by Maryland or Virginia, but Maryland authorizes local governments to provide property tax credits equal to 50 to 70 percent of the increase in property taxes for property owners who participate in the state's Voluntary Cleanup Program. The tax credits may be granted for five years, or 10 years if the property is in an enterprise zone. Montgomery County and Baltimore City are among the jurisdictions that offer the property tax credits.

PURPOSE: The purpose of this subsidy is to provide incentives for individuals and organizations to clean up brownfields voluntarily, which would in turn reduce public health risks and promote economic development by encouraging the reuse of contaminated properties.

IMPACT: Owners of property that is contaminated by hazardous substances may benefit from this provision. This tax provision is claimed on a line of the tax form that includes other items; therefore no precise estimate of this provision is possible. Discussions with officials in the D.C. Department of the Environment and environmental advocacy groups did not reveal any evidence that environmental savings accounts are being used. Therefore, the revenue loss for fiscal years 2012 through 2015 is characterized as "minimal" (less than $50,000 per year).

[346] See D.C. Official Code § 8-631.02(2).

Income Tax
Subtractions

132. Rental assistance to police officers

District of Columbia Code: D.C. Official Code § 42-2902
Sunset Date: None
Year Enacted: 1993

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	minimal	minimal	minimal	minimal
Total	**minimal**	**minimal**	**minimal**	**minimal**

Note: "Minimal" means that the forgone revenue is estimated as less than $50,000 per year, although precise data are lacking.

DESCRIPTION: Metropolitan Police Department (MPD) officers are eligible to participate in the "Police and Landlords for Unity and Safety" (PLUS) program, which provides officers who live in the District of Columbia with discounted rent from public and private housing providers.

The D.C. Housing Authority (DCHA) is required by law to offer public housing units at a discounted rent to MPD officers, with priority given to officers who already live in the District. In addition, MPD officers may receive discounted rent from private housing providers. The discounted rent received by an MPD officer is not counted as income in calculating District of Columbia income tax liability.

Any officer who receives discounted rent must notify the Chief of Police of the terms of the discount, and provide a copy of the lease or written agreement detailing the terms of the housing rental to the Chief of Police.

PURPOSE: The purpose of this provision is to encourage MPD officers to live in the District of Columbia, particularly in public housing, and thereby promote safety and security in the communities where they live.

IMPACT: MPD officers, and the communities where they reside, are the intended beneficiaries of this provision. According to DCHA, one MPD officer is living at a DCHA property and receiving discounted rent, but no data were available on the number of officers receiving the benefit at private properties.

The estimated revenue loss is minimal (less than $50,000 per year) because in most cases the discounted rent would not be taxable even without the explicit subtraction. The federal definition of taxable income (which is also used by the District except for specific cases in which the District "decouples" from the federal definition) requires taxpayers to report discounted rent as income only when the renter is providing a particular good or service in return.[347] Therefore, police officers receiving discounted rent would not ordinarily be required to declare the discount as income unless they were providing security or other services to the landlord. The PLUS program does not require that police officers perform any duties in return for the discounted rent.

[347] See Internal Revenue Service Publication 525, "Taxable and Nontaxable Income," January 1, 2012.

Income Tax
Subtractions

133. Compensatory damages awarded in a discrimination case

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(U) and § 47-1806.10
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$25	$25	$26	$27
Total	**$25**	**$25**	**$26**	**$27**

DESCRIPTION: A taxpayer may exclude from District of Columbia gross income a court award intended to compensate him or her for the pain and suffering associated with unlawful employment discrimination. The exclusion does not apply to back pay, front pay (future wages), or punitive damages.[348]

PURPOSE: The purpose of the subtraction is to preserve the full value of the awards that are intended to compensate individuals for the pain and suffering associated with unlawful employment discrimination.

IMPACT: Individuals who have won an employment discrimination suit or received a monetary settlement of an employment discrimination claim benefit from this provision. During tax year 2008, 31 tax filers claimed the subtraction. More than half (16) of the claimants had a D.C. adjusted gross income above $100,000, while only four claimants had income of $50,000 or less, perhaps because higher-income households can more easily afford the legal representation needed to pursue a discrimination case successfully.

[348] D.C. law provides that damages pertaining to back pay and front pay are to be averaged over the period of back and future wages involved. This spreading of back pay and front pay protects the taxpayers from having to pay a large lump sum in taxes in one year, and avoids the perverse result in which a taxpayer could be pushed into a higher tax bracket due to the award of back pay and front pay.

Income Tax
Subtractions

134. Poverty lawyer loan assistance

District of Columbia Code: D.C. Official Code § 47-1803.02(a)(2)(X)
Sunset Date: None
Year Enacted: 2007

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$33	$33	$33	$33
Total	**$33**	**$33**	**$33**	**$33**

DESCRIPTION: Loans that are awarded and subsequently forgiven through the District of Columbia Poverty Lawyer Loan Assistance Repayment Program (LRAP) can be excluded from District of Columbia gross income.

LRAP is intended to encourage law students and attorneys to practice in areas of civil law deemed to serve the public interest. Participants who practice law in the designated areas, live in the District of Columbia, have an annual adjusted gross income of less than $65,000, and exhaust all other loan assistance opportunities, can receive loans to repay the debt incurred while obtaining their law degree. The loans are forgiven when the participant completes the service obligation, which requires at least 45 weeks of work within any 12-month period for which the participant applies for assistance

During FY 2012, the District of Columbia Bar Foundation is designated by law as the program administrator. In subsequent years, the Deputy Mayor for Public Safety and Justice may serve as program administrator or designate a non-profit entity to administer the program.

PURPOSE: The purpose of this substraction is to encourage attorneys to enter public-interest work and thereby expand access to legal services for low-income residents.

IMPACT: LRAP participants benefit from this provision, as do the organizations and clients who receive legal services from the participants. During tax year 2008, 44 tax filers claimed the subtraction.

Income Tax
Credits

135. Economic development zone incentives for businesses

District of Columbia Code:	D.C. Official Code § 6-1501, § 6-1502, § 6-1504, and § 47-1807.06
Sunset Date:	None
Year Enacted:	1988

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$0**	**$0**	**$0**	**$0**

DESCRIPTION: D.C. law designates three economic development zones that are eligible for tax and other development incentives: the Alabama Avenue zone, the D.C. Village zone, and the Anacostia zone. The Mayor may also designate additional economic development zones (subject to Council approval), based on evidence of economic distress such as high levels of poverty, high levels of unemployment, low income, population loss, and other criteria set forth in the law.

A business entity that is located within an economic development zone is eligible for corporate franchise tax credits or unincorporated business franchise tax credits if (1) the business has signed a "First Source" agreement with the D.C. government setting the goal that 51 percent of new hires shall be D.C. residents, and (2) the business is subject to the D.C. franchise tax.

The available credits include (1) a credit equal to 50 percent of wages paid to low-income workers who are D.C. residents, up to a maximum of $7,500 per employee per year, (2) a credit equal to 50 percent of the workers' compensation premiums paid on behalf of workers who are D.C. residents, and (3) a rent credit for businesses that rent space to a non-profit child care center. The value of the rent credit is equal to the difference between the fair market value for the space and the actual rent charged to the child care center. If the rent credit exceeds the tax liability of a business, it can carry the credit backward or forward for up to five years.

The Mayor must submit and the Council must approve a resolution that qualifies the business for the incentives. The resolution must identify the business, specify the types of incentives to be granted, and estimate the annual dollar value of each franchise tax credit.

The federal government has also established an enterprise zone in the District of Columbia, which provides businesses operating in the zone with federal wage tax credits, expensing and capital gains tax benefits, and tax-exempt bond financing.

Maryland provides income tax credits for each new worker hired by a business in any of 29 enterprise zones and also authorizes localities to offer real property tax credits to businesses located in a zone.[349] Business that locate in the Baltimore City or Prince George's County zones

[349] The income tax credits are $1,000 for each new worker but the credit rises to $6,000 over three years if the worker is "economically disadvantaged." The real property tax credits are applied to a percentage of the taxes due on any expansion, renovation, or capital improvement; the percentage decreases over a period of 10 years.

are eligible for larger property and income tax credits, as well as personal property tax credits. Virginia is phasing out the tax credits provided under its enterprise zone program and replacing them with grants.[350]

PURPOSE: The purpose of the incentives is to promote conomic development in neighborhoods in economic distress, and to increase the employment of low-income D.C. residents.

IMPACT: Businesses located in an economic development zone are eligible to benefit from these incentives, as are low-income residents. Nevertheless, only two incentive packages have been approved since the economic development zones were created, and neither package included business tax incentives (both packages included real property tax incentives).

[350] Virginia Department of Housing and Community Development, Virginia Enterprise Zones: 2010 Qualification Year Annual Report, available from www.dhcd.virginia.gov, pp. 506.

Income Tax
Credits

136. Qualified high-technology companies: business income tax reduction

District of Columbia Code: D.C. Official Code § 47-1817.06
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Business Income Tax Loss	$5,144	$5,305	$5,396	$5,646
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$5,144**	**$5,305**	**$5,396**	**$5,646**

DESCRIPTION: High-technology companies are eligible for a credit that reduces the marginal business tax rate from 9.975 percent (the standard business tax rate) to 6 percent.

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies. The lower corporate tax rate is part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[351]

Neither Maryland nor Virginia offers a comparable business tax reduction, but each state offers an array of incentives to technology firms which are described under tax expenditure #114, "Qualified high-technology companies: capital gains."

PURPOSE: The purpose of the credit is to encourage high-technology companies to locate, expand, and remain in the District of Columbia, thereby strengthening the District's employment and economic base.

IMPACT: Qualified high-technology companies benefit from the tax credit, although there could also be spillover benefits in terms of greater employment and business activity. In tax year 2009, 114 companies qualified for the credit. The credit violates the principle of horizontal equity because firms in other industries with equivalent levels of income do not receive similar tax relief.

[351] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, employment credits, property tax abatements, sales tax exemptions, and personal property tax exemptions, are discussed elsewhere in this section.

Income Tax
Credits

137. Qualified high-technology companies: employee relocation incentives

District of Columbia Code: D.C. Official Code § 47-1817.02
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$3,470	$3,578	$3,640	$3,809
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$3,470**	**$3,578**	**$3,640**	**$3,809**

Note: The estimated revenue loss shown above results not only from the employee relocation credits, but also from three additional credits for high-technology companies (see tax expenditures #138 – #140).

DESCRIPTION: A qualified high-technology company[352] is authorized to claim corporate tax credits for the relocation costs paid to, or on behalf of, a qualified employee[353] to reimburse actual moving expenses, to assist in financing the purchase of a home, or pay for the required security deposit or lease payments for the first year of a lease. The credit may not exceed $5,000 per taxable year for each employee relocated to the District from another state, or $7,500 per taxable year for each employee relocated to the District from another state if the employee also relocates his or her principal residence into the District.

A company may not claim the credit until it has relocated at least two qualified employees and employed them for at least six months in the District. The credit is not available for employees who work less than 35 hours per week, and the company may not claim the credit if it has claimed a deduction for the relocation costs. If the amount of the credit exceeds the amount otherwise due, a company may carry forward the unused amount of the credit for 10 years.

The employment relocation credits are part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[354]

PURPOSE: The purpose of the credit is to encourage high-technology companies to relocate, expand, and stay in the District of Columbia by ensuring that they can relocate key employees. In

[352] A qualified high-technology company must derive at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies.

[353] A qualified employee is someone who is employed in the District of Columbia by a high-technology company.

[354] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, property tax abatements, sales tax exemptions, and personal property tax exemptions, are discussed elsewhere in this section.

turn, the growth of the high-technology industry is intended to strengthen the District's economic and employment base.

IMPACT: High-technology companies, and their employees who relocate to the District of Columbia, benefit from this provision. There may also be spillover benefits in terms of greater employment and business activity. However, the credit violates the principle of horizontal equity because firms in other industries with equivalent levels of income are not eligible for similar tax relief.

The estimate of forgone revenue shown on the previous page reflects not only the reduced tax due to the relocation credits, but also the revenue loss from three other credits for high-technology companies (see tax expenditures #138-#140). The four credits are combined on Line 2 of Schedule UB, "Business Credits." Therefore, the revenue loss attributable to each provision is not known.

Income Tax
Credits

138. Qualified high-technology companies: employment incentives

District of Columbia Code: D.C. Official Code § 47-1817.03
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	included in #137	included in #137	included in #137	included in #137
Personal Income Tax Loss	$0	$0	$0	$0
Total	**included in #137**	**included in #137**	**included in #137**	**included in #137**

DESCRIPTION: A qualified high technology company is allowed a credit against its corporate franchise tax liability equal to 10 percent of the wages paid during the first 24 calendar months of employment to a qualified employee hired after December 31, 2000. The credit for each qualified employee shall not exceed $5,000 per taxable year. If the credit exceeds the amount of tax otherwise due from a high-technology company, the unused amount of the credit may be carried forward for 10 years.

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies. A qualified employee is a person who is employed in the District of Columbia by a qualified high-technology company.

The employment credits are part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[355]

Maryland offers a job creation tax credit as well as tax credits for hiring ex-offenders, but these incentives are not specific to the high-technology sector (or any other sector). Virginia provides a major business facility tax credit for firms that create at least 50 new jobs (25 new jobs for firms in economically distressed areas or enterprise zones) relative to a base year, as well as a green job creation tax credit and a clean fuel vehicle job creation tax credit, but once again, the incentives are not targeted specifically at the high-technology sector.

PURPOSE: The purpose of the credit is to encourage the growth of high-technology industries and high-technology employment in the District of Columbia, and thereby strengthen the District's economic base.

[355] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, property tax abatements, sales tax exemptions, and personal property tax exemptions, are discussed elsewhere in this section.

IMPACT: High-technology companies in the District of Columbia benefit from this provision. There may also be spillover benefits in terms of greater employment and business activity. However, the credit violates the principle of horizontal equity because firms in other industries with equivalent levels of income are not eligible for similar tax relief.

There is no estimate on the previous page of the revenue loss specifically due to this provision because companies combine this credit with three other credits (see tax expenditures #137, #139, and #140) on Line 2 of Schedule UB, “Business Credits.” Therefore, the revenue loss attributable to each provision is not known.

Income Tax
Credits

139. Qualified high-technology companies: incentives to employ disadvantaged workers

District of Columbia Code: D.C. Official Code § 47-1817.05
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Business Income Tax Loss	included in #137	included in #137	included in #137	included in #137
Personal Income Tax Loss	$0	$0	$0	$0
Total	**included in #137**	**included in #137**	**included in #137**	**included in #137**

DESCRIPTION: A qualified high technology company may take credits against its franchise tax liability equal to 50 percent of the wages paid to a qualified disadvantaged employee during the first 24 calendar months of employment. The credit may not exceed $15,000 in a taxable year for each disadvantaged employee, and the credit is not allowable if the company "accords the qualified employee lesser benefits or rights than it accords other employees in similar jobs." If the amount of the allowable credit exceeds the tax otherwise due, the company may carry forward the unused amount of the credit for 10 years.

A qualified disadvantaged employee refers to a District of Columbia resident who is receiving benefits from the Temporary Assistance to Needy Families (TANF) program; was a recipient of TANF in the period immediately preceding employment; was released from incarceration within 24 months of being hired by a qualified high-technology company; or qualifies for the Welfare-to-Work Tax Credit or the Work Opportunity Tax Credit under the U.S. Internal Revenue Code.

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies. The employment credits are part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[356]

Maryland offers tax credits to employers who hire ex-offenders, but this incentive is not specific to the high-technology sector (or to any other sector). Virginia provides a tax credit of up to $750 for hiring TANF recipients (for businesses with 100 employees or less), but once again the incentive is not limited to the high-technology sector.

[356] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, property tax abatements, sales tax exemptions, and personal property tax exemptions, are discussed elsewhere in this section.

PURPOSE: The purpose of this tax abatement is to encourage high-technology companies to employ and retain disadvantaged workers.

IMPACT: Disadvantaged workers in the District of Columbia benefit from this tax credit, as do high-technology companies that employ the workers. However, the credit violates the principle of horizontal equity because firms in other industries with equivalent levels of income are not eligible for similar tax relief.

There is no estimate on the previous page of the revenue loss specifically due to this provision because companies combine this credit with three other credits (see tax expenditures #137, #138, and #140) on Line 2 of Schedule UB, "Business Credits." Therefore, the revenue loss attributable to each provision is not known.

Income Tax
Credits

140. Qualified high-technology companies: incentives to retrain disadvantaged workers

District of Columbia Code: D.C. Official Code § 47-1817.04
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	included in #137	included in #137	included in #137	included in #137
Personal Income Tax Loss	$0	$0	$0	$0
Total	**included in #137**	**included in #137**	**included in #137**	**included in #137**

DESCRIPTION: A qualified high technology company may take a credit against its franchise tax liability for the expenditures paid or incurred during the taxable year for retraining a qualified disadvantaged employee. The credit cannot exceed $20,000 for each qualified disadvantaged worker during the first 18 months of employment. If the credit exceeds the amount of tax otherwise due from the company, the unused amount of the credit may be carried forward for 10 years, or can be taken as a refundable credit in an amount up to 50 percent of the credit.

A qualified disadvantaged employee refers to a District of Columbia resident who is receiving benefits from the Temporary Assistance to Needy Families (TANF) program; was a recipient of TANF in the period immediately preceding employment; was released from incarceration within 24 months of being hired by a qualified high-technology company; or qualifies for the Welfare-to-Work Tax Credit or the Work Opportunity Tax Credit under the U.S. Internal Revenue Code.

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies. The retraining credits are part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[357]

Virginia provides a worker retraining tax credit of up to 30 percent of the costs of non-credit courses at an in-state community college or private school,[358] but the incentive is not targeted at the high-technology sector. Maryland does not provide tax incentives for worker retraining.

PURPOSE: The purpose of the credit is to encourage high-technology companies to invest in the skills of disadvantaged workers and, thereby, to help disadvantaged workers attain better jobs with higher wages and more potential for advancement within the high-technology sector.

[357] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, property tax abatements, sales tax exemptions, and personal property tax exemptions, are discussed elsewhere in this section.

[358] Virginia limits the credit to $100 per student annually for classes taken at a private school.

IMPACT: Disadvantaged workers in the District of Columbia benefit from this tax credit, as do high-technology companies that employ the workers. However, the credit violates the principle of horizontal equity because firms in other industries with equivalent levels of income are not eligible for similar tax relief.

There is no estimate on the previous page of the revenue loss specifically due to this provision because companies combine this credit with three other credits (see tax expenditures #137, #138, and #139) on Line 2 of Schedule UB, "Business Credits." Therefore, the revenue loss attributable to each provision is not known.

Income Tax
Credits

141. First-time home purchase for D.C. government employees

District of Columbia Code: D.C. Official Code § 42-2506
Sunset Date: None
Year Enacted: 2000

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$116	$116	$116	$116
Total	**$116**	**$116**	**$116**	**$116**

DESCRIPTION: District government employees and public charter school employees, as well as individuals who have accepted an offer to serve as a District of Columbia police officer, firefighter, emergency medical technician, public school teacher, or public charter school teacher, are eligible for a $2,000 income tax credit in the year that they buy a home in the District and the following four years. To receive the credit, the individual must be a first-time homebuyer in the District and remain a District of Columbia resident. Any portion of the credit that is not used in a tax year cannot be carried forward, carried back, or refunded.

When first-time homebuyer credits were first authorized in 2000, only police officers were eligible, but the law was amended in 2007 to include the other groups of employees listed above.

PURPOSE: The purpose of the credit is to aid in the recruitment and retention of highly qualified employees (particularly teachers, police officers, firefighters, and emergency medical technicians); to strengthen the District of Columbia's economic and tax base; and to encourage employees to live in the District and become engaged in its civic and neighborhood life.

IMPACT: District government employees, as well as individuals who have accepted an offer to serve as a District of Columbia police officer, firefighter, emergency medical technician, or teacher, benefit from this tax credit. As noted above, there may also be spillover benefits for District of Columbia neighborhoods and the District economy. The credit violates the principle of horizontal equity because only some groups of new homebuyers are eligible.

During tax year 2009, 58 tax filers claimed the credit. As shown in the table on the next page, the benefits were concentrated on middle-income households. Tax filers with incomes from $25,001 to $75,000 claimed 62 percent of the benefits.

