OVERVIEW OF THE FEDERAL TAX SYSTEM AS IN EFFECT FOR 2007

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JOINT COMMITTEE ON TAXATION

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CONTENTS

INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a summary of the present-law Federal tax system as in effect for 2007.

The current Federal tax system has four main elements: (1) an income tax on individuals and corporations (which consists of both a "regular" income tax and an alternative minimum tax); (2) payroll taxes on wages (and corresponding taxes on self-employment income); (3) estate, gift, and generation skipping taxes, and (4) excise taxes on selected goods and services. This document provides a broad overview of each of these elements.[2]

A number of aspects of the Federal tax laws are subject to change over time. For example, some dollar amounts and income thresholds are indexed for inflation. The standard deduction, tax rate brackets, and the annual gift tax exclusion are examples of amounts that are indexed for inflation. In general, the Internal Revenue Service adjusts these numbers annually and publishes the inflation adjusted amounts in effect for a tax year prior to the beginning of that year. Where applicable, this document generally includes dollar amounts in effect for 2007 and notes whether dollar amounts are indexed for inflation.

In addition, a number of the provisions in the Federal tax laws have been enacted on a temporary basis or have parameters that vary by statute from year to year. For example, the recently enacted Tax Relief and Health Care Act of 2006 extended a number of expired or soon to expire provisions on a temporary basis. In addition, the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 were initially generally to expire at the end of 2010; some provisions of that Act have subsequently been modified or made permanent. For simplicity, this document describes the Federal tax laws in effect in 2007 and generally does not include references to provisions as they may be in effect for future years or to termination dates for expiring provisions. A list of expiring tax provisions may be found in Joint Committee on Taxation, *List of Expiring Federal Tax Provisions 2006-2020*, (JCX-1-07), January 11, 2007.

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[1] This document may be cited as follows: Joint Committee on Taxation, *Overview of the Federal Tax System as in Effect for 2007* (JCX-2-07), January 12, 2007.

[2] If certain requirements are met, certain entities or organizations are exempt from Federal income tax. A description of such organizations is beyond the scope of this document.

I. SUMMARY OF PRESENT-LAW FEDERAL TAX SYSTEM

A. Individual Income Tax

In general

A United States citizen or resident alien generally is subject to the U.S. individual income tax on his or her worldwide taxable income.[3] Taxable income equals the taxpayer's total gross income less certain exclusions, exemptions, and deductions. Graduated tax rates are then applied to a taxpayer's taxable income to determine his or her individual income tax liability. A taxpayer may face additional liability if the alternative minimum tax applies. A taxpayer may reduce his or her income tax liability by any applicable tax credits.

Adjusted gross income

Under the Internal Revenue Code of 1986 (the "Code"), gross income means "income from whatever source derived" except for certain items specifically exempt or excluded by statute. Sources of income include compensation for services, interest, dividends, capital gains, rents, royalties, alimony and separate maintenance payments, annuities, income from life insurance and endowment contracts (other than certain death benefits), pensions, gross profits from a trade or business, income in respect of a decedent, and income from S corporations, partnerships,[4] trusts or estates.[5] Statutory exclusions from gross income include death benefits payable under a life insurance contract, interest on certain State and local bonds, employer-provided health insurance, employer-provided pension contributions, and certain other employer-provided benefits.

An individual's adjusted gross income ("AGI") is determined by subtracting certain "above-the-line" deductions from gross income. These deductions include trade or business expenses, capital losses, contributions to a tax-qualified retirement plan by a self-employed individual, contributions to individual retirement arrangements ("IRAs"), certain moving expenses, and alimony payments.

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[3] Foreign tax credits generally are available against U.S. income tax imposed on foreign source income to the extent of foreign income taxes paid on that income. A nonresident alien generally is subject to the U.S. individual income tax only on income with a sufficient nexus to the United States.

[4] In general, partnerships and S corporations are treated as pass-through entities for Federal income tax purposes. Thus, no Federal income tax is imposed at the entity level. Rather, income of such entities is passed through and taxed to the owners at the individual level.

