FACTS from EBRI

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Tax Expenditures and Employee Benefits: Estimates from the FY 2011 Budget

• The federal government supports the provision of employee benefits through preferential tax treatment in the Internal Revenue Code. The Congressional Budget Act of 1974 (P.L. 93-344) requires that a list of "tax expenditures" (federal tax revenue forgone due to preferential provisions) be included in the budget. The concept of "tax expenditures" has always been controversial, particularly as it relates to programs that are "tax deferred" (such as retirement plans, under which tax revenue ultimately will be collected) rather than "tax exempt" (meaning programs in which no revenue will ever be collected) (*EBRI Issue Brief*, no. 134, February 1993, provides a full review of this controversy).

• For the next fiscal year (2011), all employee benefits-related tax expenditures ($380.83 billion) will account for 36.0 percent of the $1,056.71 billion tax expenditures in the budget. Tax-favored employment-based health insurance benefits will account for the largest tax expenditure presented in the budget ($176.964 billion, or 16.7 percent of the total amount and 51.3 percent of all employee benefits-related tax expenditures), followed by employment-based retirement plans ($111.691 billion, or 10.6 percent of the total amount and 32.4 percent of all employee benefit related tax expenditures) (see figure).

• The following is a listing of the employee benefits tax expenditures, as published in President Obama's Fiscal Year 2011 budget, prepared by the White House Office of Management and Budget, using a methodology that is flawed but mandated by Congress.

There are three types of tax treatments for employee benefits: tax exemption, tax deferral, and other preferential treatment:

- *Tax-exempt* treatment in the tax code 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 2011 budget, the tax exemption for employment-based health insurance is projected to cost the federal government $1,053.794 billion from 2011 through 2015. 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 (1) the contributions the employer and/or the employee makes to the plan, and/or (2) on the earnings on plan assets as they accumulate, but will typically be taxed on portions not previously taxed when the benefit is paid. 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) plans), and individual

Employee Benefit Tax Expenditures

White House Fiscal Year 2011 Budget Estimates

	($ millions) Tax Expenditures, by Fiscal Year			
	2010[a]	2011[a]	2015[a]	2011–2015[a]
Transportation				
Exclusion of reimbursed employee parking expenses	$3,020	$3,100	$3,590	$16,660
Exclusion for employer-provided transit passes	560	530	670	3,000
Education, Training, Employment and Social Services				
Exclusion of employer-provided educational assistance	690	30	0	30
State pre-paid tuition plans	1,390	1,580	2,050	9,190
Exclusion of employer-provided child care	1,210	1,370	1,630	7,440
Employer-provided child care credit	20	10	0	10
Exclusion of employee meals and lodging (other than military)	1,060	1,110	1,370	6,180
Health				
Exclusion of employer contributions for medical insurance premiums and medical care	159,868	176,964	248,600	1,053,794
Self-employed medical insurance premiums	5,250	5,740	7,780	33,370
Medical Savings Accounts/Health Savings Accounts	2,030	2,130	2,590	11,780
Distributions from Retirement Plans for Premiums for Health and Long-term Care Insurance	300	330	490	2,020
Exclusion of Social Security Benefits				
Old-Age and Survivors Insurance benefits for retired workers	21,410	20,240	26,810	115,150
Benefits for dependents and survivors	3,850	3,140	3,330	15,990
Disability Insurance benefits	6,950	7,160	8,580	39,020
Income security				
Exclusion of railroad retirement system benefits	320	300	250	1,340
Exclusion of workers' compensation benefits	5,870	5,940	6,370	30,820
Exclusion of special benefits for disabled coal miners	40	40	40	200
Exclusion of military disability pensions	110	110	120	560
Net Exclusion of Pension Contributions				
Employment-based plans	94,909	111,691	130,163	608,320
Employer plans	41,360	44,630	53,980	247,480
401(k)	53,549	67,061	76,183	360,840
Individual Retirement Accounts	12,780	14,080	16,500	78,940
Keoghs plans	13,890	15,120	22,610	95,760
Special ESOP rules (other than investment credit)	1,700	1,800	2,200	10,000
Low and Moderate Income Savers	1,180	1,170	960	5,320
Exclusion of Other Employee Benefits				
Premiums on group term life insurance	2,110	2,160	2,390	11,500
Premiums on accident and disability insurance	330	340	360	1,770
Income of trust to finance supplementary unemployment benefits	40	50	60	260
Veterans' Benefits and Services				
Exclusion of veterans' disability compensation and death benefits	4,130	4,370	5,510	24,620
Exclusion of veterans' pensions	200	220	270	1,270
Total	345,217	380,825	495,293	2,184,314
Addendum				
Deductibility of mortgage interest on owner-occupied homes	92,180	104,540	149,560	637,560

Source: Executive Office of the President, Office of Management and Budget, *Analytical Perspectives, Budget of the Untied States Government,*

Fiscal Year 2011, www.whitehouse.gov/omb/budget/Analytical_Perspectives/

[a] Projected.

retirement accounts (IRAs). According to the president's 2011 budget, the tax exemption for employer plans is projected to cost the federal government $608.32 billion from 2011 through 2015. When IRAs and Keoghs are added, the tax revenue loss estimate is $783.02 billion for 2011–2015.

The revenue loss estimate for pension contributions and earnings is different from health insurance. The tax revenue loss estimate is actually a *deferral* of taxation, rather than an exemption. 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.

• *Other benefits* are subject to limits and/or provisions with respect to tax treatment. For example, employer payments to the premium of life insurance 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 2011 budget, the tax exemption for employment-based life insurance is projected to cost the federal government $11.5 billion from 2011 through 2015.

For data for all years 1975–2009, go to *EBRI's Databook on Employee Benefits, Chapter 5*. There is also a spreadsheet with inflation-adjusted dollars.

For more information, contact Ken McDonnell, (202) 775-6300, or see EBRI's Web site at www.ebri.org.
Source: Executive Office of the President, Office of Management and Budget, *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2011*,
www.gpoaccess.gov/usbudget/fy10/pdf/spec.pdf