First-Time Home Purchase for D.C. Government Employees -- 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	0	0%	$0	0%
$1 to $25,000	5	9%	$10	9%
$25,001 to $50,000	17	29%	$34	29%
$50,001 to $75,000	19	33%	$38	33%
$75,001 to $100,000	7	12%	$14	12%
$100,001 to $150,000	8	14%	$16	14%
$150,001 to $200,000	1	2%	$2	2%
Over $200,000	1	2%	$2	2%
Total	58	100%	$116	100%

Income Tax
Credits

142. Job growth tax credit

District of Columbia Code: D.C. Official Code § 47-1807.09, § 47-1807.51 - § 47-1807.56
Sunset Date: January 1, 2030
Year Enacted: 2010

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$158	$399	$721
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$0**	**$158**	**$399**	**$721**

DESCRIPTION: The Mayor has the authority to issue job growth tax tax credits against the franchise tax for business projects[359] that meet the following criteria: (1) add at least 10 net new jobs in the District of Columbia with an average yearly wage of at least 120 percent of the average yearly wage of D.C. residents, (2) increase income and payroll tax revenue for the District of Columbia, (3) retain any new positions for at least one year, and (4) pass a "but-for" test establishing that the project would not have occurred in the absence of the job growth tax credit. The credits would be awarded in the order of priority received and cannot exceed an amount allocated in the District's annual budget and financial plan.

Employers must submit a written application for a job growth tax credit, which must be approved by the Mayor, before a project commences in the District of Columbia. The application must describe the project as well as the jobs that will be created and the anticipated salary range, and provide documentation to meet the but-for test. The authorizing statute provides a formula for the Mayor to determine a maximum credit for the life of the project as well as an annual credit equal to 50 percent of a firm's Social Security payroll tax paid that year for new D.C. resident employees. Unused credits may be carried over for a period of as long as 10 years.

Maryland provides job creation tax credits to firms that are expanding or relocating to Maryland. To qualify for the credits, a business must have created at least 60 new, full-time jobs during a 24-month period (the threshold drops to 25 new, full-time jobs in designated priority funding areas). Firms that qualify can claim credits equal to 2.5 percent of aggregate annual wages for all newly-created, full-time jobs, up to a maximum of $1,000 per new job, except in targeted areas where the credit is larger (5 percent of annual wages, up to $1,500 per new job). A firm's total credits cannot exceed $1 million per year, but excess credits can be carried forward for five years.

Virginia offers major business facility tax credits of $1,000 per job created to firms that create at least 50 new full-time jobs by establishing or expanding a business faciliity in the state (the threshold is 25 new full-time jobs in areas designated as economically distressed). The credits are earned in increments over a three-year period and credits can be recaptured proportionately if employment decreases during the five years following the initial credit year. Unused credits can be carried forward for 10 years.

[359] A "project" is defined as "any business project that ecnourages, promotes, and stimulates economic development in key economic sectors and that is approved by the Mayor as specified in § 47-1807.54." See D.C. Official Code § 47-1807.51(8).

PURPOSE: The purpose of the credit is to create a broad-based incentive for businesses to start new projects in the District of Columbia that will increase employment among D.C. residents.

IMPACT: Although firms that increase their hiring would be the immediate beneficiaries of the credit, District residents would be the ultimate beneficiaries if the credit stimulated higher employment and tax revenue.

Two academic experts on job tax credits, Timothy Bartik and John Bishop, contend that such credits "should be simple: easy for employers to understand, easy for employers who are actually expanding payroll to claim, and easy … to administer. Second, the credit should be stringent: it should be difficult for employers to claim the credit *unless they are actually expanding employment and payroll*" (emphasis in the original).[360]

No revenue loss is estimated for FY 2012 because funds were not appropriated for the credit in the FY 2012 budget.

[360] Timothy Bartik and John Bishop, "The Job Tax Credit: Dismal Projections for Employment Call for a Quick, Efficient, and Effective Response," Economic Policy Institute Briefing Paper, October 20, 2009, available at www.epi.org, p. 12.

Income Tax
Credits

143. Paid leave for organ or bone marrow donors

District of Columbia Code: D.C. Official Code § 47-1807.08 and § 47-1808.08
Sunset Date: None
Year Enacted: 2006

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	no estimate	no estimate	no estimate	no estimate
Personal Income Tax Loss	$0	$0	$0	$0
Total	**no estimate**	**no estimate**	**no estimate**	**no estimate**

DESCRIPTION: A business that provides its employees with a paid leave of absence to serve as an organ or bone marrow donor may claim a non-refundable credit equal to 25 percent of the regular salary paid during the leave of absence, not to exceed 30 days for an organ donation and seven days for a bone marrow donation.

To qualify for the credit, the leave provided by the business must be in addition to any medical, personal, or other paid leave provided to the employee. In addition, the credit does not apply if the employee is eligible for leave under the U.S. Family and Medical Leave Act of 1993. The credit does not reduce the minimum tax liability for a business, and the business also cannot deduct the salary paid to the employee during any period for which the paid leave is in effect.

Neither Maryland nor Virginia offers employer incentives to encourage organ or bone-marrow donations. However, Virginia allows organ and tissue donors personal income tax deductions of up to $10,000 for unreimbursed medical expenses that have not been taken as a medical deduction on the taxpayer's federal income taxes.

PURPOSE: The purpose of the credit is to increase the number of private employers who allow their employees paid leave to serve as organ and bone marrow donors.

IMPACT: Employees who serve as organ or bone marrow donors are the intended beneficiaries of this provision, which should also generate indirect benefits by expanding the number of organ or bone marrow donors. There were two claimants of this credit in tax year 2009.

The revenue loss for FY 2012-FY 2015 cannot be estimated, because ORA follows the policy of the U.S. Internal Revenue Service providing that, "No statistical tabulation may be released outside the agency with cells containing data from fewer than three returns." [361] This policy is intended to protect the confidentiality of individual tax records.

[361] U.S. Internal Revenue Service, Publication 1075, "Tax Information Security Guidelines for Federal, State, and Local Agencies and Entities" (August 2010), p. 66.

Income Tax
Credits

144. Employer-assisted home purchases

District of Columbia Code: D.C. Official Code § 47-1807.07 and § 47-1808.07
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	minimal	minimal	minimal	minimal
Personal Income Tax Loss	$0	$0	$0	$0
Total	**minimal**	**minimal**	**minimal**	**minimal**

Note: "Minimal" means that the forgone revenue is estimated as less than $50,000 per year, although precise data are lacking.

DESCRIPTION: A business in the District of Columbia with at least one employee may receive a tax credit equal to one-half of the amount of homeownership assistance provided to its employees during the taxable year, provided that (1) the credit received for each employee shall not exceed $2,500, (2) the assistance is provided through a certified employer-assisted home purchase program, (3) the assistance is used for the purchase of a qualified residential real property, and (4) the eligible employee is a new homebuyer (someone who did not own a principal place of residence in the District in the prior 12 months).

To be eligible, an employee must have a household income less than or equal to 120 percent of the area median income.

PURPOSE: The purpose of the credit is to leverage private-sector assistance for new homeownership in the District of Columbia among low- to moderate-income individuals and families. By providing a tax credit equal to 50 percent of the housing assistance provided by a business, up to $2,500 annually for each year, the District has in effect created a matching incentive for employer-assisted home purchases.

IMPACT: Low- to moderate-income taxpayers who are eligible for an employer-assisted home purchase program benefit from this tax credit. There may also be spillover benefits in terms of a stronger tax base for the District, increased demand for housing, and more stable neighborhoods.

The revenue loss from the credit is difficult to estimate because the District's business tax forms do not include a separate line for employer-assisted home purchases. Instead, the credit is combined with other credits into a single line on the tax forms. Nevertheless, the estimated revenue loss for the FY 2012 to FY 2015 period is characterized as "minimal" for several reasons. First, two-thirds of D.C. corporate franchise taxpayers (66.9 percent in tax year 2009) and unincorporated business taxpayers (65.4 percent in tax year 2009) pay the minimum tax and cannot benefit from the credits. In addition, the credits were designed during a booming housing market; since that time, the housing market has leveled off. Finally, the D.C. Association of Realtors indicates that usage of the credits has been modest.

Income Tax
Credits

145. Lower-income, long-term homeownership

District of Columbia Code: D.C. Official Code § 47-1806.09 - § 47-1806.09f
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$5	$5	$5	$5
Total	**$5**	**$5**	**$5**	**$5**

DESCRIPTION: The District offers a lower-income, long-term homeowner credit to residents with a household income equal to or less than 50 percent of the area median income who own an eligible residence (one that receives the homestead deduction) as a principal place of residence and have resided in that home for at least seven consecutive years. Eligible homeowners get a credit on their District of Columbia income tax equal to the difference between the current real property tax bill and 105 percent of their real property tax bill in the prior year.

The credit is refundable, meaning that the taxpayer can get a check for any amount by which the credit exceeds his or her income tax liability. Because household income determines eligibility, this means that the income of anyone who shares the housing – even someone who is unrelated to the taxpayer – counts toward the 50 percent median income cap. To claim the credit, taxpayers must fill out Schedule L, the “Lower Income Long-Term Homeowner Credit.”

PURPOSE: The purpose of the credit is to protect lower-income, long-term homeowners in the District of Columbia from rapid increases in real property taxes that could force them to sell their homes and possibly to leave the District.

IMPACT: Lower-income, long-term homeowners in the District of Columbia benefit from this provision. In tax year 2010, 25 tax filers claimed the credit.

Income Tax
Credits

146. Property tax circuit breaker

District of Columbia Code: D.C. Official Code § 47-1806.06
Sunset Date: None
Year Enacted: 1977

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$4,041	$4,041	$4,041	$4,041
Total	**$4,041**	**$4,041**	**$4.041**	**$4,041**

DESCRIPTION: Low-income homeowners and renters (those with annual household gross income of $20,000 or less) may claim a property tax credit that is applied to the taxpayer's income tax liability. To qualify, the taxpayer must have been a D.C. resident throughout the taxable year. The credit is refundable; if the amount of the credit exceeds tax liability, the taxpayer receives the excess amount in the form of a refund.

For homeowners, the credit equals the amount by which a homeowner's property tax bill exceeds a percentage of household income (the relevant percentage varies throughout the $0 to $20,000 income range), up to a maximum of $750.

For renters, the imputed property tax payment is 15 percent of total rent payments. The renter also receives a credit equal to the amount by which his or her imputed property tax payment exceeds a percentage of household income (the relevant percentage varies throughout the $0 to $20,000 income range), up to a maximum of $750.

There is a separate formula for determining the benefits available to elderly, blind, or disabled taxpayers, but the credit is once again capped at $750.

The program is known as a "circuit breaker" program because it provides tax relief when a household's real property tax grows large as a percentage of income. According to the Lincoln Land Institute, 33 states and the District operated at least one circuitbreaker program in 2008.[362]

Because household income determines eligibility, this means that the income of anyone who shares the housing – even someone who is unrelated to the taxpayer – counts toward the $20,000 threshold. To claim the credit, taxpayers must fill out schedule H, "Homeowner and Renter Property Tax Credit," which requires documention of the income of all household members.

Maryland also offers a circuitbreaker program based on household income. Homeowners with income up to $60,000 can claim a credit on taxes that result from the first $300,000 in assessed value. Renters can also qualify for a credit of up to $750 based on the assumption that 15 percent of their rent is used to pay property tax. Virginia does not have a circuitbreaker program.

[362] John Bowman, Daphne Kenyon, Adam Langley, and Bethany Paquin, Property Tax Circuit Breakers: Fair and Cost-Effective Relief for Taxpayers, Lincoln Land Institute of Land Policy Focus Report, 2009, p. 2.

<u>PURPOSE</u>: The purpose of the credit is to enhance income security for residents whose property taxes are high relative to their income, such as elderly residents on fixed incomes. Although the tax relief is provided through the income tax system, it is based on the amount by which an individual or family's property tax bill exceeds a specified percentage of income.

<u>IMPACT</u>: The beneficiaries of this provision are taxpayers who have an annual household gross income of $20,000 or less, and own or rent a home in the District of Columbia that serves as their primary place or residence. During tax year 2009, 7,248 tax filers claimed the credit. The benefits of this provision are fairly evenly distributed among taxpayers with income below $20,000, as shown in the table below.

Property Tax Circuit Breaker - 2009

Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	1,075	15%	$646	16%
$1 to $5,000	1,367	19%	$788	20%
$5,001 to $10,000	1,433	20%	$817	20%
$10,001 to $15,000	1,792	25%	$979	24%
$15,001 to $20,000	1,581	22%	$810	20%
Total	7,248	100%	$4,041	100%

Income Tax
Credits

147. Earned income tax credit

District of Columbia Code: D.C. Official Code § 47-1806.04(f)
Sunset Date: None
Year Enacted: 2000

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$46,864	$48,364	$47,870	$49,856
Total	**$46,864**	**$48,364**	**$47,870**	**$49,856**

DESCRIPTION: An individual who receives a federal earned income tax credit (EITC), as authorized by section 32 of the U.S. Internal Revenue Code (26 U.S.C. § 32), is eligible for a District of Columbia EITC equal to 40 percent of the federal credit. The credit is refundable, meaning that if the taxpayer's credit exceeds his or her D.C. income tax liability, he or she receives the balance in the form of a refund.

Working families with children who have annual incomes below $35,000 to $49,000 (depending on marital status and number of children) generally are eligible for the federal EITC. In addition, low-income workers without children who have incomes below $13,600 ($18,700 for a married couple) can receive a very small federal EITC.[363] The EITC has a phase-in range where the credit increases along with earnings, then hits a plateau where the credit remains constant, and then has a phase-out range where the credit falls to zero.

The American Recovery and Reinvestment Act (ARRA) of 2009 also revised the federal EITC by providing a larger subsidy for families with three or more children and increasing benefits for married couples in order to reduce a "marriage penalty." Although the ARRA expansions were originally adopted only for 2009 and 2010, Congress extended the provisions through the end of 2012. Those changes are mirrored in the D.C. EITC.

The D.C. EITC is also available to non-custodial parents between the ages of 18 and 30 who are in compliance with a court order for child support payments. Because these taxpayers are not eligible for the federal EITC, they must fill out an additional form (Schedule N, "Non-Custodial Parent EITC claim") to claim the D.C. EITC. Taxpayers cannot claim both the D.C. EITC and the low-income credit.

The majority of states (23 of 41) with a broad-based income tax also offer their own EITCs, including Maryland and Virginia. The District's 40 percent refundable EITC is the most generous in the nation.[364] Maryland offers taxpayers the choice of a 25 percent refundable EITC, or a 50 percent non-refundable EITC. Virginia provides a 20 percent non-refundable EITC. Montgomery County is one of three localities nationwide to offer an EITC; it matches the refundable EITC provided by the state of Maryland.

[363] Center on Budget and Policy Priorities, "Policy Basics: The Earned Income Tax Credit," September 6, 2011, available at www.cbpp.org.

[364] Cordes and Juffras, p. 312.

<u>PURPOSE</u>: The purpose of the credit is to promote self-sufficiency among low-income workers, thereby reducing poverty and welfare dependency. The refundability of the EITC makes it a particularly powerful anti-poverty tool.

<u>IMPACT</u>: Low-income working parents eligible for the federal EITC, as well as non-custodial parents who qualify for the District of Columbia EITC, benefit from this credit. During tax year 2009, 50,937 tax filers claimed the D.C. EITC. Tax filers with income between $10,000 and $20,000 received 48 percent of the value of the credit, as shown in the table below. This is consistent with the structure of the credit, whereby the income range for receiving the maximum credit is between about $8,000 and $15,000.

Researchers have found that the EITC leads to significant increases in employment among single mothers while not reducing labor supply among those who were already in the labor market.[365] One estimate is that the EITC lifted 2.5 million children out of poverty nationwide in 2005, more than any other government program.[366]

Proponents also contend that state EITCs are simple to administer; there is no additional bureaucracy needed to deliver the benefits. The D.C. EITC requires only one additional line on the income tax form and a simple calculation (federal EITC * .4), except for eligible non-custodial parents, who don't qualify for the federal EITC.

Earned Income Tax Credit - 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	661	1.3%	$327	1%
$1 to $10,000	16,074	31.6%	$8,390	18%
$10,001 to $20,000	16,109	31.6%	$21,750	48%
$20,001 to $30,000	11,657	22.9%	$12,054	27%
$30,001 to $40,000	6,079	11.9%	$2,849	6%
Greater than $40,000	357	0.7%	$83	0%
Total	50,937	100.0%	$45,455	100.0%

365 Nada Eissa and Hilary Hoynes, "Redistribution and Tax Expenditures: The Earned Income Tax Credit," *National Tax Journal* (64)(2, Part 2), June 2011, p. 704.

366 Eissa and Hoynes, p. 690.

Income Tax
Credits

148. Low-income credit

District of Columbia Code: D.C. Official Code § 47-1806.04(e)
Sunset Date: None
Year Enacted: 1987

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$1,437	$1,437	$1,437	$1,437
Total	**$1,437**	**$1,437**	**$1,437**	**$1,437**

DESCRIPTION: A taxpayer qualifies for a low-income credit if he or she meets the following requirements: (1) the taxpayer filed a federal tax return and his or her federal tax before credits and payments is zero, (2) the taxpayer's federal adjusted gross income is less than the sum of his or her federal personal exemptions and federal standard deduction, and (3) the taxpayer's amount of taxable income on the form D-40 is more than zero.

The credit is calculated in accordance with a table prescribed by the Mayor. For tax year 2011, the credit ranged from $129 to $1,443, depending on the taxpayer's filing status and number of personal exemptions.

The credit is non-refundable, which means that the credit can reduce the amount of D.C. tax that is owed, but does not result in a tax refund if the credit exceeds the amount of income tax liability. Taxpayers cannot claim both the D.C. earned income tax credit and the low-income credit.

Maryland provides a non-refundable "poverty-level credit" to taxpayers with earned income and Maryland adjusted gross income below the federal poverty standards. The credit equals the lesser of the state income tax paid or 5 percent of the taxpayer's earned income. Similarly, Virginia offers a non-refundable "credit for low-income individuals" for taxpayers with Virginia adjusted gross income that falls below the federal poverty level. The credit cannot exceed $300 for each person claimed as a personal exemption on the Virginia tax return, and taxpayers who claim certain other exemptions or deductions are not eligible for the low-income credit.

PURPOSE: The purpose of the low-income credit is to eliminate income tax liability for poor households. This goal is achieved by making the District's income tax threshold equal to the federal income tax threshold. The "tax threshold" is defined as "the point at which a taxpayer begins to owe income tax after allowance of the standard deduction and all personal exemptions to which the taxpayer is entitled, but before application of any itemized deductions or credits."[367]

IMPACT: D.C. taxpayers who do not have any federal tax liability benefit from this credit. During tax year 2009, 8,033 tax filers claimed the credit. Tax filers with income between $5,000 and $15,000 claimed roughly half (48 percent) of the value of the credit, as shown in the table on the next page.

[367] See D.C. Official Code § 47-1806.4(e)(1).

The credit is particularly likely to benefit low-income individuals and families who cannot qualify for the EITC because they have little or no earnings (such as retirees). In addition, the low-income credit may particularly benefit low-income childless adults, who receive much smaller EITC benefits than families with children.

Low-Income Credit - 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	297	4%	$52	4%
$1 to $5,000	1,288	16%	$120	8%
$5,001 to $10,000	3,392	42%	$423	29%
$10,001 to $15,000	1,268	16%	$278	19%
$15,001 to $20,000	811	10%	$276	19%
Greater than $20,000	977	12%	$289	20%
Total	8,033	100%	$1,437	100%

Income Tax
Credits

149. Brownfield revitalization and cleanup

District of Columbia Code: D.C. Official Code § 8-637.01
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$0	$0	$0	$0
Total	**$0**	**$0**	**$0**	**$0**

DESCRIPTION: The Mayor is authorized to submit proposed rules to the Council to establish business franchise tax credits for businesses that clean up and redevelop "brownfields," which are defined as "abandoned, idled property or industrial property where expansion or redevelopment is complicated by actual or perceived environmental contamination."[368] The total credits awarded to a business would be capped at 100 percent of the costs of cleanup and 25 percent of the costs for development of the brownfield.

A review did not identify similar business tax incentives offered by Maryland or Virginia, but Maryland authorizes local governments to provide property tax credits equal to 50 to 70 percent of the increase in property taxes for property owners who participate in the state's Voluntary Cleanup Program. The tax credits may be granted for five years, or 10 years if the property is in an enterprise zone. Montgomery County and Baltimore City are among the jurisdictions that offer the property tax credits.

PURPOSE: The intent of this tax expenditure is to provide incentives for businesses to clean up brownfields voluntarily, which would in turn reduce public health risks and promote economic development by encouraging the reuse of contaminated properties.

IMPACT: Businesses that own contaminated property are the intended beneficiaries of this provision, which is also designed to have spillover benefits to society by reducing environmental risks and contaminants while promoting the redevelopment of brownfields. Nevertheless, the credits have not been offered because implementing regulations have not been proposed.[369]

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[368] See D.C. Official Code § 8-631.02(2).