[5] In general, estates and most trusts pay tax on income at the entity level, unless the income is distributed or required to be distributed under governing law or under the terms of the governing instrument. Such entities determine their tax liability using a special tax rate schedule and are subject to the alternative minimum tax. Certain trusts, however, do not pay Federal income tax at the trust level. For example, certain trusts that distribute all income currently to beneficiaries are treated as "pass-through" or conduit entities (similar to a partnership). Other trusts are treated as being owned by grantors in whole or in part for tax purposes; in such cases, the grantors are taxed on the income of the trust.

Taxable income

In order to determine taxable income, an individual reduces AGI by any personal exemption deductions and either the applicable standard deduction or his or her itemized deductions. Personal exemptions generally are allowed for the taxpayer, his or her spouse, and any dependents. For 2007, the amount deductible for each personal exemption is $3,400. This amount is indexed annually for inflation. The deduction for personal exemptions is reduced or eliminated for taxpayers with incomes over certain thresholds, which are indexed annually for inflation. The applicable thresholds for 2007 are $156,400 for single individuals, $234,600 for married individuals filing a joint return and surviving spouses, $195,500 for heads of households, and $117,300 for married individuals filing separate returns.

A taxpayer also may reduce AGI by the amount of the applicable standard deduction. The basic standard deduction varies depending upon a taxpayer's filing status. For 2007, the amount of the standard deduction is $5,350 for single individuals and married individuals filing separate returns, $7,850 for heads of households, and $10,700 for married individuals filing a joint return and surviving spouses. An additional standard deduction is allowed with respect to any individual who is elderly or blind.[6] The amounts of the basic standard deduction and the additional standard deductions are indexed annually for inflation.

In lieu of taking the applicable standard deductions, an individual may elect to itemize deductions. The deductions that may be itemized include State and local income taxes (or, in lieu of income**,** sales), real property and certain personal property taxes, home mortgage interest, charitable contributions, certain investment interest, medical expenses (in excess of 7.5 percent of AGI), casualty and theft losses (in excess of 10 percent of AGI and in excess of $100 per loss), and certain miscellaneous expenses (in excess of two percent of AGI). The total amount of itemized deductions allowed is reduced for taxpayers with incomes over a certain threshold amount, which is indexed annually for inflation. The threshold amount for 2007 is $156,400 ($78,200 for married individuals filing separate returns).

Tax liability

In general

A taxpayer's net income tax liability is the greater of (1) regular individual income tax liability reduced by credits allowed against the regular tax, or (2) tentative minimum tax reduced by credits allowed against the minimum tax. The amount of income subject to tax is determined differently under the regular tax and the alternative minimum tax, and separate rates schedules apply. Lower rates apply for long-term capital gains; those rates apply for both the regular tax and the alternative minimum tax

[6] For 2007, the additional amount is $1,050 for married taxpayers (for each spouse meeting the applicable criterion) and surviving spouses. The additional amount for single individuals and heads of households is $1,300. If an individual is both blind and aged, the individual is entitled to two additional standard deductions, for a total additional amount (for 2007) of $2,100 or $2,600, as applicable.

Regular tax liability

To determine regular tax liability, a taxpayer generally must apply the tax rate schedules (or the tax tables) to his or her regular taxable income. The rate schedules are broken into several ranges of income, known as income brackets, and the marginal tax rate increases as a taxpayer's income increases. Separate rate schedules apply based on an individual's filing status. For 2007, the regular individual income tax rate schedules are as follows:

Table 1.–Federal Individual Income Tax Rates for 2007

If taxable income is:	Then income tax equals:
Single Individuals	
Not over $7,825	10% of the taxable income
Over $7,825 but not over $31,850	$782.50 plus 15% of the excess over $7,825
Over $31,850 but not over $77,100	$4,386.25 plus 25% of the excess over $31,850
Over $77,100 but not over $160,850	$15,689.75 plus 28% of the excess over $77,100
Over $160,850 but not over $349,700	$39,148.75 plus 33% of the excess over $160,850
Over $349,700	$101,469.25 plus 35% of the excess over $349,700
Heads of Households	
Not over $11,200	10% of the taxable income
Over $11,200 but not over $42,650	$1,120 plus 15% of the excess over $11,200
Over $42,650 but not over $110,100	$5,837.50 plus 25% of the excess over $42,650
Over $110,100 but not over $178,350	$22,700 plus 28% of the excess over $110,100
Over $178,350 but not over $349,700	$41,810 plus 33% of the excess over $178,350
Over $349,700	$98,355.50 plus 35% of the excess over $349,700
Married Individuals Filing Joint Returns and Surviving Spouses	
Not over $15,650	10% of the taxable income
Over $15,650 but not over $63,700	$1,565 plus 15% of the excess over $15,650
Over $63,700 but not over $128,500	$8,772.50 plus 25% of the excess over $63,700
Over $128,500 but not over $195,850	$24,972.50 plus 28% of the excess over $128,500
Over $195,850 but not over $349,700	$43,830.50 plus 33% of the excess over $195,850
Over $349,700	$94,601 plus 35% of the excess over $349,700

Married Individuals Filing Separate Returns

Not over $7,825	10% of the taxable income
Over $7,825 but not over $31,850	$782.50 plus 15% of the excess over $7,825
Over $31,850 but not over $64,250	$4,386.25 plus 25% of the excess over $31,850
Over $64,250 but not over $97,925	$12,486.25 plus 28% of the excess over $64,250
Over $97,925 but not over $174,850	$21,915.25 plus 33% of the excess over $97,925
Over $174,850	$47,300.50 plus 35% of the excess over $174,850

An individual's marginal tax rate may be reduced by the allowance of a deduction equal to a percentage of income from certain domestic manufacturing activities.[7]

<u>Alternative minimum tax liability</u>

An alternative minimum tax is imposed on an individual, estate, or trust in an amount by which the tentative minimum tax exceeds the regular income tax for the taxable year. The tentative minimum tax is the sum of (1) 26 percent of so much of the taxable excess as does not exceed $175,000 ($87,500 in the case of a married individual filing a separate return) and (2) 28 percent of the remaining taxable excess. The taxable excess is so much of the alternative minimum taxable income ("AMTI") as exceeds the exemption amount. The maximum tax rates on net capital gain and dividends used in computing the regular tax are used in computing the tentative minimum tax. AMTI is the taxpayer's taxable income increased by the taxpayer's tax preferences and adjusted by determining the tax treatment of certain items in a manner that negates the deferral of income resulting from the regular tax treatment of those items.

The exemption amounts are: (1) $45,000 ($62,550 in taxable years beginning in 2006) in the case of married individuals filing a joint return and surviving spouses; (2) $33,750 ($42,500 in taxable years beginning in 2006) in the case of other unmarried individuals; (3) $22,500 ($31,275 in taxable years beginning in 2006) in the case of married individuals filing separate returns; and (4) $22,500 in the case of an estate or trust. The exemption amounts are phased out by an amount equal to 25 percent of the amount by which the individual's AMTI exceeds (1) $150,000 in the case of married individuals filing a joint return and surviving spouses, (2) $112,500 in the case of other unmarried individuals, and (3) $75,000 in the case of married individuals filing separate returns or an estate or a trust. These amounts are not indexed for inflation.

[7] This deduction is described in more detail below in the summary of the tax rules applicable to corporations.

Among the preferences and adjustments applicable to the individual alternative minimum tax are accelerated depreciation on certain property used in a trade or business, circulation expenditures, research and experimental expenditures, certain expenses and allowances related to oil and gas and mining exploration and development, certain tax-exempt interest income, and a portion of the amount of gain excluded with respect to the sale or disposition of certain small business stock. In addition, personal exemptions, the standard deduction, and certain itemized deductions, such as State and local taxes and miscellaneous deductions items, are not allowed to reduce alternative minimum taxable income.

