



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

August 31, 2004

H.R. 1231

A bill to amend the Internal Revenue Code of 1986 to allow Federal civilian and military retirees to pay health insurance premiums on a pretax basis and to allow a deduction for TRICARE supplemental premiums

As reported by the House Committee on Governmental Reform on July 7, 2004

SUMMARY

H.R. 1231 would modify the tax treatment of certain health insurance premiums paid by federal civilian retirees and by active-duty and retired military personnel. It would allow federal civilian and military retirees to pay for health insurance premiums on a pre-tax basis when those premiums are paid through a pension reduction arrangement. It would also allow active-duty and retired military personnel to deduct certain supplemental premiums or enrollment fees for TRICARE, the military's health care program, from their taxable income.

The Joint Committee on Taxation (JCT) estimates that enacting the legislation would reduce federal revenues by \$549 million in 2005, about \$4.4 billion over the 2005-2009 period, and about \$12.1 billion over the 2005-2014 period. The Congressional Budget Office (CBO) estimates that implementing the bill would cost a total of \$2 million in 2005, \$1 million of which would be subject to availability of appropriated funds.

JCT has determined that H.R. 1231 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would not affect the budgets of state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 1231 is shown in the following table and assumes enactment on October 1, 2004. The costs of this bill fall within budget functions 050 (national defense) and 600 (income security).

	By Fiscal Year, in Millions of Dollars									
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014

CHANGES IN REVENUES

Exclusion for FEHB Premiums Paid By Federal Civilian Retirees	-499	-756	-829	-902	-976	-1054	-1265	-1419	-1530	-1650
Exclusion for TRICARE Prime Premiums Paid By Military Retirees	-22	-32	-33	-35	-35	-36	-40	-41	-41	-41
Exclusion for TRICARE Dental Premiums Paid By Military Retirees	-25	-38	-42	-46	-49	-53	-64	-71	-77	-82
Deduction for TRICARE Supplemental Insurance Premiums Paid By Active-Duty and Retired Military Personnel	<u>-3</u>	<u>-23</u>	<u>-25</u>	<u>-27</u>	<u>-29</u>	<u>-31</u>	<u>-33</u>	<u>-40</u>	<u>-42</u>	<u>-45</u>
Estimated Revenues	-549	-849	-929	-1,009	-1,089	-1,174	-1,402	-1,571	-1,690	-1,819

CHANGES IN DIRECT SPENDING

Office of Personnel Management										
Estimated Budget Authority	1	0	0	0	0	0	0	0	0	0
Estimated Outlays	1	0	0	0	0	0	0	0	0	0

CHANGES IN SPENDING SUBJECT TO APPROPRIATION

Department of Defense										
Estimated Authorization Level	1	0	0	0	0	0	0	0	0	0
Estimated Outlays	1	0	0	0	0	0	0	0	0	0

SOURCES: Joint Committee on Taxation and CBO.

NOTES: Details may not add to totals due to rounding.

FEHB = Federal Employees Health Benefits program.

TRICARE refers to the military's health insurance program.

BASIS OF ESTIMATE

H.R. 1231 would modify the tax treatment of certain health insurance premiums paid by federal civilian retirees and by active-duty and retired military personnel. It would allow federal civilian and military retirees to pay for health insurance premiums on a pre-tax basis when those premiums are paid through a pension reduction arrangement. It would also allow active-duty and retired military personnel to deduct certain supplemental premiums or enrollment fees for TRICARE, the military's health care program, from their taxable income.

For purposes of the estimate, JCT and CBO assumed that H.R. 1231 will be enacted on October 1, 2004.

Revenues

JCT has provided an estimate of the revenue effects of H.R. 1231. In total, JCT estimates that enacting the bill would reduce governmental receipts by \$549 million in 2005, about \$4.4 billion between 2005 and 2009, and about \$12.1 billion over the 2005-2014 period.

Most of the reduction in revenues would result from excluding from taxable income the portion of pension income of federal civilian retirees that is withheld to pay the retiree share of premiums for health insurance coverage under the Federal Employees Health Benefits program. JCT estimates that doing so would decrease federal revenues by \$499 million in 2005, about \$4 billion over the 2005-2009 period, and about \$10.9 billion over the 2005-2014 period. The bill also would provide similar income tax exclusions for military retirees for TRICARE Prime and TRICARE Dental premiums. Together, providing those exclusions would decrease governmental receipts by about an additional \$900 million between 2005 and 2014. Lastly, H.R. 1231 would allow active-duty and retired military personnel to deduct TRICARE supplemental premiums from taxable income, which JCT estimates would reduce federal revenues by just under \$300 million over the 2005-2014 period.

Direct Spending

In order to implement the provisions of H.R. 1231, the Office of Personnel Management (OPM) would incur additional administrative costs to notify retirees of the new benefit and change their computer systems to accommodate the new tax treatment of beneficiaries' benefits. Based on information provided by OPM, CBO estimates this would increase the agency's expenses by \$1 million in 2005. While most administrative spending by OPM is subject to appropriation, expenses arising from administering income tax withholdings on retirement benefits are considered direct spending.

Spending Subject to Appropriation

As with OPM, the Department of Defense (DoD) would incur additional administrative costs primarily to notify retirees and active-duty personnel of the new benefit and to reflect the special tax treatment of enrollee contributions toward qualified expenses in their data systems. Based on information from DoD, CBO estimates that such activities would cost DoD about \$1 million in fiscal year 2005, assuming the availability of appropriated funds.

SUMMARY OF EFFECT ON REVENUES AND DIRECT SPENDING

The effects of H.R. 1231 on revenues and direct spending over the 2005-2014 period are shown in the following table.

	By Fiscal Year, in Millions of Dollars									
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Changes in receipts	-549	-849	-929	-1,009	-1,089	-1,174	-1,402	-1,571	-1,690	-1,819
Changes in outlays	1	0	0	0	0	0	0	0	0	0

SOURCES: Joint Committee on Taxation and CBO.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

JCT has determined that H.R. 1231 contains no intergovernmental or private-sector mandates as defined in UMRA and would not affect the budgets of state, local, or tribal governments.

ESTIMATE PREPARED BY:

Federal Revenues: Annabelle Bartsch
Federal Costs: Geoffrey Gerhardt and Sam Papenfuss

ESTIMATE APPROVED BY:

G. Thomas Woodward
Assistant Director for Tax Analysis

Paul R. Cullinan
Chief, Human Resources Cost Estimating Unit
Budget Analysis Division