[369] If the Mayor proposed regulations, the Council would have 45 days to review the rules (excluding Saturdays, Sundays, legal holidays, and periods of Council recess), and if the Council did not act within this period, the rules would be deemed approved.

Income Tax
Credits

150. Child and dependent care

District of Columbia Code: D.C. Official Code § 47-1806.04(c)
Sunset Date: None
Year Enacted: 1977

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Business Income Tax Loss	$0	$0	$0	$0
Personal Income Tax Loss	$6,680	$6,680	$6,680	$6,680
Total	**$6,680**	**$6,680**	**$6,680**	**$6,680**

DESCRIPTION: An individual who receives a federal child and dependent care tax credit, as authorized by section 21 of the U.S. Internal Revenue Code (26 U.S.C. § 21), is eligible for a District of Columbia income tax credit equal to 32 percent of the federal credit. The credit is not refundable (it cannot exceed the amount of the individual's tax liability).

The U.S. Internal Revenue Code limits the credit to care provided for a dependent child under the age of 13, or a spouse or certain other dependents who are incapable of self-care. The care must have been provided in order that the taxpayer, and his or her spouse if the taxpayer is married, can work or look for work. The individual receiving the care must have lived with the taxpayer for at least half of the year. The value of the federal credit ranges from 20 percent to 35 percent (depending on income) of dependent care expenses of as much as $3,000 for one qualifying individual and $6,000 for two or more qualifying individuals.[370]

The expenses qualifying for the credit must be reduce by the amount of any employer-provided dependent care benefits that the taxpayer excluded from his or her gross income.

Maryland offers a child and dependent care tax credit similar to the District's: individuals with income up to $25,000 and joint filers with income up to $50,000 receive credits up to 32.5 percent of the federal credit which are phased out near the top of the eligibility scale. Maryland also allows single filers to deduct up to $3,000 and joint filers to deduct up to $6,000 in actual child and dependent care expenses. Virginia does not provide a child and dependent care credit, but allows taxpayers who qualify for the federal credit to deduct up to $3,000 in care expenses for one dependent and up to $6,000 for two or more dependents.

PURPOSE: The purpose of the credit is to assist families in paying for child and dependent care so that a parent or caretaker may work or look for work.

IMPACT: Individuals and families eligible for the federal child and dependent care tax credit benefit from the D.C. credit. During tax year 2009, 15,799 tax filers claimed the credit. Tax filers with income of $25,000 or less claimed the majority (60 percent) of the benefit in terms of reduced tax liability, as shown in the table on the next page.

[370] U.S. Internal Revenue Service, "Top Ten Facts About the Child and Dependent Care Credit," IRS Tax Tip 2009-46.

Child and Dependent Care Credit - 2009				
Income Category (AGI)	**Number**	**Share**	**Amount ($ in 000s)**	**Share**
Breakeven or Loss	53	0.3%	$12	0%
$1 to $25,000	3,229	20%	$4,037	60%
$25,001 to $50,000	6,122	39%	$1,459	22%
$50,001 to $75,000	1,867	12%	$381	6%
$75,001 to $100,000	807	5%	$152	2%
$100,001 to $150,000	1,107	7%	$198	3%
$150,001 to $200,000	830	5%	$138	2%
$200,001 to $500,000	1,456	9%	$239	4%
Over $500,000	328	2%	$65	1%
Total	15,799	100%	$6,680	100%

REAL PROPERTY TAX

Real Property Tax
Abatements

151. New or improved buildings used by high-technology companies

District of Columbia Code: D.C. Official Code § 47-811.03
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: Two types of non-residential or mixed-use buildings are eligible for a freeze on property taxes for a five-year period, if more than 50 percent of the tenants are qualified high-technology companies, or at least 50 percent of the aggregate square footage is leased to a qualified high-technology company using the premises as an office or retail space.

First, new buildings which received their initial certificate of occupancy after December 31, 2000, are eligible for the property tax freeze. In addition, existing buildings that were improved in order to adapt or convert the property for use by a qualified high-technology company are also eligible for the tax abatement.

The property tax abatements are part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[371]

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies.

PURPOSE: The purpose of the abatement is to ensure that high-technology companies have adequate space and to protect property owners against sharp increases in their tax liability that may accompany the development or conversion of space for use by high-technology companies. More generally, the tax abatement is intended to encourage the growth of high-technology companies in the District of Columbia and thereby expand the District's economy and employment base.

IMPACT: High-technology companies in the District of Columbia, as well as the property owners who lease space to high-technology companies, are the intended beneficiaries of this provision. Nevertheless, tax records indicate that there have been no claimants for the abatement in recent years.

[371] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, employment credits, sales tax exemptions, and personal property tax exemptions, are discussed elsewhere in this section.

Real Property Tax
Abatements

152. Non-profit organizations locating in designated neighborhoods

District of Columbia Code: D.C. Official Code § 47-857.11 - § 47-857.16
Sunset Date: None
Year Enacted: 2010

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$500 maximum	$500 maximum	$500 maximum	$500 maximum

DESCRIPTION: Non-profit organizations[372] as well as property owners who lease office space to the non-profits, can qualify for real property tax abatements for a period of 10 years if they are located in an "eligible non-profit zone." The authorizing statute defines five non-profit zones and allows the Mayor to designate additional zones, which must be approved by act of the Council.

Eligible non-profits or property owners can receive a real property tax abatement of $8 per square foot for 10 consecutive years if they: (1) purchase or lease 5,000 square feet of office space, (2) occupy at least 75 percent of the space, (3) purchase or lease the space at the market rate, and net of any real estate taxes, (4) do not receive any other real property tax abatement or tax-increment financing for the office space, and (5) occupy the new space by September 30, 2013, if located in the Capitol Riverfront, Mount Vernon Triangle, or NOMA zones, or by September 30, 2016, if located in the Anacostia zone, the Minnesota-Benning zone, or a zone designated by the Mayor.

Eligible non-profits or property owners cannot claim the abatement for more than 100,000 square feet of office space, and the annual abatement cannot exceed their real property tax liability. The total annual abatement is capped at $500,000, and the total abatement for each zone over 10 years is capped as follows: $600,000 for the Anacostia zone, $2.6 million for the Capitol Riverfront zone, $800,000 in zones designated by the Mayor; $600,000 in the Minnesota-Benning zone, $1.2 million in the Mount Vernon Triangle zone, and $2.6 million in the NOMA zone. Non-profits must apply to the Mayor and receive a certification of eligibility in order to claim an abatement.

PURPOSE: The purpose of the abatement is "to provide an incentive for (non-profits) to locate their offices in emerging commercial neighborhoods of the District of Columbia."[373]

IMPACT: Eligible non-profits and property owners who lease space to the non-profits benefit from the abatements. Although two non-profits have been approved for the abatements,[374] they has not taken effect at the time of this writing and the value of the abatements had not been

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[372] For purposes of this program, eligible non-profit organizations are those that are exempt from federal income tax under sections 501(c)(3), (4), and (6) of the U.S. Internal Revenue Code.

[373] See Title 10-B, Section 6300.1 of the D.C. Municipal Regulations.

[374] The approved non-profits are the American Iron and Steel Institute at 25 Massachusetts Avenue, N.W., and Case Western Reserve, at 820 First Street, N.E. Although the Office of Revenue Analysis normally does not provide tax information about specific individuals or organizations, D.C. Official Code § 47-1001 allows disclosure of tax-exempt properties.

calculated. The Office of the Deputy Mayor for Economic Development has decided not to offer additional abatements.[375] The abatements violate the principle of horizontal equity because other organizations with the same economic resources do not receive similar benefits.

[375] Michael Neibauer, "D.C. Ends Nonprofit Tax Abatement, Citing Low Interest in Progam," *Washington Business Journal*, December 9, 2011.

Real Property Tax
Abatements

153. Improvements to low-income housing

District of Columbia Code: D.C. Official Code § 47-866
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: If the owner of an eligible housing accommodation makes improvements of at least $10,000 per housing unit in a 24-month period, the owner is eligible for a tax abatement equal to the increase in real property tax liability for each of the subsequent five years, relative to a base year before the improvements were completed.

To qualify, the owner must offer at least 25 percent of the units at rents that are affordable to households with income below 50 percent of the area median. In addition, the owner must maintain the property as low-income housing throughout the five-year period, and is not eligible for the abatement if he or she has recovered the costs of renovation through another program.

The total abatements provided through this tax provision are capped at $1 million annually. To receive the benefit, the property owner must submit an application to the Mayor at least 30 days before the physical improvements begin and receive certification from the Mayor after the improvements are completed. The Mayor must also determine that the improvements are unlikely to be made without the tax abatement. In Mayor's Order 2009-202, dated November 25, 2009, Mayor Fenty designated the Department of Housing and Community Development (DHCD) as the agency responsible for administering this tax abatement program.[376]

PURPOSE: The purpose of the abatements is to preserve and upgrade the supply of affordable housing by encouraging owners to rehabilitate their housing units and making the abatements contingent on the affordability of the housing to low-income individuals and families.

IMPACT: The owners of affordable-housing accommodations who improve their housing are the intended beneficiaries of this provision, along with the low-income residents who live in the housing units. Nevertheless, DHCD has not received any applications for the abatement.

[376] Mayor's Order 2009-202, entitled "Delegation of Authority – Tax Abatements under Section 291 of the Housing Act of 2002," was published in the D.C. Register, Vol. 56, No. 49, p. 9222, December 4, 2009.

Real Property Tax
Abatements

154. New residential developments

District of Columbia Code: D.C. Official Code § 47-857.01 - § 47-857.10
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$3,331	$3,331	$3,157	$1,491

DESCRIPTION: The Mayor is authorized to grant up to $8 million annually in real property tax abatements for new residential developments. The tax abatement for any eligible property expires at the end of the 10th tax year after the tax year in which a certificate of occupancy is issued for the property. An eligible property must be improved by new structures or undergo rehabilitation, and have 10 or more units devoted to residential use.

The $8 million annual limit is divided among projects in three areas: (1) $2.5 million in tax abatements for new housing projects and new mixed-income housing projects downtown, (2) $2 million in tax abatements for new housing projects and new mixed-income housing projects in Housing Priority Area A ("Mount Vernon Square North"), and (3) $3.5 million in tax abatements for new, mixed-income housing projects in other parts of the District of Columbia, which includes a set-aside of up to $500,000 for real property located in square 2910.[377]

Recipients of the tax abatements include the "Mass Court Apartments" at 300 Massachusetts Avenue, N.W., the "Meridian at Gallery Place" apartments at 450 Massachusetts Avenue, N.W., the "Quincy Court" condominium at 1117 10th Street, N.W., and "The Residences at Georgia Avenue" at 4100 Georgia Avenue, N.W.

The amount of tax relief varies according to the location of the property and other factors, such as the type of construction and the percentage of affordable housing units. The rules governing the program are set forth in Title 10-B, Chapter 59 of the D.C. Municipal Regulations. The Office of the Deputy Mayor for Planning and Economic Development administers the program.

A property that claims a tax abatement for vacant rental housing (see tax expenditure #158) or receives tax-increment financing is not eligible for the new residential development abatements.

PURPOSE: The regulations state that the program's purpose is "to provide tax abatements as incentives for the production of new housing downtown and for the production of affordable, mixed-income housing in high-cost areas of the District of Columbia."[378]

IMPACT: The tax abatements are intended to deliver broad-based benefits by promoting the growth of mixed-income communities with commercial and residential uses, thereby

[377] Square 2910 is bounded by Kansas Avenue, Upshur Street, Georgia Avenue, and Taylor Street in Northwest D.C.

[378] See Title 10-B, Section 5900 of the D.C. Municipal Regulations.

strengthening the District's economic and tax base.[379] In particular, the downtown and Mount Vernon Square North areas are targeted beneficiaries of the program. The revenue loss declines in FY 2014 and FY 2015 because some properties are coming to the end of the 10-year eligibility period. The abatements violate the principle of horizontal equity because similar developments in other parts of the city do not qualify for equivalent tax relief.

[379] This summary draws on the Council of the District of Columbia, Committee on Finance and Revenue, "Committee Report on Bill 14-183, the 'HomeStart Financial Incentives Act of 2001," dated November 13, 2001.

Real Property Tax
Abatements

155. NoMA residential developments

District of Columbia Code: D.C. Official Code § 47-859.01 - § 47-859.05
Sunset Date: None
Year Enacted: 2009

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$4,263	$4,689	$4,689	$4,689

DESCRIPTION: The Mayor is authorized to grant up to $5 million annually and $50 million in total real property tax abatements for new residential developments in the North of Massachusetts Avenue (NoMA) neighborhood of Wards 5 and 6. The tax abatement for any eligible property expires at the end of the 10th tax year after the tax year in which a certificate of occupancy is issued for the property. An eligible property must be improved by new structures or undergo rehabilitation, and have 10 or more units devoted to residential use. There is also an overall cap of 3,000 on the number of new residential units that can qualify for the abatement.

The tax abatement is set at $1.50 per residential floor-area ratio square foot, multiplied by the total square footage as certified by the project architect and the Mayor. The rules governing the program are set forth in Title 10-B, Chapter 62 of the D.C. Municipal Regulations. The Office of the Deputy Mayor for Planning and Economic Development administers the program.

A property that claims a tax abatement for vacant rental housing (see Tax Expenditure #158) or receives tax-increment financing is not eligible for the NoMA abatements.

PURPOSE: The purpose of the abatements is to encourage new multi-family residential development in the NoMA neighborhood. Noting that residential development had slowed considerably due to a weakening economy and credit crunch, the Council's Committee on Finance and Revenue stated in its report on the authorizing legislation that, "The tax abatement bill would give an incentive to new builders to break ground and create new residential development in the NoMA area. The tax incentives contained in the bill are modeled after the successful Housing Act of 2002."[380] (see tax expenditure #154, "New residential developments").

IMPACT: Housing developers and residents of the new housing developments stand to benefit from the tax abatements, which are also intended to have broader benefits by strengthening the District's economic and tax base. The abatements violate the principle of horizontal equity because they similar developments in other parts of the city do not qualify for equivalent tax relief.

[380] Council of the District of Columbia, Committee on Finance and Revenue, Report on Bill 18-18, the "NoMA Residential Development Tax Abatement Act of 2009," March 16, 2009, p. 2.

Real Property Tax
Abatements

156. Preservation of section 8 housing

District of Columbia Code: D.C. Official Code § 47-865
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$6	$11

DESCRIPTION: If the owner of a housing accommodation who receives subsidies through a project-based housing assistance program ("Section 8" program) of the U.S. Department of Housing and Urban Development (HUD) renews or extends the HUD contract with substantially the same conditions for at least five years, the owner is eligible for a tax abatement. To qualify, the housing must be located in an area where the average rent for one-bedroom and two-bedroom apartments exceeds the fair-market rent (as defined by HUD) by 25 percent or more.

If the contract is renewed for five years, the owner qualifies for a tax abatement for each of the five years equal to 75 percent of any increment to his or her real property tax liability compared to a base year immediately prior to the first year of the abatement. If the contract is renewed for 10 years, the owner qualifies for a tax abatement for each year equal to 100 percent of the increment to his or her real property tax liability compared to the base year.

In Mayor's Order 2009-202, dated November 25, 2009, Mayor Fenty designated the Department of Housing and Community Development as the agency responsible for administering this tax abatement program.[381]

PURPOSE: The purpose of the abatements is to protect the supply of affordable housing by encouraging owners of housing who participate in federally-subsidized housing programs for low-income households to remain in the programs. The abatements are limited to areas where the average rents exceed the fair-market rent by 25 percent in order to target the benefits where they are most needed.[382]

IMPACT: The owners of housing accommodations in qualified areas who renew their contracts with HUD to provide section 8 housing are the intended beneficiaries of this provision, along with residents of federally-subsidized housing located in the qualified areas. However, only one property owner (Trinity Towers Apartments, LP, which owns 3017 14th Street, N.W.) has claimed an abatement since the program began. One factor that has limited participation is that HUD has executed one-year renewals with many housing providers.

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[381] Mayor's Order 2009-202, entitled "Delegation of Authority – Tax Abatements under Section 291 of the Housing Act of 2002," was published in the D.C. Register, Vol. 56, No. 49, p. 9222, December 4, 2009.

[382] This summary draws on the Council of the District of Columbia, Committee on Finance and Revenue, "Committee Report on Bill 14-183, the 'HomeStart Financial Incentives Act of 2001," dated November 13, 2001. The tax abatements for preservation of section 8 housing originated in Bill 14-183, which became Law 14-114, the "Housing Act of 2002," effective April 19, 2002.

The projected revenue loss for FY 2012 is zero because the assessed value of the qualifying property has dipped below the assessed value in the base year. Under an assumption of 5 percent annual growth in the assessed value there would be no revenue loss in FY 2013 and only a minor revenue loss in FY 2014 and FY 2015.

Real Property Tax
Abatements

157. Single-room-occupancy housing

District of Columbia Code: D.C. Official Code § 42-3508.06
Sunset Date: None
Year Enacted: 1994

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: The Mayor is authorized to provide tax abatements, as well as deferral or forgiveness of water and sewer fees and other indebtedness to the District government, to encourage the development of single-room-occupancy housing for low- and moderate-income tenants. These incentives shall be granted following negotiations and the signing of a written agreement between the Mayor and housing providers who are developing or operating single-room-occupancy housing accommodations.

The written agreement may establish a formula for abating property tax liability for the relevant property or properties. The abatement applies for a period of not longer than 10 years, beginning during the first year that the newly constructed or rehabilitated single-room-occupancy housing becomes available for occupancy.

To qualify for the incentives, a housing provider must demonstrate to the satisfaction of the Mayor that the single-room-occupancy housing (1) is affordable to low- and moderate-income tenants and that the rent is reduced by the benefits received, (2) complies with the District's zoning regulations, (3) includes at least 95 square feet of space and a clothing storage unit, (4) provides toilet and shower or bathing facilities on each floor, (5) includes common day room, kitchen, and laundry facilities, (6) provides a 24-hour manual or electronic security system, and (7) is supervised by a manager who resides on the premises.

PURPOSE: The purpose of the incentives is to encourage the development of single-room-occupancy housing for low- and moderate-income tenants.

IMPACT: Organizations that develop or operate single-room-occupancy housing for low- and moderate-income tenants are the intended beneficiaries of this provision, along with the low- and moderate-income tenants who need affordable housing. Nevertheless, the Department of Housing and Community Development reports that there has been no use of the incentives.

Real Property Tax
Abatements

158. Vacant rental housing

District of Columbia Code: D.C. Official Code § 42-3508.02
Sunset Date: None
Year Enacted: 1985

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: An owner of newly constructed rental housing accommodations is eligible for tax abatements equal to 80 percent of tax liability during the first year the housing becomes available for rental. In each succeeding year, the tax liability would be increased by increments of 16 percent of the full tax liability until the property is fully taxable.

When vacant rental accommodations that have been rehabilitated become available for rental, the owner of the property also becomes eligible for an 80 percent reduction of the increased tax liability that results from the rehabilitation. In each succeeding year, the tax liability attributed to the rehabilitation would be increased by increments of 16 percent until the full value of the property is taxable. In addition, the Mayor may defer or forgive any indebtedness owed to the District, or forgive any outstanding tax liens, when a vacant rental accommodation is being rehabilitated in accordance with this program.

A project eligible for a tax abatement or the forgiveness of any indebtedness or tax lien through this program must be certified by the Mayor as being "in the best interest of the District and … consistent with the District's rental property needs in terms of its location, type, and variety of sizes or rental units." A property that receives tax incentives for new residential development in targeted neighborhoods (see tax expenditures #154 and #155) is not eligible for this program.

PURPOSE: The purpose of the abatement is to expand the supply of safe and affordable rental housing for low- to moderate-income residents of the District of Columbia.

IMPACT: Renters as well as the owners of newly constructed or rehabilitated rental housing are the intended beneficiaries of this tax incentive. According to the Department of Housing and Community Development, tax abatements have not been awarded through this program in recent years.

Real Property Tax
Exemptions

159. Development of a qualified supermarket, restaurant or retail store

District of Columbia Code: D.C. Official Code § 47-1002(23)
Sunset Date: None
Year Enacted: 1988

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$1,980	$2,278	$2,659	$3,049

DESCRIPTION: A qualified supermarket, restaurant or retail store is eligible for a real property tax exemption for 10 consecutive years beginning with the tax year in which a certificate of occupancy was issued for the development. Qualified supermarkets, restaurants, and retail stores must be located in census tracts where more than half of the households have incomes below 60 percent of the area median, as determined by the U.S. Department of Housing and Urban Development. The property must continue to be used for the original purpose in order to maintain the exemption.

