

Estimating the Impact of Federal Legislation on State Tax Systems

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Presentation Overview

- A Bit on Federal Legislative Process
- CBO: Roles and Responsibilities
 - The Congressional Budget and Impoundment Control Act
 - The Unfunded Mandates Reform Act (UMRA) –why CBO gets involved in State and Local tax issues
- How we estimate costs
- Legislative Examples



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Federal Legislative Process

□ Authorizing Committees

- Legislation that “authorizes” (creates or continues) programs
 - Mandatory spending, authorization of appropriations
- CBO provides estimates of marked up bills (approved, and ordered reported to the floor)
 - “Markup”: meeting of a committee to debate and consider amendments to a measure. (Different than a hearing)



□ Appropriations Committees

- Responsible for the 13 spending bills each year
- Unless requested, CBO’s State and Local Cost Estimates Unit does not provide estimates for these bills

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CBO: Roles and Responsibilities

- Created by the Congressional Budget and Impoundment Control Act of 1974
- Statutory mission: assist the Congress in preparing and analyzing budget. Help Congress formulate its budget plan
- Provide Congress with cost estimates to help it stay within its budget plan
- Assess the impact of federal mandates (Since 1996)



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What CBO Does NOT Do

- ❑ Make policy recommendations (strictly nonpartisan; no judgments about a legislative proposal's "merits")
- ❑ Write legislation (we evaluate different proposals, options)
- ❑ Implement programs, regulations, enforce budget rules (that's all Executive Branch)
- ❑ Audit spending or receipts (that's GAO)
- ❑ Analyze the effects of federal tax code changes on state and local governments (that's the Joint Committee on Taxation – JCT)



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Background On UMRA

- ❑ The Unfunded Mandates Reform Act (UMRA) of 1995 (Public Law 104-4): Part of the 'Contract with America'
 - Increases information about mandates & their costs
 - Increases accountability by creating a point of order
- ❑ Defines mandates as enforceable duties
 - Not grant conditions, except in limited cases for large entitlements
 - Not costs of participating in voluntary federal programs
- ❑ Requires a mandates statement for all authorizing bills ordered reported from full committees



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More Background on UMRA

- Requires CBO to estimate the direct costs of mandates – net of direct savings – resulting from complying with the mandates. Then compare to annual thresholds
 - \$50 million for intergovernmental mandates, adjusted annually for inflation
 - \$100 million for private sector mandates, adjusted annually for inflation
- Points of order for bills, amendments, motions, and conference reports with costs that do not have a CBO estimate or exceed the intergovernmental threshold
- Intended to increase information to the Congress and to provide a parliamentary hurdle if Congress wants to use it



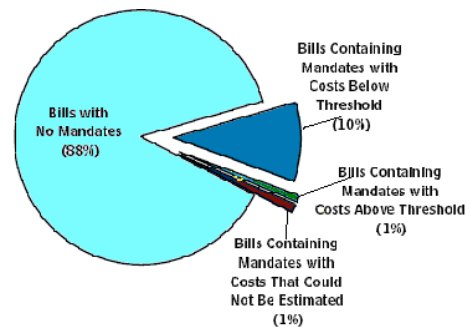
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UMRA: 10 years old

- Most bills contain no intergovernmental mandates
- Few of the bills that CBO reviews would affect state taxes (less than 1% of the total reviewed) Often these bills:
 - Preempt state authority to tax (in some way)
 - Restrict the ability of state or local governments to raise revenues

Bills Reviewed By CBO from 1996-2005

(Total Bills Reviewed: 5,769)



Source: Congressional Budget Office.



