

U.S. Budget, Taxes, and Employee Benefits An Update

The federal government supports the provision of employee benefits through preferential treatment in the tax code. The Congressional Budget Act of 1974 (P. L. 93-344) requires that a list of tax expenditures (federal government tax revenue losses due to preferential provisions) be included in the budget. Following is a listing of the employee benefits tax expenditures.

| | 1999 | 2001 | 2004 | 2000-2004 |
|-------------------------------------------------------------------------------------|------------------|------------------|------------------|--------------------|
| | (\$ millions) | | | |
| Transportation | | | | |
| Exclusion of reimbursed employee parking expenses | \$ 1,595 | \$ 1,690 | \$ 1,885 | \$ 8,770 |
| Exclusion for employer-provided transit passes | 80 | 105 | 170 | 655 |
| Education, Training, Employment, and Social Services | | | | |
| Exclusion of employer educational assistance | 215 | 15 | 0 | 225 |
| Exclusion of employer-provided child care | 1,385 | 1,510 | 1,715 | 7,890 |
| Exclusion of employee meals and lodging (other than military) | 650 | 710 | 810 | 3,715 |
| Health | | | | |
| Exclusion of employer contributions for medical insurance premiums and medical care | 72,535 | 83,095 | 101,520 | 446,075 |
| Medical savings accounts | 20 | 25 | 15 | 105 |
| Exclusion of Social Security Benefits | | | | |
| Old-Age and Survivors Insurance benefits for retired workers | 17,210 | 19,045 | 22,460 | 100,990 |
| Benefits for dependents and survivors | 3,785 | 4,065 | 4,575 | 21,190 |
| Disability insurance benefits | 2,420 | 2,820 | 3,625 | 15,445 |
| Income Security | | | | |
| Exclusion of railroad retirement system benefits | 420 | 425 | 440 | 2,155 |
| Exclusion of workers' compensation benefits | 5,330 | 5,940 | 6,755 | 30,855 |
| Exclusion of special benefits for disabled coal miners | 80 | 70 | 60 | 340 |
| Exclusion of military disability pensions | 125 | 135 | 145 | 690 |
| Net Exclusion of Pension Contributions and Earnings | | | | |
| Employer plans | 82,195 | 86,670 | 94,455 | 446,440 |
| Individual retirement accounts | 10,770 | 11,440 | 11,270 | 56,915 |
| Keogh plans | 4,025 | 4,495 | 5,285 | 23,795 |
| Special ESOP ¹ rules (other than investment credit) | 950 | 1,020 | 1,140 | 5,300 |
| Exclusion of Other Employee Benefits | | | | |
| Group term life insurance premiums | 2,075 | 2,170 | 2,335 | 11,115 |
| Accident and disability insurance premiums | 185 | 205 | 235 | 1,075 |
| Income of trust to finance supplementary unemployment benefits | 5 | 5 | 5 | 25 |
| Veterans' Benefits and Services | | | | |
| Exclusion of veterans' disability compensation | 2,940 | 3,210 | 3,650 | 16,775 |
| Exclusion of veterans' pensions | 65 | 75 | 85 | 395 |
| Total | \$209,060 | \$228,940 | \$262,635 | \$1,200,830 |

- The tax code includes three types of tax treatments for employee benefits: tax exemption, tax deferred, and other preferential treatment.
- *Tax-exempt* treatment means that the benefit is not considered taxable income to the individual. Examples of employee benefits that receive this type of tax treatment are health insurance, educational assistance, legal assistance, child-care, discounts, flexible spending accounts, parking, cafeteria facility, and meals. The largest of these is health insurance. According to the president's 2000 budget, the tax exemption for employment-based health insurance will cost the federal government \$446.1 billion from 2000 through 2004. This is tax revenue the federal government will not recoup at some later point.
- *Tax-deferred* treatment means that the employee is not immediately taxed on the contributions the employer and/or the employee makes to the plan or the earnings on plan assets as they accumulate, but will be taxed when the benefit is paid out. Examples of employee benefits that receive this type of tax treatment are Keogh plans, defined benefit pension plans, defined contribution plans such as 401(k)s, and individual retirement accounts (IRAs). According to the president's 2000 budget, the tax exemption for employment-based retirement income plans will cost the federal government \$446.4 billion from 2000 through 2004. When IRAs and Keogh plans are added, the tax revenue loss estimate is \$527.2 billion for 2000–2004.
- The revenue loss estimate for pension contributions and earnings is different from that for health insurance, and is actually a deferral of taxation. At some point in the future, when the individual starts drawing a benefit from the plan, the federal government will receive some tax revenue from the benefit payment.
- The tax treatment of other benefits is subject to limits and/or provisions. For example, employer payments for life insurance premiums are tax-exempt to the employee up to a benefit of \$50,000; any premium amount for a benefit greater than \$50,000 is taxable income to the employee. The benefit payout from a life insurance policy is not taxable income to the beneficiary. According to the president's 2000 budget, the tax exemption for employment-based life insurance will cost the federal government \$11.1 billion from 2000 through 2004.

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Source: *EBRI Databook on Employee Benefits*, fourth edition, 1997, and Executive Office of the President, Office of Management and Budget, *Analytical Perspectives, Budget of the United States Government, Fiscal Year 1999*, January 1999.

¹ Employee stock ownership plan.