If the real property is not owned by the supermarket, restaurant, or retail store, the owner of the property can qualify for the real property tax exemption (also valid for 10 years) if the owner leases the land or structure to the supermarket at a fair-market rent that is reduced by the amount of the tax exemption. The authorizing statute also provides that a qualifying supermarket, restaurant, or retail store that leases real property which is part of a larger development can receive a rebate from the D.C. government for its pro-rata share of the property tax paid, if the owner of the property has already paid the tax.

However, the authorizing statute provides that any new exemptions for a qualified supermarket, restaurant, or retail store beginning on or after October 1, 2010, shall not be granted "until the fiscal effect of any such new exemptions is included in an approved budget and financial plan."[383]

PURPOSE: The purpose of this exemption is to encourage the construction and operation of supermarkets, restaurants and retail stores in lower-income areas of the city.

IMPACT: Individuals and organizations that are constructing and operating supermarkets, restaurants, and retail stores in the target areas benefit from this provision, as do residents of these areas. Presently, 13 supermarkets and one restaurant claim the exemption. The exemption violates the principle of horizontal equity because other businesses locating in the target areas do not receive a similar exemption.

The estimates of forgone revenue shown above are based on past experience suggesting that an additional two stores will qualify each year.

[383] See D.C. Official Code § 47-3802(c)(1).

Real Property Tax
Exemptions

160. High-technology commercial real estate database and service providers

District of Columbia Code: D.C. Official Code § 47-4630
Sunset Date: None
Year Enacted: 2010

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$700	$700	$700	$700

DESCRIPTION: Real property that is leased and occupied by a high-technology commercial real estate database and service provider qualifies for a 10-year exemption from the real property tax, subject to certain conditions. The real property must be located in an enterprise zone or a low- or moderate-income area, must have been occupied by December 31, 2010, and must continue to be occupied by the high-technology database and service provider. In addition, (1) the lease for the real property must last at least 10 years, (2) the tenant must employ a minimum of 250 employees in the District of Columbia, (3) the tenant must enter into an agreement with the Department of Small and Local Business Development concerning small and local business participation in any design, buildout, or improvement of the real property, and (4) the real property owner must pass the exemption through to the high-technology database and service provider.

The exemption does not take effect until the firm certifies to the Department of Employment Services that it has increased the number of new employees residing in the District of Columbia by at least 100, relative to a baseline employment level as of January 5, 2010. The firm must maintain employment at greater than the baseline level throughout the term of the abatement. The value of the exemption is capped at $700,000 annually and at $6,185,000 over 10 years.

PURPOSE: According to the Council committee report on the authorizing legislation, "The purpose of this legislation is to encourage business relocation into the District. The legislation will enable the attraction of a niche technology industry to the District."[384] The Office of the Deputy Mayor for Planning and Economic Development also expressed the view that the provision would increase employment, business activity, and tax revenue.[385]

IMPACT: The CoStar Group, which leases space at 1331 L Street, N.W., benefited from a $700,000 exemption in tax year 2011. Because the authorizing statute requires that the property must have been occupied by December 31, 2010, there will be no additional beneficiaries.

[384] Council of the District of Columbia, Committee on Finance and Revenue, Report on Bill 18-476, the "High Technology Commercial Real Estate Database and Service Providers Tax Abatement Act of 2008," November 24, 2009, p. 1.

[385] Council of the District of Columbia, Committee on Finance and Revenue, Report on Bill 18-476, the "High Technology Commercial Real Estate Database and Service Providers Tax Abatement Act of 2008," November 24, 2009, p. 3.

Real Property Tax
Exemptions

161. Educational institutions

District of Columbia Code: D.C. Official Code § 47-1002(10)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$102,031	$102,031	$102,337	$102,541

DESCRIPTION: Buildings belonging to and operated by schools, colleges, or universities "which are not organized or operated for private gain, and which embrace the generally recognized relationship of teacher and student," are exempt from real property taxation.

Exempting educational institutions from the real property tax is standard practice throughout the United States. Both Virginia and Maryland exempt educational institutions from real property taxation.

PURPOSE: The exemption supports a general policy of providing property tax exemptions to non-profit organizations that provide religious, charitable, social, scientific, literary, educational, or cultural benefits to the general public.

IMPACT: Educational institutions benefit directly from the exemption, which is also expected to provide broader societal benefits such as a better-informed citizenry and a more productive workforce. An estimated 475 properties qualify for the educational institutions exemption.

Real Property Tax
Exemptions

162. Libraries

District of Columbia Code: D.C. Official Code § 47-1002(7)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$431	$431	$432	$433

DESCRIPTION: Library buildings that belong to and are operated by organizations that are not organized or operated for private gain, and are open to the public generally, are exempt from real property taxation.

It is not clear whether private, non-profit libraries in other states are exempt from real property taxation. Libraries may qualify for real property exemptions granted to educational institutions or to art and cultural organizations, depending on the specific definitions of those categories in each state and how the statutory language has been interpreted.

PURPOSE: The exemption supports a general policy of providing property tax exemptions to non-profit organizations that provide religious, charitable, social, scientific, literary, educational, or cultural benefits to the general public.

IMPACT: Libraries benefit from the exemption, but there may be a wider social benefit because the libraries are open to the public and threby provide opportunities for learning and enrichment to the general populace. Presently, the Folger Shakespeare Library is the only library that qualifies for this exemption.

Real Property Tax
Exemptions

163. Embassies, chanceries, and associated properties of foreign governments

District of Columbia Code: D.C. Official Code § 47-1002(3)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$41,125	$41,125	$41,248	$41,330

DESCRIPTION: Property belonging to foreign governments and used for diplomatic purposes is exempt from real property taxation in the District of Columbia. To claim the exemption, a foreign government must send a diplomatic note to the U.S. Department of State's Office of Foreign Missions, which submits the request for property tax exemption to the D.C. government along with a "Foreign Government Information Request Form" that is completed by the foreign government.[386]

Exempting embassies and chanceries from real property taxation is standard practice, but such property is concentrated in cities such as D.C. and New York City. Neighboring jurisdictions such as Montgomery County, Arlington County, and Fairfax County exempt the property of foreign governments from the real property tax.

PURPOSE: The purpose of the exemption is to uphold a principle of international law that foreign governments are entitled to exemption from the taxation of real property owned by the foreign government and used by its diplomatic mission. Any portion of the property that is not used for diplomatic or consular purposes is not exempt from the District's real property tax.

IMPACT: Foreign governments that own embassies, chanceries, and associated properties in the District of Columbia benefit from this exemption. An estimated 604 properties qualify for a real property tax exemption based on this provision.

[386] U.S. Department of State, Office of Foreign Missions, "Diplomatic Note 06-01," dated April 12, 2006.

Real Property Tax
Exemptions

164. Federal government property

District of Columbia Code: D.C. Official Code § 47-1002(1)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$823,442	$823,442	$825,912	$827,559

DESCRIPTION: Property belonging to the United States is exempt from real property taxation in the District of Columbia, "unless the taxation of same has been authorized by Congress."

PURPOSE: This exemption recognizes the federal government's immunity from taxation by states or municipalities. This immunity has been established in numerous court decisions, beginning with *McCulloch v. Maryland*, 17 U.S. 316 in 1819, and has been reinforced in other cases including *Clallam County v. United States*, 263 U.S. 341 in 1923; *Cleveland v. United States*, 323 U.S. 329, 333 in 1945; *United States v. Mississippi Tax Commission*, 412 U.S. 363 in 1973; and *United States v. Mississippi Tax Commission*, 421 U.S. 599 in 1975.

IMPACT: The United States government benefits from this exemption. Presently, 2,814 properties receive the federal government exemption.

Real Property Tax
Exemptions

165. Miscellaneous properties

District of Columbia Code: Title 47 of the D.C. Official Code, Chapters 10 and 46
Sunset Date: Varies[387]
Year Enacted: Multiple years

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$69,063	$69,063	$69,270	$69,408

DESCRIPTION: This tax expenditure includes (1) properties that qualify for a tax exemption based on multiple categories, and (2) individual properties that were granted statutory exemptions but did not fall into any of the categories of tax-exempt property, such as non-profit educational institutions, non-profit hospitals, and charitable organizations. Real property exemptions for individual properties are found in Chapter 10 ("Property Exempt from Taxation") and Chapter 46 ("Special Tax Incentives") of Title 47 ("Taxation, Licensing, Permits, Assessments, and Fees") of the D.C. Official Code.

PURPOSE: The purpose of the exemptions is to reflect special circumstances that were deemed significant enough to warrant a real property tax exemption, as determined by the D.C. Council or the U.S. Congress.

IMPACT: The property owners who benefit from these tax exemptions represent a diverse array of organizations and commercial enterprises. An estimated 2,541 properties fall into the miscellaneous category.

An example of property that would qualify as multi-purpose exempt is land owned by the Washington Metropolitan Area Transit Authority (which is tax-exempt) that is the site of a tax-exempt affordable housing development.

Examples of organizations that have been awarded individual tax exemptions include the National Society of the Colonial Dames of America, the Young Men's Christian Association, the National Education Association, the Woolly Mammoth Theatre Company, the Rosedale Conservatory, the Capitol Hill Community Garden Land Trust, the Heurich House Foundation, the Brentwood Retail Center, the OTO Hotel at Constitution Square, and the Allen Chapel A.M.E. Senior Residential Retail Project.

[387] Some of the individual properties have sunset dates for their tax exemptions, but the more common restriction is that the exemption is valid so long as the property continues to be used for the same purpose as when the exemption was granted.

Real Property Tax
Exemptions

166. Hospital buildings

District of Columbia Code: D.C. Official Code § 47-1002(9)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$13,137	$13,137	$13,177	$13,203

DESCRIPTION: Hospital buildings that belong to and are operated by organizations "which are not organized or operated for private gain" are exempt from real property taxation.

Exempting non-profit hospitals from the real property tax is standard practice throughout the United States. Both Virginia and Maryland exempt non-profit hospitals from real property taxation.

PURPOSE: The exemption supports a general policy of providing property tax exemptions to non-profit organizations that provide religious, charitable, social, scientific, literary, educational, or cultural benefits to the general public.

IMPACT: Non-profit hospitals benefit from the exemption, but the general public is also intended to benefit from this subsidy to hospital care. Presently, 13 properties receive the hospital building exemption.

Real Property Tax
Exemptions

167. Historic property

District of Columbia Code: D.C. Official Code § 47-842 - § 47-844
Sunset Date: None
Year Enacted: 1974

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$119	$119	$120	$120

DESCRIPTION: The D.C. Council is authorized to grant tax relief to the owners of buildings that have been designated as historic by the Historic Preservation Review Board.[388] The tax relief is provided through agreements between the D.C. government and the property owners lasting at least 20 years, in order to assure the continued maintenance of the historic buildings.

The authorizing statute provides that the agreements "shall, as a condition for tax relief, require reasonable assurance that such buildings will be used and properly maintained and such other conditions as the Council finds to be necessary to encourage the preservation of historic buildings." The D.C. government can seek recovery of back taxes, with interest, if the conditions for the exemption are not fulfilled.

Montgomery County provides a Historic Preservation Tax Credit against the real property tax, equal to 10 percent of the amount expended by the taxpayer for restoring or preserving a historic property. Both Maryland and Virginia offer state historic preservation tax credits against other taxes (personal income, corporate income, and insurance premiums taxes in both states, and the bank franchise tax in Virginia).

PURPOSE: The purpose of this provision is to protect historic buildings and landmarks in the District of Columbia; preserve the city's historic, aesthetic, and cultural heritage; foster civic pride; and enhance the city's attractiveness to visitors, thereby promoting economic development.

IMPACT: Although the owners of historic buildings receive the direct benefits of the tax relief, there may be a broader benefit to D.C. residents from the preservation of the city's cultural and social history, as well as neighborhood beautification and improvement. Presently, two properties receive partial tax exemptions due to their historic status: the Potomac Boat Club at 3530 K Street, N.W., and the Washington Club, at 15 Dupont Circle, N.W.[389]

[388] Although the statute cites the Joint Committee on Landmarks of the National Capital as the designating authority, the Joint Committee was replaced by the Historic Preservation Review Board in 1978.

[389] The partial exemptions for both properties apply for 20 years. The Potomac Boat Club's exemption extends through FY 2021 and the Washington Club's exemption extends through FY 2024.

Real Property Tax
Exemptions

168. Homestead deduction

District of Columbia Code: D.C. Official Code § 47-850
Sunset Date: None
Year Enacted: 1978

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$54,673	$61,436	$62,389	$64,471

DESCRIPTION: Taxpayers who live in their own home in the District of Columbia may take a homestead deduction that reduces the taxable value of their home. Presently, the homestead deduction is $67,500. Annual cost-of-living adjustments to the homestead deduction were suspended for several years due to the budget crisis that resulted from the economic recession, but the adjustments will resume beginning on October 1, 2012.[390]

To qualify for the homestead deduction, the taxpayer must file an application with the Office of Tax and Revenue. Only homes with five or fewer dwelling units, including the unit occupied by the owner, are eligible. Taxpayers may not claim the deduction for more than one home.

Although neighboring jurisdictions in Maryland and Virginia provide a variety of tax relief to homeowners, they do not offer a provision similar to the District's homestead deduction. The Virginia Constitution allows the General Assembly to authorize localities to grant real property tax exemptions or deferrals to the elderly and disabled, but does not authorize a homestead exemption similar to the District's.

PURPOSE: The purpose of the homestead deduction is to encourage homeowners to live in the District of Columbia and to provide tax relief to resident homeowners.

IMPACT: District of Columbia residents who own their home benefit from this provision. In 2011, 91,879 owner-occupied residential properties qualified for the homestead exemption. Mark Haveman and Terri Sexton point out that, "Exemptions and credits for specified dollar amounts will result in a greater percentage tax reduction for owners of low-value homes, while exemptions and credits for a percentage of value will provide a greater dollar savings to owners of high-value homes."[391]

[390] The suspension of the cost-of-living adjustments was made by Title VII-V of D.C. Law 18-111, the "Fiscal Year 2010 Budget Support Act of 2009." Under current law, once the suspension ends the exemption was to be adjusted to make up for the three years of forgone inflation adjustments. In his FY 2013 budget, Mayor Gray proposed basing the inflation adjustment only on the past year's change in the price level, but the proposal had not yet become law at the time this was written.

[391] Mark Haveman and Terri Sexton, "Property Tax Assessment Limits: Lessons from Thirty Years of Experience" Policy Focus Report PF018 of the Lincoln Institute of Land Policy, 2008, p. 33.

Real Property Tax
Exemptions

169. Lower-income homeownership households and cooperative housing associations

District of Columbia Code: D.C. Official Code § 47-3503
Sunset Date: None
Year Enacted: 1983

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$1,079	$1,079	$1,082	$1,084

DESCRIPTION: Certain property transferred to a "qualifying lower income homeownership household" is exempt from real property taxation. A qualifying lower-income homeownership household must meet two requirements: (1) household income can be no greater than 120 percent of the lower-income guidelines established for the Washington metropolitan area by the U.S. Department of Housing and Urban Development (HUD), and (2) the household must own the property in fee simple or receive at least a 5 percent qualified ownership interest as part of a shared equity financing agreement. The fair market value of the property being transferred cannot exceed 80 percent of the median sale price for homes in the District of Columbia.

As of December 1, 2011, the household income limits ranged from $59,040 for a one-person household to $111,300 for a household with eight or more people. The current limit on the purchase price of the home is $332,000.

In addition, if there is a shared equity financing agreement in place, the renting household must receive a "credit against rent" that is equal to the value of the property tax exemption multiplied by the percentage of the household's qualified ownership interest.

The real property tax exemption is valid until the end of the fifth tax year following the year in which the property was transferred. During the five-year period, the owner must continue to occupy the property. If the property is owned by a cooperative housing association, it must continue to rent at least 50 percent of the units to households that meet the income standard for a qualifying lower income homeownership household and benefit from the "credit against rent" requirement throughout the five-year period.

PURPOSE: The authorizing statute states that, "The purpose of this act is to expand homeownership opportunities for lower-income families to the maximum extent possible at the lowest possible cost to the District of Columbia."[392]

IMPACT: Households with annual income no greater than 120 percent of the lower-income guidelines established for the Washington metropolitan area benefit from this exemption. There may be spillover benefits for society if homeownership leads to neighborhood improvement and stability by giving people a greater stake in their communities.

[392] See D.C. Official Code § 47-3501(7).

Real Property Tax
Exemptions

170. Multi-family and single-family rental and cooperative housing for low- and moderate-income persons

District of Columbia Code: D.C. Official Code § 47-1002(20)
Sunset Date: None
Year Enacted: 1978

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$12,949	$12,949	$12,988	$13,013

<u>DESCRIPTION</u>: Multi-family and single-family rental and cooperative housing, as well as individual condominium units, are exempt from the real property tax if they are rented to low- and moderate-income persons and qualify for at least one of the following federal programs: (1) the mortgage interest subsidy program for owners of rental housing projects for lower-income families, (2) the "Section 8" housing voucher program, (3) the rent supplement program for needy tenants, (4) the mortgage insurance program for moderate-income and displaced families, and (5) the supportive housing direct loan program for the low-income elderly.

<u>PURPOSE</u>: The purpose of this provision is to increase and maintain the stock of affordable housing in the District of Columbia.

<u>IMPACT</u>: Owners of housing that is rented to low- and moderate-income families benefit from this provision, as do their tenants.

Real Property Tax
Exemptions

171. Nonprofit housing associations

District of Columbia Code: D.C. Official Code § 47-3505
Sunset Date: None
Year Enacted: 1983

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$7,553	$7,553	$7,576	$7,591

DESCRIPTION: Property transferred to a qualifying non-profit housing association[393] is exempt from the real property tax through the end of the third year in which the property was transferred, provided that the association certifies its intent to transfer the property to (1) a qualifying lower-income ownership household, (2) a multi-family housing property where at least 35 percent of the households are qualifying lower income ownership households, or (3) a cooperative housing association where at least 50 percent of the units are occupied by qualifying lower income ownership households and receive a "credit against rent."[394]

A qualifying lower-income homeownership household must meet two requirements: (1) household income can be no greater than 120 percent of the lower-income guidelines established for the Washington metropolitan area by the U.S. Department of Housing and Urban Development (HUD), and (2) the household must own the property in fee simple or receive at least a 5 percent qualified ownership interest as part of a shared equity financing agreement. As of December 1, 2011, the household income limits ranged from $59,040 for a one-person household to $111,300 for a household with eight or more people.

Maryland exempts property owned by a non-profit association from the state real property tax.

PURPOSE: The authorizing statute states that, "The purpose of this act is to expand homeownership opportunities for lower-income families to the maximum extent possible at the lowest possible cost to the District of Columbia."

IMPACT: Non-profit housing associations and the lower-income residents they assist in attaining homeownership benefit from this provision. There may be spillover benefits for society if homeownership leads to neighborhood improvement and stability by giving people a greater stake in their communities.

[393] Specifically, an eligible non-proft housing association is one that is exempt from federal income tax under sections 501(c)(3) or 501(c)(4) of the U.S. Internal Revenue Code.

[394] The credit against rent is equal to the value of the property tax exemption multiplied by the percentage of the household's qualified ownership interest.

Real Property Tax
Exemptions

172. Resident management corporations

District of Columbia Code: D.C. Official Code § 47-1002(24)
Sunset Date: None
Year Enacted: 1992

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: Public housing that is transferred to a qualifying resident management corporation is exempt from the real property tax through the end of the 10th tax year following the year in which the property is transferred. A resident management corporation is a non-profit corporation in which public housing residents are the sole voting members.

PURPOSE: The purpose of the exemption is to give low-income families living in a public housing project the opportunity to become owners of the public housing. Once residents become owners, they are expected to have a stronger stake in the maintenance of the property and the quality of life in the community.

IMPACT: Resident management corporations and the individuals they serve are the intended beneficiaries of this provision. According to the D.C. Housing Authority, the Kenilworth-Parkside project is the only property that has been transferred to a resident management corporation.

Because the Kenilworth-Parkside Resident Management Corporation assumed control in 1992, that property is now taxable. Therefore, there are presently no beneficiaries and no exemptions are projected for the FY 2012 through FY 2015 period.

Real Property Tax
Exemptions

173. Correctional Treatment Facility

District of Columbia Code: D.C. Official Code § 47-1002(25)
Sunset Date: None
Year Enacted: 1997

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$3,495	$3,495	$3,505	$3,512

DESCRIPTION: The Correctional Treatment Facility (CTF), located on Lot 800 of Square 1112, is exempt from real property taxation as long as the facility on that site is used as a correctional facility housing inmates in the custody of the Department of Corrections (DOC).