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Estimating the Cost of Legislation

- UMRA focuses on the direct costs of legislation
- Direct Costs include:
 - Expenditures necessary to comply with mandate
 - Revenues lost when complying with mandate
 - Amounts state, local, and tribal governments are prohibited from raising in revenue
 - Incremental costs and first order costs only
- CBO also identifies “other impacts” of legislation if they would be significant
- Not all costs result from mandates
- Step 1: Review Legislative Language
 - Get input from a variety of stakeholders/sources
- Step 2: Determine affected state and local governments
 - Changes to current law and potential mandates under UMRA
- Step 3: Quantify Budgetary Effects for each provision
 - Incremental spending or forgone revenue with respect to current law/practice using a variety of data sources
- Step 4: Make a Threshold Determination
 - Add total costs of mandates and subtract direct savings 9



Legislative Example: Internet Tax Freedom Act (ITFA)

- The ITFA was a mandate as defined in UMRA. (Originally passed in 1998, extended twice)
 - Temporarily prohibited states from assessing taxes on Internet access services – preemption of state law
 - Certain states – already taxing access – were “grandfathered”
 - Extension passed in 2004 expanded the definition of “Internet Access”
- Estimating Questions
- Which states are currently taxing “Access” & other telecom services?
 - Are companies paying these taxes?
 - How will an expanded definition of “Internet Access” affect what states can tax?
 - How will changes in the telecom industry affect taxable activities under current law? Under the bill?



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Legislative Example: Internet Tax Freedom Act (ITFA)

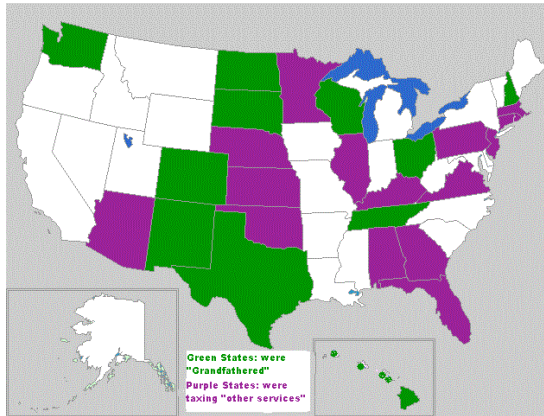
CBO's ESTIMATE (2003)
Grandfathered States: (2007)
\$80-\$120 m/yr
Taxes on DSL: (2005)
\$40-\$80 m/yr
Subtotal: \$120-\$200m
per year

PLUS: Impacts from the
New Definition of
"Access" Up to \$3 billion
per year in telecom
taxes, by 2009

**TOTAL: no more than
\$3 BILLION
annually, by 2009**



CBO's Estimate of States Taxing
Internet Access (2003)



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Legislative Example: Video Franchise/Telecom Bill (H.R. 5252)

SUMMARY

- When there is certain competition in the market for cable television, the bill would allow for national, rather than local, franchises
- Local governments:
 - Would be prohibited from charging certain fees to providers of video service who have a national franchise
 - Could benefit from being able to charge franchise fees to new subscribers
- If there is a national franchise, the bill would preempt state and local laws that address:
 - Consumer protection
 - Cable franchises
 - The use of municipal rights of way



ESTIMATING ISSUES

- ☞ What are locals and states currently collecting? For what?
- ☞ How would this law change that?
- ☞ How fast will there be competition in the cable market under current law? Under this bill?
- ☞ Should we offset losses to local governments with increased revenues from competition?
- ☞ Are there any other impacts?

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Legislative Examples: Video Franchise/Telecom Bill

CBO's Cost Estimate (H.R. 5252)

-  **Direct Costs by 2011:
\$150-\$450 million**
-  **New Revenues: \$50 to
\$100 million**
-  **Total Net Costs: \$100-
\$350 million by 2011**
-  **Other Impacts: In-kind
losses**



Senate Bill S. 2682

- Hearings held May 18 and 25
- Revised draft to be issued June 5
- Markup scheduled for June 20
- Current draft has similar provisions to H.R. 5252 although could have a more significant revenue impact

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Conclusion

- CBO:
 - Provides estimates for bills marked up by full authorizing committees and other reports on request
 - Estimates the direct costs of legislation and identifies other impacts
 - Does not estimate the effect of federal tax code changes on state and local revenues
- UMRA requires CBO to provide estimates for impacts on state and local governments
- Legislation that affects state and local taxes and fees include the ITFA and bills changing the rules for Video Franchises
- Legislation on the horizon:
 - "Business Activity Tax Simplification Act" (H.R. 1956; S. 2721)
 - "Telecommuter Tax Fairness Act" (H.R. 2558; S. 1097)
 - "Economic Development Act of 2005" (H.R. 2471; S. 1066)



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