The CTF, which houses all of DOC's female and juvenile prisoners as well as some male prisoners who are a medium-security risk or lower, is owned and managed by the Corrections Corporation of America, which purchased the facility from the D.C. government in 1997 under a sale/leaseback arrangement.

PURPOSE: The purpose of this provision is to maintain the tax-exempt status of the CTF following the change from government to private ownership.

IMPACT: The operators of the CTF benefit from this provision, which was offered as part of a larger agreement in which the D.C. government received up-front revenue from the sale of the CTF.

Real Property Tax
Exemptions

174. Art galleries

District of Columbia Code: D.C. Official Code § 47-1002(6)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$2,102	$2,085	$2,091	$2,095

DESCRIPTION: Art gallery buildings belonging to and operated by "organizations which are not organized or operated for private gain" are exempt from real property taxation, provided that they are open to the public generally and do not charge admission more than two days per week.

Non-profit art and cultural organizations are exempt from real property taxation in Maryland and not in Virginia.

PURPOSE: The exemption supports a general policy of providing property tax exemptions to non-profit organizations that provide religious, charitable, scientific, literary, educational, or cultural benefits to the general public.

IMPACT: Art galleries benefit from the exemption, but there may be a wider social benefit because the galleries are open to the public and provide general cultural enrichment. Some of the galleries or museums that benefit from this exemption are Decatur House, the Hillwood Estate, and the Textile Museum. Many other galleries or museums are exempt through other provisions of the property tax code; for example, some are located on federal property and others have been exempted from real property taxation by a special act of Congress.

Real Property Tax
Exemptions

175. Cemeteries

District of Columbia Code: D.C. Official Code § 47-1002(12)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$5,548	$5,548	$5,565	$5,576

DESCRIPTION: Cemeteries dedicated to and used solely for burial purposes and not organized or operated for private gain, including buildings and structures reasonably necessary and usual to the operation of a cemetery, are exempt from real property taxation.

Real property tax exemptions for non-profit cemeteries are standard nationwide. Both Maryland and Virginia exempt non-profit cemeteries from real property taxation.

PURPOSE: The exemption supports a general policy of providing property tax exemptions to non-profit organizations that provide religious, charitable, scientific, literary, educational, or social benefits to the general public.

IMPACT: Non-profit cemeteries benefit from the exemption, but there may be a wider social benefit as well. Presently, 22 cemeteries qualify for the real property tax exemption.

Real Property Tax
Exemptions

176. Charitable organizations

District of Columbia Code: D.C. Official Code § 47-1002(8)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$14,272	$14,272	$14,315	$14,343

DESCRIPTION: Buildings belonging to and operated by institutions "which are not organized or operated for private gain," and are used "for purposes of public charity principally in the District of Columbia," are exempt from real property taxation.

Real property exemptions for charitable organizations represent standard practice throughout the United States. Maryland and Virginia exempt charitable organizations from the real property tax.

PURPOSE: The exemption supports a general policy of providing property tax exemptions to non-profit organizations that provide religious, charitable, scientific, literary, educational, or cultural benefits to the general public.

IMPACT: Charitable organizations benefit directly from the exemption, which is also expected to provide broader societal benefits by encouraging the voluntary provision of social services. An estimated 492 properties receive a real property tax exemption based on this provision. Some experts have pointed out that the exemption may be poorly targeted, because it favors charitable non-profits that own real estate, and may encourage some non-profits to invest more in real property than is optimal from the standpoint of maximizing social welfare (for example, the invesment in real estate could come at the expense of an organization's charitable mission itself).

Real Property Tax
Exemptions

177. Churches, synagogues, and mosques

District of Columbia Code: D.C. Official Code § 47-1002(13)
Sunset Date: None
Year Enacted: 1942

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$59,481	$59,481	$59,660	$59,779

DESCRIPTION: Churches, including buildings and structures reasonably necessary and usual in the performance of the activities of the church, are exempt from real property taxation. A church building is defined as a building "primarily and regularly used by its congregation for public religious worship."[395]

In addition, the following types of property belonging to religious orders or societies are exempt from real property taxation: buildings belonging to religious corporations or societies primarily and regularly used for religious worship, study, training, and missionary activities; pastoral residences owned by a church and actually occupied by the church's pastor, rector, minister, or rabbi (with a limit of one pastoral residence for any church or congregation); and Episcopal residences owned by a church and used exclusively as the residence of a bishop of the church.

Real property tax exemptions for churches, synagogues, mosques, and other places of religious worship are standard nationwide. Both Maryland and Virginia exempt churches, synagogues, and mosuqes from real property taxation.

PURPOSE: The exemption reflects a general policy of providing property tax exemptions to non-profit organizations that provide religious, charitable, scientific, literary, educational, or cultural benefits to the general public. More specifically, the exemption is intended to promote the free exercise of religion and respect the separation of church and state.

IMPACT: Churches, synagogues, mosques, and other places of worship benefit from the exemption, but the exemption is also intended to benefit society more broadly by promoting the free exercise of religion and the separation of church and state. An estimated 1,158 properties qualify for a real property tax exemption on this basis.

[395] See D.C. Official Code § 47-1002(13).

Real Property Tax
Exemptions

178. Washington Metropolitan Area Transit Authority properties

District of Columbia Code: D.C. Official Code § 9-1107.01
Sunset Date: None
Year Enacted: 1966

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	\$9,723	\$9,723	\$9,752	\$9,771

DESCRIPTION: The Washington Metropolitan Area Transit Authority Compact establishes the rules that govern the operation and administration of the regional mass transit system, commonly known as "Metro." The District of Columbia, the State of Maryland, and the Commonwealth of Virginia are signatories to the Compact. Article XVI ("General Provisions"), Section 78 of the Compact, exempts the Washington Metropolitan Area Transit Authority (WMATA) and its Board from all taxes or assessments on any property that WMATA owns or controls.

PURPOSE: As stated in the Compact, WMATA's mission "is in all respects for the benefit of the people of the signatory states and is for a public purpose." WMATA's exemption from all taxes or assessments on its property helps WMATA fulfill its mission of improving transportation throughout the region, and extends to this regional organization the tax exemption that is provided to federal and local government property.

IMPACT: Residents of the Washington metropolitan area benefit from this tax exemption, as do the businesses and visitors who also rely on the Metro system, because the exemption allows WMATA to devote more of its resources to serving the public. An estimated 421 properties qualify for a real property tax exemption based on this provision.

Real Property Tax
Credits

179. First-time homebuyer credit for D.C. government employees

District of Columbia Code: D.C. Official Code § 42-2506
Sunset Date: None
Year Enacted: 2000

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$291	$291	$292	$292

DESCRIPTION: District of Columbia government employees; employees of District of Columbia public charter schools; and individuals who have accepted an offer to be a District of Columbia police officer, firefighter, emergency medical technician, public school teacher, or public charter school teacher are eligible for property-tax credits if they are first-time homebuyers in the District of Columbia.

When first-time homebuyer credits were first authorized in 2000, only police officers were eligible, but the law was amended in 2007 to include the other groups of employees listed above.

The property-tax credit phases out over five years. In the first year, the credit equals 80 percent of property tax liability; in the second year, 60 percent; in the third year, 40 percent; and in the fourth and fifth years, 20 percent.

PURPOSE: The purpose of the credit is to provide a tool to recruit and retain qualified employees (particularly teachers, police officers, firefighters, and emergency medical technicians); to strengthen the economic and tax base; and to encourage employees to live in the District of Columbia and become engaged in its civic and neighborhood life.

IMPACT: District government employees, as well as individuals who have accepted an offer to serve as a District of Columbia police officer, firefighter, emergency medical technician, or teacher benefit from this tax credit. As noted above, there may also be spillover benefits for District of Columbia neighborhoods and the District economy. However, the credit violates the principle of horizontal equity because only some groups of new homebuyers are eligible.

According to the Department of Housing and Community Development, use of the credits has been steady in recent years, rising from 70 claimants in 2008 to 86 claimants in 2010, before dropping to 72 claimants in 2011.

Real Property Tax
Credits

180. Assessment increase cap

District of Columbia Code: D.C. Official Code § 47-864
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$28,416	$28,416	$28,501	$28,558

DESCRIPTION: Homeowners who qualify for a homestead deduction (those who occupy a home in the District of Columbia as their principal residence) are also eligible for an annual assessment cap credit. This credit limits the taxable assessed value of the individual's home to a 10 percent increase from the prior tax year.

If during the prior tax year the property was sold, its value was increased due to a change in its zoning classification, or the assessment of the property was clearly erroneous due to an error in calculation or measurement of improvements, then the taxpayer does not qualify for the assessment increase cap. In addition, the authorizing statute provides that the taxable assessment of a property qualifying for a homestead deduction shall never fall below 40 percent of the current tax year's assessed value.

Maryland also imposes a 10 percent cap on the annual increase in a home's taxable assessed value. The cap applies to all counties and municipalities in Maryland, which can also choose to adopt a cap lower than 10 percent. Virginia law limits the property tax growth in each locality to a 1 percent annual increase, excluding increases in property tax values that result from new construction or improvements, but localities have the authority to exceed the 1 percent cap after holding a public hearing on the issue.

PURPOSE: The purpose of the cap is to protect resident homeowners from sharp growth in property values and assessments. In the early to middle part of the past decade, the value of residential real property soared in the District of Columbia. Assessed values often rose by more than 20 percent annually, and sometimes more than doubled in a single year. From fiscal year 2002 to fiscal year 2007, the assessed value of residential real property in the District almost tripled from $24.9 billion to $73.1 billion.[396] The cap was intended to protect resident homeowners from these rapid increases in real property tax liability, and was also designed to smooth the transition from triennial assessments to annual assessments.

IMPACT: Homeowners who have a principal residence in the District of Columbia benefit from the cap on the annual increase in real property assessments, if the assessed value of their property rises by more than 10 percent in one year. In 2011, 95,291 owner-occupied households were subject to the asssessment increase cap. Due to the variation in rates of property value growth in different neighborhoods, the assessment increase cap can create equity problems. Some taxpayers will pay real property tax based on the full assessed value, while others who live in rapidly appreciating areas that benefit from the cap will not.

[396] Government of the District of Columbia, Office of the Chief Financial Officer, CAFR 2008: Comprehensive Annual Financial Report, Year Ended September 30, 2008 (January 2009), p. 160.

Real Property Tax
Credits

181. Senior citizens and persons with disabilities

District of Columbia Code: D.C. Official Code § 47-863
Sunset Date: None
Year Enacted: 1986

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$14,590	$14,590	$14,634	$14,663

DESCRIPTION: Senior citizens (age 65 or older) and persons with disabilities qualify for a 50 percent reduction in real property tax liability on a home that they own and occupy in the District of Columbia, provided that their household adjusted gross income is less than $100,000.

Taxpayers must file an application with the Office of Tax and Revenue in order to qualify. A senior citizen or person with a disability must own at least 50 percent of the property or cooperative unit, which must be the taxpayer's principal place of residence.

Montgomery County offers a real property Senior Tax Credit that is equal to 25 percent of a taxpayer's combined State Homeowners' Tax Credit and the county supplement to that credit. As authorized by Virginia law, the city of Alexandria as well as Arlington and Fairfax Counties provide full or partial real property tax exemptions, to low- and moderate-income senior citizens and those who are permanently and totally disabled. The amount of the exemption depends on household gross income, and there is also an asset limit for eligible households.

PURPOSE: The purpose of the credit is to protect senior citizens and people with disabilities, who often live on fixed incomes, from real property tax liabilities that may be difficult or impossible for them to pay.

IMPACT: The beneficiaries of this provision are senior citizens and people with disabilities who live in their own homes in the District of Columbia and have adjusted gross income less than $100,000. In 2011, 18,320 properties qualified for the credit. The credit violates the principle of horizontal equity because residents with adjusted gross income of less than $100,000 who are not senior citizens or persons with disabilities are not eligible for the same relief.

Real Property Tax
Credits

182. Brownfield revitalization and cleanup

District of Columbia Code: D.C. Official Code § 8-637.01
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: The Mayor is authorized to submit proposed rules to the Council to establish real property tax credits for property owners who clean up and redevelop "brownfields," which are defined as "abandoned, idled property or industrial property where expansion or redevelopment is complicated by actual or perceived environmental contamination."[397] The total credits awarded to a property owner would be capped at 100 percent of the costs of cleanup and 25 percent of the costs for development of the contaminated property.

Maryland authorizes local governments to provide property tax credits equal to 50 to 70 percent of the increase in property taxes for property owners who participate in the state's Voluntary Cleanup Program. The tax credits may be granted for five years, or 10 years if the property is in an enterprise zone. Montgomery County and Baltimore City are among the jurisdictions that offer the property tax credits.

PURPOSE: The purpose of this tax expenditure is to provide incentives for property owners to clean up brownfields voluntarily, which would in turn reduce public health risks and promote economic development by encouraging the reuse of contaminated properties.

IMPACT: The owners of contaminated property are the intended beneficiaries of this provision, which is also designed to have spillover the benefits for the public by reducing environmental risks and contaminants while promoting the redevelopment of brownfields. Nevertheless, the credits have not been offered because the implementing regulations have not been proposed.[398]

[397] See D.C. Official Code § 8-631.02(2).

[398] If the Mayor proposed regulations, the Council would have 45 days to review the rules (excluding Saturdays, Sundays, legal holidays, and periods of Council recess), and if the Council did not act within this period, the rules would be deemed approved.

Real Property Tax
Credits

183. Condominium and cooperative trash collection

District of Columbia Code: D.C. Official Code § 47-872 (condominiums) and § 47-873 (cooperatives)
Sunset Date: None
Year Enacted: 1990

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$5,177	$5,281	$5,386	$5,494

DESCRIPTION: Owners of condominium units and cooperative dwelling units may qualify for a trash collection credit against their real property tax liability if they pay for garbage collection instead of receiving city garbage service. The credit, which is $98 for 2011, is adjusted annually for inflation.

In order to qualify for the credit, the property must be occupied by the owner and used for non-transient residential purposes. In addition, the property must be located in a condominium or cooperative housing building with more than four dwelling units.

PURPOSE: The purpose of the credit is to help defray the costs of garbage collection for real property owners who do not receive trash collection services from the D.C. government.

IMPACT: Condominium or cooperative housing owners who pay for garbage collection benefit from this credit. In 2011, 50,800 homeowners qualified for the credit.

Real Property Tax
Multiple

184. Economic development zone incentives

District of Columbia Code: D.C. Official Code § 6-1501 - § 6-1503
Sunset Date: None
Year Enacted: 1988

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: D.C. law designates three economic development zones that are eligible for tax and other development incentives: the Alabama Avenue zone, the D.C. Village zone, and the Anacostia zone. The Mayor may also designate additional economic development zones, subject to Council approval by resolution. The designation of additional zones must be based on evidence of economic distress such as high levels of poverty, high levels of unemployment, low income, population loss, and other criteria set forth in the authorizing statute.

The available real property incentives include property tax reductions that are gradually phased out over five years (the reduction is 80 percent the first year, and is then reduced by 16 percent each year until reaching zero in year six); the deferral or forgiveness of any property tax owed on the property; and the forgiveness of costs or fees associated with a nuisance property infraction. To qualify, a property owner in an eligible zone must have constructed or substantially rehabilitated the property after October 20, 1988, and must comply with zoning regulations.

The Mayor must submit and the Council must approve a resolution that qualifies the property for the incentives. The resolution must identify the real property and its owner; specify each tax or charge to be reduced, deferred, or forgiven; and state the dollar amount of each tax incentive.

Montgomery County offers Enterprise Zone Tax Credits to businesses that locate in designated areas of downtown Silver Spring, Takoma Park/Long Branch, and Wheaton. The credits equal a percentage of the increase in real property liability, relative to a base year, and are phased out over 10 years.

PURPOSE: The purpose of the incentives is to encourage commercial, industrial, and residential development, and thereby to create jobs, increase homeownership, and stabilize neighborhoods characterized by high poverty and unemployment rates, low income levels, population loss, and other indicators of economic distress.

IMPACT: Owners of newly constructed or improved real property in an economic development zone are the intended beneficiaries of the incentives. However, only two incentive packages have been approved since the zones were created,[399] and neither is in effect today. There are no proposals pending to use the economic development zone incentives.

[399] Council Resolution 11-290, approved on April 16, 1996, awarded a real property tax abatement to the Good Hope Marketplace project in the Alabama Avenue Development Zone. Council Resolution 12-605, approved on July 17, 1998, forgave water and sewer charges for the Walter Washington Estates project in the Alabama Avenue Development Zone, and also authorized the forgiveness and reduction of real property taxes owed by the project.

Real Property Tax
Rebate

185. Public charter school tax rebate

District of Columbia Code: D.C. Official Code § 47-867
Sunset Date: None
Year Enacted: 2005

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$554	$554	$560	$565

DESCRIPTION: A public charter school that leases a school facility from an entity that is subject to the District's real property tax is entitled to a rebate equal to the school's pro-rata share of the lessor's tax on the property, provided that the school is liable under its lease for that share of the tax, and the lessor paid the tax.

Public charter schools must apply for the rebate by filing Form FP-305 with the Office of Tax and Revenue.

PURPOSE: The purpose of the rebate is to put public charter schools that lease their facilities on an equal footing with other public schools that own their facilities and are exempt from taxation on the real property.

IMPACT: Public charter schools that lease their school buildings benefit from this provision. During tax year 2010, six charter schools claimed a rebate.

The estimates of forgone revenue shown above are based on a five-year average (2006-2010) of the rebates provided. Annual rebates grew from $213,000 in FY 2006 to $858,000 in FY 2008 before dropping to $575,000 in FY 2010. Nevertheless, the forecast for FY 2012 to FY 2015 does not reflect a continued decline because the number of charter schools in the District has grown steadily since charters first opened in 1999.

Presently, there are 53 public charter schools with 98 campuses that serve more than 32,000 students. The D.C. Public Charter School Board has approved applications for 11 new charter schools that will open in the fall of 2013.[400]

[400] District of Columbia Public Charter School Board, "D.C. Public Charter School Board Receives 11 Charter School Applications," press release issued February 6, 2012.

Real Property Tax
Multiple

186. Homeowners in enterprise zones

District of Columbia Code: D.C. Official Code § 47-858.01 - § 47-858.05
Sunset Date: None
Year Enacted: 2002

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: The D.C. government provides real property tax abatements for homeowners in an enterprise zone who substantially rehabilitate their home. Census tracts with poverty rates of 20 percent or more qualify as enterprise zones.

To qualify for the abatements, a property owner must have a household income less than 120 percent of the area median income. In order to receive a tax abatement, an owner must receive certification from the Mayor that the property and rehabilitation meet the requirements of the law.

The tax abatement is measured as a percentage of the amount by which the homeowner's tax liability for the property increased after the substantial rehabilitation. During the year in which the rehabilitation is completed and the following three years, the taxpayer can deduct 100 percent of the increased tax liability. In the fourth year, the taxpayer can deduct 75 percent; in the fifth year, 50 percent; and in the sixth year, 25 percent. In the seventh year after the rehabilitation is completed, the property is fully taxable.

PURPOSE: The purpose of the abatement is to promote the revitalization of neighborhoods classified as enterprise zones, to attract new residents to the District of Columbia, and to strengthen the District's tax base.

IMPACT: Low- to moderate-income owners of homes in enterprise zones are the intended beneficiaries of these provisions, which are also intended to create spillover benefits for neighborhoods with poverty rates of 20 percent or more. Presently, there are no beneficiaries of these tax abatements and none are projected for the FY 2012 to FY 2015 period.

Real Property Tax
Deferrals

187. Low-income homeowners

District of Columbia Code: D.C. Official Code § 47-845.02
Sunset Date: None
Year Enacted: 2005

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$2,758	$2,758	$2,766	$2,771

DESCRIPTION: A taxpayer who occupies a home or condominium in the District of Columbia as his or her principal place of residence can defer any real property tax in excess of his or her real property tax for the prior year, if the taxpayer has a household adjusted gross income of less than $50,000. Real property tax deferred in accordance with this provision bears interest at the rate of 8 percent annually. The amount of real property tax deferred, including the interest on amounts deferred in prior years, cannot exceed 25 percent of the assessed value of the property in the current tax year.

To qualify for the deferral, the taxpayer must file an application with the Office of Tax and Revenue. Senior citizens (those who are 65 or older) must undergo home equity conversion mortgage counseling in order to qualify for the deferral.

Montgomery County also allows certain homeowners to defer paying the amount by which their real property tax liability exceeds the amount due the prior year. To qualify, the household must have had gross income of $120,000 or less the previous year, and at least one of the owners must have lived in the home as his or her principal place of residence for the prior five years. Interest on the deferred taxes accrues annually at a rate set by the county. In addition to the District of Columbia, 25 states had some type of tax deferral program in place in 2005.[401]

PURPOSE: The purpose of the deferral is to protect low- and moderate-income property owners from sharp increases in real property tax liability that may outpace the growth of their incomes.

IMPACT: Homeowners with annual household adjusted gross income less than $50,000 benefit from this provision.

[401] Haveman and Sexton, p. 35.

Real Property Tax
Deferrals

188. Low-income, senior-citizen homeowners

District of Columbia Code: D.C. Official Code § 47-845.03
Sunset Date: None
Year Enacted: 2005

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$827	$827	$830	$831

DESCRIPTION: A taxpayer who is 65 years of age or older, occupies a home or condominium in the District of Columbia as his or her principal place of residence, and has a household adjusted gross income of less than $50,000 can defer any real property tax owed in a given tax year. The deferred taxes bear interest at the rate charged by the U.S. Internal Revenue Service on underpayments of federal income taxes, but will not exceed 8 percent per year. The amount of tax deferred, plus interest accrued on the taxes deferred in previous years, is limited to 25 percent of the assessed value of the property in the current tax year.

Several additional requirements apply. The homeowner must live in a home with no more than five dwelling units, and the senior citizen or citizens must own at least 50 percent of the house or condominium. The homeowner must also undergo home equity conversion mortgage counseling and file an application with the Office of Tax and Revenue to qualify for the deferral.

This tax deferral differs from the deferral available for low-income homeowners described on the previous page (see tax expenditure #187, "Low-income homeowners") by covering the *entire* property tax bill, rather than just the yearly increase in property tax liability.

Montgomery County allows certain homeowners to defer paying the amount by which their real property tax liability exceeds the amount due the prior year. To qualify, the household must have had gross income of $120,000 or less the previous year, and at least one of the owners must have lived in the home as his or her principal place of residence for the prior five years. Interest on the deferred taxes accrues annually at a rate set by the county. In addition to the District of Columbia, 25 states had some type of tax deferral program in place in 2005.[402]

PURPOSE: The purpose of the tax deferral is to protect low- and moderate-income senior citizens from real property tax burdens that they cannot afford. This provision recognizes that many senior citizens are "house-rich" but "cash-poor," because many senior citizens live on fixed incomes that may not keep with the assessed value of homes.

IMPACT: Senior citizen homeowners with annual household adjusted gross income less than $50,000 benefit from this provision. The deferral violates the principle of horizontal equity because non-elderly homeowners with the household adjusted gross income of less than $50,000 do not receive similar tax relief.

[402] Haveman and Sexton, p. 35.

DEED RECORDATION AND TRANSFER TAX

Deed Recordation and Transfer Tax
Exemptions

189. Educational institutions

District of Columbia Code:	D.C. Official Code § 42-1102(3) for the deed recordation tax D.C. Official Code § 47-902(3) for the transfer tax
Sunset Date:	None
Year Enacted:	1962 (deed recordation tax) and 1980 (transfer tax)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$1,026	$1,026	$1,029	$1,031

DESCRIPTION: Organizations that are exempt from real property taxation in the District of Columbia pursuant to D.C. Official Code § 47-1002 are also exempt from the deed recordation tax and transfer taxes. Educational institutions are among the groups covered under § 47-1002 that qualify for this blanket exemption.

PURPOSE: The purpose of the exemption is to extend the real property tax exemption for educational institutions to the other two taxes related to real property: the deed recordation tax and the transfer tax. As a result, there is uniform treatment under the real property, deed recordation, and transfer taxes for educational institutions.

IMPACT: Educational institutions benefit from this exemption, which would also be expected to have spillover benefits for their employees and students. Moreover, there could be broader benefits to society because education promotes a better-trained workforce and a more informed citizenry.

Deed Transfer Tax
Exemptions

190. Bona-fide gifts to the District of Columbia

District of Columbia Code: D.C. Official Code § 47-902(24)
Sunset Date: None
Year Enacted: 2011

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: Real property that is transferred to the District of Columbia as a "bona fide gift," at the request of the D.C. government and without any consideration for the transfer, is exempt from the real property transfer tax.[403]

PURPOSE: The enactment of this provision was motivated by the transfer of property from PEPCO to the D.C. government in 2008. The property was conveyed as a gift so that the D.C. government could complete a portion of the Metropolitan Branch Pedestrian and Bicycle Trail.[404]

IMPACT: The D.C. government and donors of property are the intended beneficiaries of this exemption. The transfer from PEPCO is the only gift of property to the D.C. government known to have occurred in recent years. A more common way of transferring private land to the District involves the exchange of privately-owned land for a publicly-owned parcel.

[403] The transfer tax on real property is based on consideration paid for the transfer, but when there is no consideration, the tax is based on the fair market value of the property conveyed.

[404] PEPCO was reimbursed by the D.C. government for the $47,850 transfer tax PEPCO paid on transferring the property.

Deed Recordation and Transfer Tax
Exemptions

191. Embassies, chanceries, and associated properties of foreign governments

District of Columbia Code:	D.C. Official Code § 42-1102(3) for the deed recordation tax D.C. Official Code § 47-902(3) for the transfer tax
Sunset Date:	None
Year Enacted:	1962 (deed recordation tax) and 1980 (transfer tax)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$417	$417	$418	$419

DESCRIPTION: Organizations that are exempt from real property taxation in the District of Columbia pursuant to D.C. Official Code § 47-1002 are also exempt from the deed recordation and transfer taxes. Foreign governments are among the groups covered under § 47-1002 that qualify for this blanket exemption, which applies to the embassies and other properties that foreign governments use for diplomatic purposes.

PURPOSE: The purpose of the exemption is to uphold a principle of international law that foreign governments are entitled to exemption from taxation of real property owned by the foreign government and used by its diplomatic mission. Any portion of the property that is not used for diplomatic or consular purposes is not exempt from the District's deed recordation or transfer tax. The exemption also ensures that there is uniform treatment under the real property, deed recordation, and transfer taxes for properties purchased by foreign governments for diplomatic uses.

IMPACT: Foreign governments that own embassies, chanceries, and associated properties in the District of Columbia benefit from this exemption.

Deed Recordation and Transfer Tax
Exemptions

192. Federal government

District of Columbia Code:	D.C. Official Code § 42-1102(2) for the deed recordation tax D.C. Official Code § 47-902 (2) for the transfer tax
Sunset Date:	None
Year Enacted:	1962 (deed recordation tax) and 1980 (transfer tax)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$672	$672	$674	$675

DESCRIPTION: Property acquired by the United States government is exempt from the deed recordation and transfer taxes, unless taxation of the property has been specifically authorized by the U.S. Congress.

PURPOSE: This exemption recognizes the fact that the federal government is immune from taxation by the states or municipalities. This immunity has been established in numerous court decisions, beginning with *McCulloch v. Maryland*, 17 U.S. 316 in 1819, and has been reinforced in other cases including *Clallam County v. United States*, 263 U.S. 341 in 1923; *Cleveland v. United States*, 323 U.S. 329, 333 in 1945; *United States v. Mississippi Tax Commission*, 412 U.S. 363 in 1973; and *United States v. Mississippi Tax Commission*, 421 U.S. 599 in 1975.

IMPACT: The United States government benefits from this exemption.

Deed Recordation and Transfer Tax
Exemptions

193. Other properties exempt from real property taxation

District of Columbia Code:	D.C. Official Code § 42-1102(3) for the deed recordation tax D.C. Official Code § 47-902(3) for the transfer tax
Sunset Date:	None
Year Enacted:	1962 (deed recordation tax) and 1980 (transfer tax)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$923	$923	$926	$928

DESCRIPTION: Properties exempted from the real property tax by D.C. Official Code § 47-1002 also receive a blanket exemption from the deed recordation and transfer taxes.[405] In addition to some major types of tax-exempt properties that are specifically exempted by statute from the deed recordation and transfer tax (churches, educational institutions, embassies, and charitable organizations), there are a number of other institutions that also receive the deed recordation and transfer tax exemptions through this blanket exemption. These institutions, which are included in the estimate of forgone revenue shown above, include non-profit hospitals, libraries, art galleries, and cemeteries.

PURPOSE: The purpose of this exemption is to promote equitable treatment for non-profit institutions under the real property tax, the deed recordation tax, and the transfer tax. In addition, the exemption recognizes and encourages the public benefits provided by many non-profit entities such as hospitals and libraries.

IMPACT: The owners of non-profit hospitals, libraries, art galleries, cemeteries, and other organizations that are exempt from real property taxation in the District of Columbia benefit from this parallel exemption from the deed recordation and transfer taxes.

[405] There are two narrow exceptions to this rule. D.C. law provides that the following tax-exempt properties do not receive corresponding exemptions from the deed recordation and transfer taxes: (1) property for which payments in lieu of taxes (PILOTs) are being made pursuant to a PILOT agreement, and (2) land in the Capper/Carrollsburg PILOT area that is not otherwise exempt from real property taxation.

Deed Recordation Tax
Exemptions

194. Special act of Congress

District of Columbia Code: D.C. Official Code § 42-1102(4)
Sunset Date: None
Year Enacted: 1962

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$367	$367	$368	$368

DESCRIPTION: A deed to property acquired by an institution, organization, corporation, or association entitled to an exemption from real property by a special act of Congress is exempt from the deed recordation tax, provided that the property is acquired "solely for a purpose or purposes for which such special exemption was granted."

A similar exemption applicable to the transfer tax was repealed by D.C. Law 14-282, the "Tax Clarity and Recorder of Deeds Act of 2002," which took effect on April 4, 2003.[406]

PURPOSE: The purpose of this exemption is to extend the deed recordation tax exemption to properties that have been exempted from real property taxation in the District of Columbia by a special act of Congress. Exempting the properties from both taxes promotes uniformity and equity in property taxation.

IMPACT: Owners of property that qualifies for a real property tax exemption in the District of Columbia by a special act of Congress benefit from this exemption. Examples include properties owned by the Daughters of American Revolution, the National Education Association, the American Veterans of World War II, the American Association of University Women, and Woodrow Wilson House.

[406] See section 11(o)(4) of this legislation.

Deed Recordation and Transfer Tax
Exemptions

195. Cooperative housing associations

District of Columbia Code:	D.C. Official Code § 42-1102(14), § 47-3503(a)(2), and § 47-3503(a)(3) for deed recordation tax D.C. Official Code § 47-902(11) and § 47-3503(b)(2) for transfer tax
Sunset Date:	None
Year Enacted:	1983

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$355	$355	$356	$356

DESCRIPTION: A property acquired by a cooperative housing association is exempt from the deed recordation and transfer taxes if at least 50 percent of the units are occupied by households with an annual income no greater than 120 percent of the lower-income guidelines established by the U.S. Department of Housing and Urban Development for the Washington metropolitan area.

As of December 1, 2011, the household income limits ranged from $59,040 for a one-person household to $111,300 for a household with eight or more people. The current limit on the purchase price of the home is $332,000.

The cooperative housing association must receive a credit against the purchase price of the property equal to the total transfer tax that would have been due without the exemption. This provision is necessary because the transfer tax is usually paid by the seller of the property.

Maryland also exempts cooperative housing associations from its property transfer tax.

PURPOSE: The authorizing statute states that, "The purpose of this act is to expand homeownership opportunities for lower-income families to the maximum extent possible at the lowest possible cost to the District of Columbia."[407] The statute further states that, "Expansion of homeownership opportunities for lower income families is beneficial to the public peace, health, safety and general welfare."[408]

IMPACT: Cooperative housing associations with at least 50 percent of units occupied by lower-income households benefit from this provision.

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[407] See D.C. Official Code § 47-3501(7).

[408] See D.C. Official Code § 47-3501(6).

Deed Transfer Tax
Exemptions

196. Inclusionary zoning program

District of Columbia Code: D.C. Official Code § 47-902(23)
Sunset Date: None
Year Enacted: 2007

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$4	$15	$31	$62

DESCRIPTION: Transfers of property to a qualifying low- or moderate-income household pursuant to the Inclusionary Zoning (IZ) program are exempt from the transfer tax on real property. IZ requires an affordable housing set-aside in new developments of 10 or more units, or a substantial rehabilitation that expands an existing building's floor-area ratio (FAR) by 50 percent or more and adds 10 or more units, in exchange for an increase in density. There are exemptions for certain zones and historic districts.

IZ is targeted at households earning less than 50 percent of area median income (AMI), and between 50 percent and 80 percent of AMI, depending on the zoning and the type of construction. The amount of the affordable housing set-aside (which ranges between 8 and 10 percent of the residential space) also varies depending on the zoning and construction type. Affordable units offered through the IZ program have rental or sales price caps that are tied to AMI. In return for providing affordable units, developers receive a 20 percent bonus density.

After housing is built in accordance with the IZ program, the developer or owner of the affordable unit issues a notice of availability to the Department of Housing and Community Development (DHCD), which then holds a lottery to select an eligible household for each unit. Prospective renters and buyers have to submit information about their income and household size, a declaration of eligibility, a mortgage pre-qualification (if applicable), and any other documents required by the Mayor.

PURPOSE: The purpose of the exemption is to further the IZ program's goals of producing affordable housing for residents, creating mixed-income neighborhoods, and increasing homeownership opportunities for low- and moderate-income households.

IMPACT: Low- and moderate-income households are the intended beneficiaries of this provision. As of February 2012, two IZ units had been produced but not had been sold. Thus far, many housing construction projects have been exempt from IZ because of geographic exemptions, because they received development approvals before the effective date of IZ, or because they were subject to housing affordability requirements as a planned unit development[409] or through other D.C. government programs.[410]

[409] A planned unit development enjoys flexibility on design elements such as building height and density if the project offers public benefits related to services including but not limited to affordable housing.

[410] Department of Housing and Community Development, "Inclusionary Zoning Annual Report," March 14, 2011, available at www.dhcd.dc.gov.

Deed Recordation and Transfer Tax
Exemptions

197. Lower-income homeownership households

District of Columbia Code:	D.C. Official Code § 42-1102(12), § 47-3503(a)(1), and § 47-3503(a)(3) for deed recordation tax D.C. Official Code § 47-902(9) and § 47-3503(b)(1) for transfer tax
Sunset Date:	None
Year Enacted:	1983

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$142	$142	$143	$143

DESCRIPTION: Property that is transferred to a "qualifying lower-income homeownership household" is exempt from the deed recordation and transfer taxes. A qualifying lower-income homeownership household must meet two requirements: (1) household income can be no greater than 120 percent of the lower-income guidelines established for the Washington metropolitan area by the U.S. Department of Housing and Urban Development (HUD), and (2) the household must own the property in fee simple or receive at least a 5 percent qualified ownership interest as part of a shared equity financing agreement. The lower-income household must occupy the unit that qualifies for the deed recordation and transfer tax exemption. The fair market value of the property being transferred cannot exceed 80 percent of the median sale price for homes in the District of Columbia.

As of December 1, 2011, the household income limits ranged from $59,040 for a one-person household to $111,300 for a household with eight or more people. The current limit on the purchase price of the home is $332,000.

The lower-income purchaser or the persons acquiring qualified ownership interests under a shared equity financing agreement must receive a credit against the purchase price of the property equal to the total transfer tax that would have been due without the exemption. This provision is necessary because the transfer tax is usually paid by the seller.

PURPOSE: The authorizing statute states that, "The purpose of this act is to expand homeownership opportunities for lower-income families to the maximum extent possible at the lowest possible cost to the District of Columbia."[411] The statute further states that, "Expansion of homeownership opportunities for lower income families is beneficial to the public peace, health, safety and general welfare."[412]

IMPACT: Families with an annual income no greater than 120 percent of the low-income guidelines set by HUD for the Washington metropolitan area benefit from this tax expenditure, provided that they meet the other eligibility criteria described above.

[411] See D.C. Official Code § 47-3501(7).

[412] See D.C. Official Code § 47-3501(6).

Deed Recordation and Transfer Tax
Exemptions

198. Nonprofit housing associations

District of Columbia Code:	D.C. Official Code § 42-1102(13) and § 47-3505(c) for deed recordation tax D.C. Official Code § 47-902(10) and § 47-3505(b) for transfer tax
Sunset Date:	None
Year Enacted:	1983

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$213	$213	$213	$214

DESCRIPTION: Property that is transferred to a "qualifying nonprofit housing organization"[413] is exempt from the deed recordation and transfer taxes if the organization certifies its intent to do the following within the next 36 months: (1) transfer the property to a household with annual income no greater than 120 percent of the lower-income guidelines established by the U.S. Department of Housing and Urban Development for the Washington metropolitan area, (2) transfer at least 35 percent of the units in a multi-family property to households meeting the lower-income standard described above, or (3) transfer the property to a cooperative housing association that will make at least 50 percent of the units available to households meeting the lower-income standard.

As of December 1, 2011, the household income limits ranged from $59,040 for a one-person household to $111,300 for a household with eight or more people. The current limit on the purchase price of the home is $332,000.

An additional requirement for the transfer tax exemption is that the non-profit housing association must receive a credit against the purchase price of the property in an amount equal to the transfer tax that would have been due without the exemption. This provision is necessary because the transfer tax is usually paid by the seller.

PURPOSE: The authorizing statute states that, "The purpose of this act is to expand homeownership opportunities for lower income families to the maximum extent possible at the lowest possible direct cost to the District of Columbia."[414] The statute further states that, "Additional support for nonprofit housing organizations … through property tax abatements and other incentives can serve to expand homeownership for lower income families at little or no additional cost to the District of Columbia."[415]

IMPACT: Nonprofit housing associations and the lower-income households they serve benefit from this provision.

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[413] A "qualifying nonprofit housing association" has been approved by the U.S. Internal Revenue Service as exempt from federal income taxation under section 501(c)(3) or 501(c)(4) of the Internal Revenue Code.

[414] See D.C. Official Code § 47-3501(7).

[415] See D.C. Official Code § 47-3501(5).

Deed Recordation and Transfer Tax
Exemptions

199. Resident management corporations

District of Columbia Code:	D.C. Official Code § 42-1102(20) and § 47-3506.01(b)(1) for recordation tax D.C. Official Code § 47-902(15) and § 47-3506.01(b)(2) for transfer tax
Sunset Date:	None
Year Enacted:	1992

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: Public housing that is transferred to a qualifying resident management corporation is exempt from the deed recordation and transfer taxes. A resident management corporation is a non-profit corporation in which public housing residents are the sole voting members.

PURPOSE: The purpose of the exemption is to expand the opportunities of low-income families who live in a public housing project to become owners of the housing. Resident ownership is also expected to help stabilize neighborhoods by giving residents a greater stake in the safety and upkeep of the community.

IMPACT: Resident management corporations and the individuals they serve are the intended beneficiaries of this provision. According to the D.C. Housing Authority, the Kenilworth-Parkside project is the only property that has been transferred to a resident management corporation (this transfer took place in 1992). Presently, no exemptions are projected for the FY 2012 through FY 2015 period.

Deed Recordation and Transfer Tax
Exemptions

200. Charitable organizations

District of Columbia Code:	D.C. Official Code § 42-1102(3) for the deed recordation tax D.C. Official Code § 47-902 (3) for the transfer tax
Sunset Date:	None
Year Enacted:	1962 (deed recordation tax) and 1980 (transfer tax)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$1,539	$1,539	$1,543	$1,546

DESCRIPTION: Organizations that are exempt from real property taxation in the District of Columbia pursuant to D.C. Official Code § 47-1002 are also exempt from the deed recordation tax and transfer taxes. Charitable entities are among the groups covered by § 47-1002 that qualify for this blanket exemption.

PURPOSE: The purpose of the exemption is to extend the real property tax exemption for charitable entities to the other two taxes on real property: the deed recordation tax and the transfer tax. As a result, there is uniform treatment under the real property, deed recordation, and transfer taxes for charitable organizations.

IMPACT: Charitable entities benefit from this exemption, which would also be expected to have spillover benefits for the people who receive goods or services from the charitable organizations.

Deed Recordation and Transfer Tax
Exemptions

201. Churches, synagogues, and mosques

District of Columbia Code:	D.C. Official Code § 42-1102(3) for the deed recordation tax D.C. Official Code § 47-902(3) for the transfer tax
Sunset Date:	None
Year Enacted:	1962 (deed recordation tax) and 1980 (transfer tax)

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$256	$256	$257	$258

DESCRIPTION: Organizations that are exempt from real property taxation in the District of Columbia pursuant to D.C. Official Code § 47-1002 are also exempt from the deed recordation tax and transfer taxes. Churches, synagogues, and mosques are among the groups covered under § 47-1002 that qualify for this blanket exemption.

PURPOSE: The purpose of the exemption is to extend the real property tax exemption for places of worship to the two other taxes related to real property: the deed recordation tax and the transfer tax. As a result, there is uniform treatment under the real property, deed recordation, and transfer taxes for churches, synagogues, mosques, and other places of worship.

IMPACT: Churches, synagogues, mosques, and other places of worship benefit from this exemption.

Deed Recordation and Transfer Tax
Exemptions

202. Tax-exempt entities subject to a long-term lease

District of Columbia Code:	D.C. Official Code § 42-1102(27) for the deed recordation tax D.C. Official Code § 47-902(21) for the transfer tax
Sunset Date:	None
Year Enacted:	2003

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	no estimate	no estimate	no estimate	no estimate

DESCRIPTION: A property is exempt from the deed recordation and transfer taxes it is subject to a lease or ground rent for a term of at least 30 years, and if the lessor would have been exempt from real property taxation under D.C. Official Code § 47-1002 if it had owned the property outright.

PURPOSE: This exemption was created to provide equitable treatment under the deed recordation and transfer taxes for properties that are under the control of organizations that are exempt from the real property tax. This provision extends the exemption these entities receive when they acquire a property in fee simple to the conveyance of property that is subject to a lease or ground rent of at least 30 years.

IMPACT: Organizations that are exempt from the real property tax and assume control of a property through a lease of 30 years or more benefit from this provision. It was impossible to estimate the revenue loss due to this exemption because deed recordation and transfer tax exemptions are not categorized in a way that identifies tax-exempt entities subject to a long-term lease.

SALES TAX

Sales Tax
Exemptions

203. Energy products used in manufacturing

District of Columbia Code: D.C. Official Code § 47-2005(11) and (11A)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$3,705	$3,551	$3,551	$3,551

DESCRIPTION: Gross receipts from the sale of natural or artificial gas, oil, electricity, solid fuel, or steam are exempt from the sales tax when these energy products are used for (1) manufacturing, assembling, processing, or refining, or (2) preparing or refrigerating goods when used in a restaurant, including a hotel restaurant.

The exemption for energy used to produce goods in a restaurant took effect on January 1, 2010. The rest of the exemption for energy used in manufacturing dates back to 1949, when the District's sales tax was first established.

Similar exemptions are common in many states, but they are sometimes provided under broader sales tax exemptions. For example, Virginia exempts manufacturing and agricultural businesses from paying sales taxes on their purchases of materials, machinery, and equipment, based on the principle that these inputs are included in the value of goods that are taxed at the retail level.

PURPOSE: The purpose of the exemption is to recognize that energy products used in manufacturing are ordinary and necessary expenses in the production process rather than outputs offered for retail sale. The sales tax is intended to be a consumption tax rather than a tax on intermediate goods and services that are consumed or directly used in production.

IMPACT: Manufacturing businesses and restaurants benefit from the exemption. Nevertheless, the exemption creates questions of horizontal equity because many service industries use energy products as inputs but do not receive a sales tax exemption for the costs of natural or artificial gas, oil, electricity, solid fuel, or steam that they use.

Sales Tax
Exemptions

204. Internet access service

District of Columbia Code: D.C. Official Code § 47-2001(n)(2)(F)
Sunset Date: None
Year Enacted: 1999

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$3,326	$3,326	$3,326	$3,326

DESCRIPTION: Gross receipts from sales of Internet access service are exempt from the sales tax. "Internet access service" is defined as a service that "enables users to access content, information, electronic mail, or other services offered over the Internet and may also include access to proprietary content, information, and other services as part of a package of Internet access services offered to customers."[416]

Internet access service does not include (1) the sales of data processing and information services that do not involve content, information, electronic mail, or other services offered over the Internet, or (2) telecommunication services. The exemption also does not cover online purchases.

State and local taxation of Internet access has been barred by the 1998 Internet Tax Freedom Act approved by Congress. The federal Act has since been extended twice and is in effect until November 1, 2014. Even if the federal Act lapses, the local exemption will remain in place unless the Mayor and Council decide otherwise.

PURPOSE: Proponents of the tax exemption for Internet access contend that the exemption will stimulate the continued growth of a technology that has very positive economic and social impacts.

IMPACT: Individuals or firms selling Internet access service benefit from this exemption, as do their customers. Nevertheless, sales tax exemptions of this nature may create economic inefficiencies (by favoring the consumption of some items rather than others based on the tax, rather than the value of the product) and raise issues of horizontal equity. For example, some experts argue that it is inequitable to tax the computer hardware that provides Internet access but not the Internet access itself.

[416] See D.C. Official Code § 47-2001(n)(2)(F).

Sales Tax
Exemptions

205. Materials used in development of a qualified supermarket

District of Columbia Code: D.C. Official Code § 47-2005(28)
Sunset Date: None
Year Enacted: 2000

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$530	$528	$549	$571

DESCRIPTION: Gross receipts from the "sales of building materials related to the development of a qualified supermarket" are exempt from the sales tax. A qualified supermarket is located in a census tract where more than half of the households have incomes below 60 percent of the area median, as determined by the U.S. Department of Housing and Urban Development.

PURPOSE: The purpose of the exemption is to encourage the construction and operation of supermarkets in underserved areas of the city.

IMPACT: Individuals and organizations that are constructing and operating supermarkets in the target areas benefit from this provision. Consumers are also intended beneficiaries of this exemption because it is designed to provide an incentive for supermarkets to locate in areas that lack them. The exemption violates the principle of horizontal equity because other businesses locating in the target areas do not receive an exemption on the purchase of building materials.

The estimate of forgone revenue shown above is based on an assumption that two qualified supermarkets will be constructed each year.

Sales Tax
Exemptions

206. Professional and personal services

District of Columbia Code: D.C. Official Code § 47-2001(n)(2)(B)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$250,508	$255,268	$261,394	$283,810

DESCRIPTION: Gross receipts from sales of professional, insurance, or personal services are exempt from the sales tax. Examples of the sales that are exempt include accounting and bookkeeping, architectural, consulting, dental, engineering, legal, and physician services.

Maryland and Virginia provide similar exemptions to professional, insurance, and personal services. According to the Federation of Tax Administrators, professional services are taxed in only seven states.[417]

PURPOSE: This exemption is part of most state tax systems because the sales tax originated as a levy on purchases of tangible personal property by both individuals and businesses, rather than a tax on all consumption. Even as the service economy has grown, policymakers have usually chosen to exempt professional, insurance, or personal services from the sales tax.

IMPACT: Firms providing professional, insurance, or personal services benefit from this exemption, as do the consumer of these services. Nevertheless, many experts have pointed out that the substantial growth of services as a percentage of the economy means that a large share of consumption expenditures is not taxed, and that tax rates on tangible goods may therefore be higher than they otherwise would be.[418] Moreover, the exemption violates the principle of horizontal equity because two taxpayers with equal levels of consumption will pay different amounts of sales tax if one consumes more professional services than the other.

[417] Federation of Tax Administrators, "FTA Survey of Services Taxation – Update," July 2008, available at www.taxadmin.org.

[418] See for example Virginia Joint Legislative Audit and Review Commission, Review of the Effectiveness of Virginia Tax Preferences, report to the Governor and General Assembly of Virginia (January 2012), pp. 20-22.

Sales Tax
Exemptions

207. Qualified high-technology companies: certain sales

District of Columbia Code: D.C. Official Code § 47-2001(n)(2)(G)
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$631	$644	$657	$670

DESCRIPTION: The gross receipts from certain sales of intangible property or services that are otherwise taxable are exempt from the sales tax, if the sale is made by a qualified high technology company within the District of Columbia. The list of tax -exempt products and services includes website design, maintenance, hosting, or operation; Internet-related consulting, advertising, or promotion services; graphic design; banner advertising; subscription services; and Internet website design and maintenance services. This exemption does not apply to telecommunication service providers.

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies.

This sales tax exemption is part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[419]

PURPOSE: The purpose of this exemption is to encourage the growth of high-technology companies in the District of Columbia and thereby expand the District's economy and employment base.

IMPACT: High-technology companies in the District of Columbia benefit from this provision. The exemption violates the principle of horizontal equity because companies in other industries do not receive similar treatment (nor do companies that sell similar products but do not meet the definition of a qualified high-technology company).

[419] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, employment credits, property tax abatements, and personal property tax exemptions, are discussed elsewhere in this report.

Sales Tax
Exemptions

208. Qualified high-technology companies: technology purchases

District of Columbia Code: D.C. Official Code § 47-2005(31)
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$172	$175	$179	$183

DESCRIPTION: Gross receipts from the certain sales to a qualified high-technology company are exempt from the sales tax. The relevant items that are subject to the exemption include "computer software or hardware, and visualization and human interface technology equipment, including operating and applications software, computers, terminals, display devices, printers, cable, fiber, storage media, networking hardware, peripherals, and modems when purchased for use in connection with the operation of the Qualified High Technology Company."

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies.

This sales tax exemption is part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[420]

Maryland and Virginia do not provide similar exemptions, but Virginia offers a sales tax exemption for purchases of computer servers and other types of equipment used by data centers.

PURPOSE: The purpose of the exemption is to encourage the growth of high-technology companies in the District of Columbia and thereby expand the District's economy and employment base.

IMPACT: High-technology companies in the District of Columbia benefit from this provision. The exemption violates the principle of horizontal equity because companies in other industries do not receive similar treatment for their purchases.

[420] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, employment credits, property tax abatements, and personal property tax exemptions, are discussed elsewhere in this report.

Sales Tax
Exemptions

209. Transportation and communication services

District of Columbia Code: D.C. Official Code § 47-2001(n)(2)(A)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$43,231	$42,341	$43,485	$47,214

DESCRIPTION: Gross receipts from sales of transportation and communication services are exempt from the sales tax. The exemption does not include the sales of data processing services, information services, or local telephone service.

Maryland and Virginia provide similar exemptions for transportation and communication services.

PURPOSE: This exemption was included in the original establishment of the D.C. sales tax in 1949, likely because the sales tax originated as a levy on purchases of tangible personal property by both individuals and businesses, rather than taxes on all consumption. Even as the service economy has grown, policymakers continue to exempt most services from the sales tax.

IMPACT: Firms providing transportation and communication services benefit from this exemption. The exemption violates the principle of horizontal equity because firms in other industries do not receive similar treatment.

Sales Tax
Exemptions

210. Federal and D.C. governments

District of Columbia Code: D.C. Official Code § 47-2005(1)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$182,625	$184,451	$187,771	$192,278

DESCRIPTION: Gross receipts from sales to the United States government, the District of Columbia government, or any instrumentalities of either government, are exempt from the sales tax, except for sales to national banks and federal savings and loan associations.

Maryland and Virginia also exempt the state and its political subdivisions (such as counties, cities, townships) from the sales tax, in addition to the federal government exemption.

PURPOSE: The exemption for sales to the U.S. government recognizes the federal government's immunity from taxation by the states or municipalities. This immunity has been established in numerous court decisions, beginning with *McCulloch v. Maryland*, 17 U.S. 316 in 1819, and has been reinforced in other cases including *Clallam County v. United States*, 263 U.S. 341 in 1923; *Cleveland v. United States*, 323 U.S. 329, 333 in 1945; *United States v. Mississippi Tax Commission*, 412 U.S. 363 in 1973; and *United States v. Mississippi Tax Commission*, 421 U.S. 599 in 1975.

The sales tax exemption for the District government eliminates a cost that would ultimately be borne by D.C. taxpayers, and can be justified on the grounds that the local government is usually an intermediate consumer of goods and services rather than the end user.

IMPACT: The federal government and the District of Columbia government benefit from this exemption.

Sales Tax
Exemptions

211. Medicines, pharmaceuticals, and medical devices

District of Columbia Code: D.C. Official Code § 47-2005(14) and (15)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$9,636	$9,636	$9,636	$9,636

DESCRIPTION: Gross receipts from sales of medicines, pharmaceuticals, drugs, and medical devices are exempt from the sales tax. Both Maryland and Virginia exempt medicine, pharmaceuticals, and medical supplies from the sales tax, which is also a standard practice nationwide. [421] However, D.C., Maryland, and Virginia are among only 11 states that also exempt non-prescription drugs.[422]

PURPOSE: The purpose of the exemption is to make the sales tax more equitable by exempting necessities that absorb a relatively large share of the income of low-income households, and to avoid adding to the expense of potentially life-saving medicines, drugs, and medical devices. In addition, the exemption protects the elderly and people in poor health, who spend more for medical care, drugs, and medical products.

IMPACT: The sellers and purchasers of medicines, pharmaceuticals, drugs, and medical devices benefit from this exemption, as do consumers – particularly those with high medical costs such as the elderly and individuals with chronic conditions. Nevertheless, the exemption may not be well targeted at helping low-income individuals and families because it is available to all taxpayers. Data on consumer expenditures show that out-of-pocket expenditures on drugs and medical care rise along with income.[423]

Nevertheless, Virginia's Joint Legislative Audit and Review Commission (JLARC) concluded that the sales tax exemption for medicine and other health products provides significant benefits to the elderly. In examining the impact of the exemption in Virginia, JLARC stated that, "Average out-of-pocket reductions in tax liability to households with at least one member 65 or older was $66 in 2008, which was above the statewide average ($38) for all households. Their savings were enough to enable them to purchase a year-and-a-half's worth of prescription drugs for common conditions such as arthritis or diabetes, according to prices under a major retailer's discount prescription drug program."[424]

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[421] John Due and John Mikesell, "Retail Sales Tax, State and Local" in *The Encyclopedia of Taxation and Tax Policy*, Second Edition, Joseph Cordes, Robert Ebel, and Jane Gravelle, eds. (Washington, D.C.: The Urban Institute Press, 2005), p. 337.

[422] Federation of Tax Administrators, "State Sales Tax Rates and Food & Drug Exemptions," available at www.taxadmin.org.

[423] Virginia Joint Legislative Audit and Review Commission, p. 33.

[424] Virginia Joint Legislative Audit and Review Commission, pp. 33-34.

Sales Tax
Exemptions

212. Groceries

District of Columbia Code:	D.C. Official Code § 47-2001(n)(2)(E)
Sunset Date:	None
Year Enacted:	1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$56,299	$57,368	$59,491	$64,593

DESCRIPTION: Gross receipts from sales of food or drinks that are defined as eligible foods under the federal Supplemental Nutrition Assistance Program (SNAP, which was formerly known as the "Food Stamp" program) are exempt from sales tax, except sales of food or drink for immediate consumption or the sale of soft drinks.[425] Snack food is exempt from the sales tax, due to a statutory change that the District adopted in 2001.[426]

Maryland exempts groceries from the sales tax, while in Virginia groceries are subject to a sales tax of 2.5 percent instead of the standard 5.0 percent rate. Virginia is one of only 14 states to impose the sales tax on food: seven of these states apply the general rate, while seven charge a lower rate.[427] Several states that tax food also provide a rebate or tax credit to protect low-income households.

PURPOSE: The purpose of the exemption is to make the sales tax more equitable by exempting necessities that absorb a large share of the income of low-income households.

IMPACT: All residents benefit from the exemption of groceries from the sales tax, but the exemption is particularly important for low-income individuals and families. Some have observed that the benefit for low-income families is smaller than one might expect, because food purchase made through the SNAP program are already exempt from taxation.

Some experts further contend that sales tax exemptions and reductions for food are poorly targeted because they do not depend on income. Virginia's Joint Legislative Audit and Review Commission reported that households earning more than $70,000 accounted for 44 percent of Virginia households in 2008, but claimed 58 percent of the reduction in tax liability from the partial sales tax exemption for food. At the same time, households earning less than $20,000 comprised 14 percent of Virginia households, but received only 7 percent of the total benefit from the lower tax rate.[428]

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[425] Food prepared for immediate consumption is taxed at a 10 percent rate, compared to the 5.75 percent general sales tax rate.

[426] This change was part of D.C. Law 13-305, the "Tax Clarity Act of 2000, which took effect on June 9, 2001.

[427] Federation of Tax Administrators, "State Sales Tax Rates and Food & Drug Exemptions," available at www.taxadmin.org.

[428] Virginia Joint Legislative Audit and Review Commission, p. 33.

Sales Tax
Exemptions

213. Materials used in war memorials

District of Columbia Code: D.C. Official Code § 47-2005(16)
Sunset Date: None
Year Enacted: 1957

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: Gross receipts from the "sales of material to be incorporated permanently in any war memorial authorized by Congress to be erected on public grounds of the United States" are exempt from the sales tax.

PURPOSE: The purpose of the exemption is to facilitate the construction of war memorials on public grounds in the District of Columbia.

IMPACT: The exemption benefits the U.S. government by providing a sales tax exemption for materials used in the construction for war memorials that are authorized by Congress and built on federally-owned land. There is no projected revenue loss from this exemption during the FY 2012 through FY 2015 period because there are no war memorials planned for construction, according to the National Capital Planning Commission.

At the time of this writing, legislation was pending in Congress (H.R. 938 and S. 253) that would re-dedicate the District of Columbia War Memorial as both a U.S. and District of Columbia World War I Memorial, but had not come to a vote in either chamber. If such legislation were enacted, modifications to the existing memorial might be needed. The World War II Memorial, dedicated in 2004, is the most recent war memorial constructed in Washington, D.C.

Sales Tax
Exemptions

214. Non-profit (501(c)(4)) organizations

District of Columbia Code: D.C. Official Code § 47-2005(22)
Sunset Date: None
Year Enacted: 1987

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$31,147	$31,833	$32,692	$35,496

DESCRIPTION: Gross receipts from sales to an organization that is exempt from federal corporate income tax under section 501(c)(4) of the Internal Revenue Code are exempt from District of Columbia sales taxation. Organizations covered by section 501(c)(4) include "civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes."[429]

Maryland and Virginia exempt non-profit organizations from the sales tax, as do all but five states with a broad-based sales tax.[430]

PURPOSE: The purpose of the exemption is to support the activities of non-profit organizations that promote social welfare.

IMPACT: Organizations that are tax-exempt under section 501(c)(4) of the Internal Revenue Code, and the people those organizations serve, benefit from this exemption.

In a recent study, the Virginia Joint Legislative Audit and Review Commission (JLARC) found that the rate of increase in non-profit activity (as measured by per-capita expenditures) did not change significantly after 2004, when statutory changes broadened the number of non-profits eligible for Virginia's sales tax exemption. In fact, JLARC found that many charitable non-profits operating in Virginia did not use the exemption. Nevertheless, JLARC concluded that the exemption helps organizations that meet important needs such as emergency medical services, food, and housing assistance, and that the non-profits which provide the services reduce the state's burden of directly providing or funding the services.[431]

[429] See 26 U.S.C. 501(c)(4)(A).

[430] Virginia Joint Legislative Audit and Review Commission, p. 62.

[431] Virginia Joint Legislative Audit and Review Commission, pp. 58-61.

Sales Tax
Exemptions

215. Semi-public institutions

District of Columbia Code: D.C. Official Code § 47-2005(3)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$46,364	$47,384	$48,663	$50,561

DESCRIPTION: Gross receipts from sales to semi-public institutions are exempt from the sales tax if (1) the institution obtains a certificate from the Mayor stating that the institution is entitled to the sales tax exemption,[432] (2) the vendor keeps a record of each sale, (3) the institution is located in the District of Columbia, and (4) the property or services purchased are for use or consumption, or both, in maintaining and operating the institution for the purpose for which it was established, or for honoring the institution or its members.

A semi-public institution is defined as "any corporation, and any community chest, fund, or foundation, organized exclusively for religious, scientific, charitable, or educational purposes, including hospitals, no part of the net earnings of which inures to the benefit of any private shareholder or individual."[433]

Maryland and Virginia exempt non-profit organizations from the sales tax, as do all but five states with a broad-based sales tax.[434]

PURPOSE: The purpose of the exemption is to support the mission of private, non-profit institutions that provide religious, educational, social, philanthropic and other services that have important public benefits. The exemption recognizes and encourages the public benefits provided by many non-profit entities such as hospitals and libraries.

IMPACT: Semi-public (non-profit) institutions, and the people they serve, benefit from this exemption. In a recent study, the Virginia Joint Legislative Audit and Review Commission (JLARC) found that the rate of increase in non-profit activity (as measured by per-capita expenditures) did not change significantly after 2004, when statutory changes broadened the number of non-profits eligible for Virginia's sales tax exemption. In fact, JLARC found that many charitable non-profits operating in Virginia did not use the exemption. Nevertheless, JLARC concluded that the exemption helps organizations that meet important needs such as emergency medical services, food, and housing assistance, and that the non-profits which provide the services reduce the state's burden of directly providing or funding the services.[435]

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[432] The relevant form is Form FR-551, "District of Columbia Certificate of Exemption."

[433] See D.C. Official Code § 47-2001(r).

[434] Virginia Joint Legislative Audit and Review Commission, p. 62.

[435] Virginia Joint Legislative Audit and Review Commission, pp. 58-61.

Sales Tax
Exemptions

216. Miscellaneous

District of Columbia Code: D.C. Official Code § 47-2005
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	no estimate	no estimate	no estimate	no estimate

DESCRIPTION: D.C. law includes includes a number of sales-tax exemptions that are relatively small in scope. These miscellaneous exemptions cover gross receipts from (1) sales of materials and services to the printing clerks of the U.S. House of Representatives, and sales of materials and services by the printing clerks, (2) casual and isolated sales by a vendor who is not regularly engaged in the business of retail sales, (3) sales of food, beverages, and other goods made for use in the U.S. House of Representatives cloakrooms, and sales of food, beverages, and other goods made by anyone involved in operating the cloakrooms, (4) sales of food or beverages on a train, airline, or other form of transportation operating in interstate commerce, (5) food or drink that is delivered and sold without profit by a non-profit volunteer organization to persons who are confined to their homes, (6) sales of food or drink made by a senior citizen residence to the residents, guests, and employees of the senior residence, (7) sales of vessels that are subject to Article 29 of the Police Regulations, (8) sales of residential cable television services and commodities,[436] (9) sales of printing services and tangible personal property to a publisher that prints and distributes its own newspaper in the District of Columbia free of charge, (10) sales of two-way land mobile radios used for taxicab dispatch and communication, (11) sales of material or equipment used in the construction, repair, or alteration of real property, provided that the materials are temporarily stored in the District of Columbia for not longer than 90 days in order to transport the property outside the District for use solely outside the District, and (12) sales by the U.S. government or the District government.

PURPOSE: The miscellaneous exemptions serve a variety of purposes, including (1) avoiding an administrative burden on those who sell goods or services infrequently or incidentally, (2) preventing double-taxation for certain goods or services subject to other taxes when they are sold, (3) exempting goods or carriers that are passing through the District through interstate commerce or transportation, and (4) promoting the purchase of certain items.

IMPACT: Various groups of vendors and consumers benefit from these exemptions, as described above. There may also be a benefit to the Office of Tax and Revenue, because the cost of collecting sales tax on incidental or unusual transactions might exceed the amount of revenue generated. There is no estimate of the forgone revenue for these provisions, because most of the individual items are very small and difficult to estimate.

[436] These sales are subject to a gross receipts tax.

Sales Tax
Exemptions

217. Motor vehicle fuels

District of Columbia Code: D.C. Official Code § 47-2005(20)
Sunset Date: None
Year Enacted: 1981

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$21,616	$21,832	$22,050	$22,271

DESCRIPTION: Gross receipts from sales of motor vehicle fuels are exempt from the sales tax, provided that the fuels are subject to the motor vehicle fuels tax. Both Maryland and Virginia exempt motor vehicle fuels from the sales tax.

PURPOSE: The purpose of the exemption is to avoid the double taxation of motor fuels.

IMPACT: Motor vehicle owners benefit from this exemption.

Sales Tax
Exemptions

218. Public utility companies

District of Columbia Code: D.C. Official Code § 47-2005(5)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$89,847	$89,847	$89,847	$89,847

DESCRIPTION: Gross receipts from sales to a utility or a public-service company are exempt from the sales tax, provided that (1) the sales are for use or consumption in furnishing a service or commodity, and (2) the charges from furnishing the service or commodity are subject to a gross receipts tax or mileage tax in the District of Columbia. Both Maryland and Virginia provide similar exemptions.

PURPOSE: The purpose of the exemption is to protect utilities and public-service companies from double taxation. Because utilities and public-service companies are subject to a gross receipts tax, the value of the purchases made to provide utility service are already included in the base of the gross receipts tax.

IMPACT: Utility and public-service companies benefit from this exemption, as do their customers who would presumably bear some of the burden of the tax through higher rates.

Sales Tax
Exemptions

219. State and local governments

District of Columbia Code: D.C. Official Code § 47-2005(2)
Sunset Date: None
Year Enacted: 1949

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	minimal	minimal	minimal	minimal

Note: "Minimal" means that the forgone revenue is estimated as less than $50,000 per year, although precise data are lacking.

DESCRIPTION: Gross receipts from sales to a state or any of its political subdivisions (counties, cities, townships) are exempt from the sales tax, provided that the state grants a similar exemption to the District of Columbia. The term "state" refers to the states, territories, and possessions of the United States.

PURPOSE: The purpose of the exemption is to recognize that purchases made by state and local governments are not meant for final consumption, but rather as inputs to the provision of goods and services by those governments.

IMPACT: State and local governments benefit from the exemption, as do the taxpayers in those jurisdictions. The District of Columbia also benefits indirectly, because the District will not receive an exemption from the sales tax in other jurisdictions if it does not provide a reciprocal exemption.

Sales Tax
Exemptions

220. Valet parking services

District of Columbia Code:	D.C. Official Code § 47-2001 (n)(1)(L)(iv) and § 47-2001 (n)(2)(H)
Sunset Date:	None
Year Enacted:	2002

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$390	$383	$393	$413

DESCRIPTION: Gross receipts from sales of valet parking services are exempt from the sales tax.

PURPOSE: The District's sales tax generally includes "the sale of or charge for the service of parking, storing, or keeping motor vehicles or trailers."[437] Nevertheless, the District had never levied the tax on valet parking services, and policymakers decided to codify the sales tax exemption for valet parking services.[438]

IMPACT: Valet parking providers and their customers benefit from this exemption. As of February 2012, the District Department of Transportation reported that 89 valet parking permits were in effect. The estimated revenue loss from the exemption for fiscal years 2012 through 2015 is based on assumptions about the number of days each valet parking establishment is open and the money collected per day.

[437] See D.C. Official Code § 47-2001(n)(1)(L).

[438] Office of the Chief Financial Officer, "Fiscal Impact Statement: 'Fiscal Year 2003 Budget Support Act of 2002,'" June 4, 2002, p. 7.

INSURANCE PREMIUM TAX

Insurance Premium Tax
Credit

221. Certified capital investment by insurance companies

District of Columbia Code: D.C. Official Code § 31-5233
Sunset Date: None
Year Enacted: 2004

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$9,200	$9,200	$4,000	$0

DESCRIPTION: Insurance companies that invest in a certified capital company (CAPCO) can receive insurance premium tax credits equal to the amount of the insurance company's total debt and equity investment in the CAPCO. By allowing insurance companies to claim premium tax credits, the District generates a pool of investment capital.

CAPCOs must apply for certification from the Department of Insurance, Securities, and Banking (DISB), and must demonstrate that they meet statutory requirements for equity capitalization, venture capital experience, and other criteria. DISB has certified three CAPCOs.

The CAPCOs are required to invest the insurance company funds in qualified small businesses that are headquartered and conduct their principal business operations in the District, or that certify in an affidavit that they will relocate their headquarters and principal business operations to the District within 90 days after receiving an initial investment from a CAPCO. At least 25 percent of the employees of a qualified small business must live in the District, and at least 75 percent of their employees must work in the District. Qualified small businesses must also certify in an affidavit that they are unable to obtain conventional financing.

Amendments to the CAPCO statute enacted in 2010[439] created four tiers of qualified businesses, based on their primary line of business and the location of their headquarters. The size of the credit earned by a CAPCO will depend on the tier of business; for example, each dollar invested in a Tier One business will yield a credit of $1.25. The amendments also require CAPCOs to invest all of their certified capital within 10 years of being awarded insurance premium tax credits. If a CAPCO fails to make the full investment within 10 years, it is barred from using its certified capital to pay its management fees.

In any tax year, an insurance company may not claim insurance premium tax credits that exceed 25 percent of its premium tax liability, but the unused premium tax credits can be carried forward indefinitely until they are utilized. There is an aggregate limit of $50 million on the premium tax credits that may be granted and a $12.5 million limit per year. Tax year 2009 was the first year that insurance companies could claim the credit.

CAPCO programs have been adopted in eight other states, but not in Maryland or Virginia.[440]

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[439] D.C. Law 18-181, the "Certified Capital Companies Improvement Amendment Act of 2010," took effect on May 27, 2010.

[440] This information is from www.capcoprogram.com.

PURPOSE: The purpose of the credit is to encourage private capital investment in new or expanding small businesses in the District of Columbia. More generally, the CAPCO program is intended to strengthen and expand the District's economic and tax base.

IMPACT: The impact of the CAPCO program has been the subject of some dispute. The D.C. Auditor concluded in a 2009 report that the CAPCO program was ineffective, having created only 31 jobs over four years, and recommended termination of the program.[441] Professor Stephen Fuller of George Mason University offered a more optimistic assumption that same year, contending that CAPCO "has achieved its initial goals … in spite of a declining economic environment and the collapse of the conventional capital markets." Fuller credited the program with supporting early-stage businesses and helping those businesses to attract additional capital.[442]

In a report issued in 2010, the Council's Committee on Public Services and Consumer Affairs concluded that the program suffered from "misaligned incentives" and offered "little in the way of risk protection for the District government" from poor investment decisions by the CAPCOs.[443] While approving amendments designed to strengthen the program, the Committee stated that, "(U)nder no circumstances should the duration of the CAPCO program be extended through the allocation of any additional premium tax credits beyond those allocated pursuant to the original act."[444]

According to the Department of Insurance, Securities, and Banking, $23 million in CAPCO tax credits had been claimed by the end of 2010 (data for 2011 were not yet final at the time of this writing). The estimates of forgone revenue for the FY 2012-2015 period are based on an extrapolation of the data from 2009 and 2010 as well as preliminary data for 2011.

[441] Office of the District of Columbia Auditor, "Certified Capital Companies Program," March 12, 2009, available at www.dcauditor.org.

[442] Stephen Fuller, "D.C. CAPCO: Progress Report and Assessment," prepared for The D.C. Coalition for Capital, April 3, 2009.

[443] Council of the District of Columbia, Committee on Public Services and Consumer Affairs, Report on Bill 18-402, the "Certified Capital Companies Improvement Amendment Act of 2010," February 24, 2010, pp. 3-4.

[444] Council of the District of Columbia, Committee on Public Services and Consumer Affairs, Report on Bill 18-402, the "Certified Capital Companies Improvement Amendment Act of 2010," February 24, 2010, pp. 6-7.

PERSONAL PROPERTY TAX

Personal Property Tax
Exemptions

222. Digital audio radio satellite companies

District of Columbia Code: D.C. Official Code § 47-1508(a)(8)
Sunset Date: None
Year Enacted: 2000

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	no estimate	no estimate	no estimate	no estimate

DESCRIPTION: The personal property of a digital audio radio satellite service company with a license granted by the Federal Communications Commission is exempt from the personal property tax, provided that the company is subject to a gross receipts tax.

PURPOSE: The purpose of the exemption is to prevent double taxation.

IMPACT: Digital audio radio satellite companies benefit from this exemption. The Office of Revenue Analysis (ORA) cannot estimate the revenue forgone from the exemption, because there is only one provider of digital radio service located in the District of Columbia. ORA follows the policy of the U.S. Internal Revenue Service which states that, "No statistical tabulation may be released with cells containing data from fewer than three returns," in order to protect the confidentiality of individual tax records.[445]

[445] U.S. Internal Revenue Service, Publication 1075, "Tax Information Security Guidelines for Federal, State, and Local Agencies and Entities" (August 2010), p. 66.

Personal Property Tax
Exemptions

223. Qualified high-technology companies

District of Columbia Code: D.C. Official Code § 47-1508(a)(10)
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$183	$182	$182	$182

DESCRIPTION: The personal property of a "qualified high technology company" is exempt from personal property taxation for the 10 years beginning in the year of purchase. The exemption applies to personal property purchased after December 31, 2000. In addition, qualified personal property leased to a qualified high technology company under a lease-purchase or security-purchase agreement is also exempt from personal property tax for a period not to exceed 10 years.[446]

A high-technology company is considered "qualified" if it derives at least 51 percent of its gross revenue from technology-related goods and services such as Internet-related services and sales; information and communication technologies, equipment and systems that involve advanced computer software and hardware; and advanced materials and processing technologies.

The personal property tax exemption is part of a package of incentives for high-technology firms authorized by D.C. Law 13-256, the "New E-conomy Transformation Act of 2000."[447]

PURPOSE: The purpose of this exemption is to encourage the growth of high-technology companies in the District of Columbia and thereby expand the District's economy and employment base.

IMPACT: High-technology companies in the District of Columbia benefit from this provision. The exemption violates the principle of horizontal equity because businesses in other industries do not receive the same treatment.

[446] The property is not exempt from the personal property tax if it isleased to a qualified high-technology company under an operating lease.

[447] The other incentives, which include the exclusion of certain capital gains, increased expensing of capital assets, a reduced corporate tax rate, employment credits, property tax abatements, and sales tax exemptions, are discussed elsewhere in this report.

Personal Property Tax
Exemptions

224. Qualified supermarkets

District of Columbia Code: D.C. Official Code § 47-1508(a)(9)
Sunset Date: None
Year Enacted: 2000

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$304	$307	$312	$316

DESCRIPTION: The personal property of a "qualified supermarket" is exempt from personal property taxation for 10 years, subject to several conditions. First, the real property where the personal property is located must continue to be used as a supermarket. Second, if the supermarket leases the real property where it is located, the owner of the property must reduce the rent charged to the supermarket by the amount of any real property tax exemption it receives for being the site of a qualified supermarket. Third, the supermarket must meet its requirements under the "First Source" program, which requires private organizations receiving D.C. government aid to give priority to D.C. residents in filling new jobs.[448]

A "qualified supermarket" is a supermarket located in a census tract where more than half of the households have incomes below 60 percent of the area median, as determined by the U.S. Department of Housing and Urban Development.

PURPOSE: The purpose of the exemption is to encourage the construction and operation of supermarkets in underserved areas of the city.

IMPACT: Individuals and organizations that are constructing and operating supermarkets in the target areas benefit from this provision. By extension, residents of these areas benefit by gaining greater access to a wider range of food in their neighborhood. Presently, six supermarkets are benefiting from the exemption. The exemption violates the principle of horizontal equity because other businesses that locate in the same areas do not receive similar treatment.

[448] Specifically, the beneficiaries of D.C. government aid are expected to hire D.C. residents for at least 51 percent of their new jobs.

Personal Property Tax
Exemptions

225. Non-profit organizations

District of Columbia Code: D.C. Official Code § 47-1508(a)(1)
Sunset Date: None
Year Enacted: 1902

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$4	$4	$4	$4

DESCRIPTION: The personal property of any non-profit organization organized exclusively for religious, scientific, charitable, or educational purposes, including hospitals, is exempt from personal property taxation, provided that (1) that the organization obtains a letter from the Chief Financial Officer stating that it is entitled to the exemption, and (2) any personal property used for activities that generated unrelated business income subject to tax under section 511 of the U.S. Internal Revenue Code of 1986 is not exempt from the personal property tax.

PURPOSE: The exemption supports a general policy of providing tax exemptions to non-profit organizations that provide religious, scientific, charitable, educational, or cultural benefits to the general public.

IMPACT: Non-profit organizations organized exclusively for religious, scientific, charitable, educational, or cultural purposes benefit from this exemption.

Personal Property Tax
Exemptions

226. Motor vehicles and trailers

District of Columbia Code: D.C. Official Code § 47-1508(a)(3)
Sunset Date: None
Year Enacted: 1954

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$2,244	$2,266	$2,307	$2,330

DESCRIPTION: Any motor vehicle or trailer registered in the District of Columbia is exempt from personal property taxation, except that special equipment mounted on a motor vehicle or trailer and not used for the transportation of persons or property is taxed as tangible personal property. The District's personal property tax applies only to business property, so the motor vehicles owned by District residents for their personal use would not be taxed even if this exemption were not in place.

PURPOSE: The reason for the exemption is not known, but many states do not include motor vehicles in their personal property tax.[449] Motor vehicles are exempt from the personal property tax in Maryland, but personal and commercial motor vehicles in Virginia are subject to the personal property tax.[450]

IMPACT: Owners of commercial motor vehicles and trailers benefit from this exemption. As of February 2012, there were 17,419 commercial vehicles registered in the District of Columbia, according to the D.C. Department of Motor Vehicles. The exemption violates the principle of economic neutrality because firms' personal property tax liability could vary depending on the type of property owned, even if they have the same level of income or assets.

[449] John Bowman, "Personal Property Taxation" in District of Columbia Tax Revision Commission, *Taxing Simply, Taxing Fairly: Full Report* (1998), Chapter H, p. 204.

[450] In Virginia, each city or county sets its own personal property tax and the state subsidizes some personal property tax relief for non-commercial motor vehicles.

Personal Property Tax
Exemptions

227. Public utility or toll telecommunications providers

District of Columbia Code: D.C. Official Code § 47-1508(a)(3A)
Sunset Date: None
Year Enacted: 2001

(Dollars in thousands)	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Revenue Loss	$9	$9	$9	$9

DESCRIPTION: The personal property of any company that is subject to a public utility tax or the toll telecommunications tax is exempt from the personal property tax.

PURPOSE: The purpose of the exemption is to prevent double taxation.

IMPACT: Companies that are subject to the public utility tax or the toll telecommunications tax benefit from this exemption.

Personal Property Tax
Exemptions

228. Wireless telecommunication companies

District of Columbia Code: D.C. Official Code § 47-1508(7)
Sunset Date: None
Year Enacted: 1998

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	minimal	minimal	minimal	minimal

Note: "Minimal" means that the forgone revenue is estimated as less than $50,000 per year, although precise data are lacking.

DESCRIPTION: The personal property of a wireless telecommunication company is exempt from personal property taxation, except for office equipment or office furniture. This exemption includes resellers that purchase telecommunications services from another telecommunications service provider, and then resell or integrate the purchased services into a mobile telecommunication service. The exemption is valid whether the wireless company uses the property to provide a service which is subject to the toll telecommunications tax.

PURPOSE: The purpose of the exemption is to provide wireless telecommunication companies with a personal property tax exemption equivalent to the exemption provided to other telecommunication companies.

IMPACT: Wireless telecommunication companies benefit from the exemption. Nevertheless, the number of firms that claim the exemption and the associated reduction in tax are unknown because the wireless telecommunication companies do not have to file a form with the Office of Tax and Revenue to be eligible.

The estimated revenue loss is "minimal" (less than $50,000 per year) because U.S. Census Bureau data show that wireless telecommunication companies are typically small (approximately 30 employees).[451] D.C. law exempts the first $225,000 of taxable personal property from the tax, and most wireless telecommunication companies might therefore be exempt, due to their size, even without this blanket exemption. The majority of D.C. businesses have no personal property tax liability as a result of the $225,000 exemption.

The exemption violates the principle of horizontal equity because other firms with similar types or stocks of personal property do not receive similar treatment.

[451] Specifically, the 2007 Economic Census reported that there were 31 wireless telecommunication companies in the District of Columbia with 925 employees, an average of 29.8 employees per firm.

Personal Property Tax
Exemptions

229. Works of art lent to the National Gallery of Art by non-residents

District of Columbia Code: D.C. Official Code § 47-1508(a)(2)
Sunset Date: None
Year Enacted: 1950

(Dollars in thousands)	FY 2012	FY 2013	FY 2014	FY 2015
Revenue Loss	$0	$0	$0	$0

DESCRIPTION: Works of art owned by an individual who is not a resident or a citizen of the United States are exempt from the personal property tax, provided that the works of art are lent to the National Gallery of Art solely for exhibition without charge to the general public.

PURPOSE: The U.S. Congress established the exemption in order to facilitate a National Gallery of Art exhibition of the paintings of oil magnate Calouste Gulbenkian, who was considered to have one of the best private art collections in the world. Mr. Gulbenkian was unwilling to lend his paintings to the National Gallery without assurances that they would be exempt from federal and District of Columbia taxation, particularly if he were to pass away while the paintings were on loan.[452] Therefore, on September 1, 1950, Congress enacted P.L. 81-749, which established that works of art owned by a non-resident of the United States who is not a citizen of the U.S., and lent for exhibition by the National Gallery of Art, are exempt from the federal estate tax and from the D.C. inheritance and personal property taxes.[453]

The exhibit, "European Paintings from the Gulbenkian Collection," was open to the public from October 8, 1950, to May 31, 1951. Included were works by Ghirlandaio, Rubens, Van Dyck, Rembrandt, Fragonard, Gainsborough, Corot, Manet, Monet, Degas, and Renoir.

IMPACT: It is not known if the exemption has been used in any cases besides the Gulbenkian exhibit.

[452] U.S. House of Representatives, Committee on Ways and Means, 81st Congress, Report to Accompany House J. Res. 497 (Report No. 2724), July 24, 1950, pp. 1-2.

[453] The relevant provision of the inheritance tax was repealed when the inheritance tax law was rewritten in 1987.