Special capital gains and dividends rates

In general, gain or loss reflected in the value of an asset is not recognized for income tax purposes until a taxpayer disposes of the asset. On the sale or exchange of a capital asset, any gain generally is included in income. Any net capital gain of an individual is taxed at maximum rates lower than the rates applicable to ordinary income. Net capital gain is the excess of the net long-term capital gain for the taxable year over the net short-term capital loss for the year. Gain or loss is treated as long-term if the asset is held for more than one year.

Capital losses generally are deductible in full against capital gains. In addition, individual taxpayers may deduct capital losses against up to $3,000 of ordinary income in each year. Any remaining unused capital losses may be carried forward indefinitely to another taxable year.

A separate rate structure applies to capital gains and dividends. Under present law, for 2007, the maximum rate of tax on the adjusted net capital gain of an individual is 15 percent. In addition, any adjusted net capital gain otherwise taxed at a 10- or 15-percent rate is taxed at a five-percent rate. These rates apply for purposes of both the regular tax and the alternative minimum tax. Dividends are generally taxed at the same rate as capital gains.

Credits against tax

The individual may reduce his or her tax liability by any available tax credits. Tax credits are allowed for certain business expenditures, certain foreign income taxes paid or accrued, certain education expenditures, certain child care expenditures, and with respect to children under 17 and for certain elderly or disabled individuals. In addition, a refundable earned income tax credit ("EITC") is available to low-income workers who satisfy certain requirements. The amount of the EITC varies depending upon the taxpayer's earned income and whether the taxpayer has one, more than one, or no qualifying children. In 2007, the maximum EITC is $4,716 for taxpayers with more than one qualifying child, $2,853 for taxpayers with one qualifying child, and $428 for taxpayers with no qualifying children. Credits allowed against the regular tax are not uniformly allowed against the alternative minimum tax.

B. Corporate Income Tax

Taxable income

Corporations organized under the laws of any of the 50 States (and the District of Columbia) generally are subject to the U.S. corporate income tax on their worldwide taxable income.[8]

The taxable income of a corporation generally is comprised of gross income less allowable deductions. Gross income generally is income derived from any source, including gross profit from the sale of goods and services to customers, rents, royalties, interest (other than interest from certain indebtedness issued by State and local governments), dividends, gains from the sale of business and investment assets, and other income.

Allowable deductions include ordinary and necessary business expenditures, such as salaries, wages, contributions to profit-sharing and pension plans and other employee benefit programs, repairs, bad debts, taxes (other than Federal income taxes), contributions to charitable organizations (subject to an income limitation), advertising, interest expense, certain losses, selling expenses, and other expenses. Expenditures that produce benefits in future taxable years to a taxpayer's business or income-producing activities (such as the purchase of plant and equipment) generally are capitalized and recovered over time through depreciation, amortization or depletion allowances. A net operating loss incurred in one taxable year may be carried back two years or carried forward 20 years and allowed as a deduction in another taxable year. Deductions are also allowed for certain amounts despite the lack of a direct expenditure by the taxpayer. For example, a deduction is allowed for all or a portion of the amount of dividends received by a corporation from another corporation (provided certain ownership requirements are satisfied). Moreover, a deduction is allowed for a portion of the amount of income attributable to certain manufacturing activities.

The Code also specifies certain expenditures that may not be deducted, such as dividends paid to shareholders, expenses associated with earning tax-exempt income,[9] certain entertainment expenditures, certain executive compensation in excess of $1,000,000 per year, a portion of the interest on certain high-yield debt obligations that resemble equity, and fines, penalties, bribes, kickbacks and illegal payments.

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[8] Foreign tax credits generally are available against U.S. income tax imposed on foreign source income to the extent of foreign income taxes paid on that income. A foreign corporation generally is subject to the U.S. corporate income tax only on income with a sufficient nexus to the United States.

A qualified small business corporation may elect, under subchapter S of the Code, not to be subject to the corporate income tax. If an S corporation election is made, the income of the corporation will flow through to the shareholders and be taxable directly to the shareholders.

[9] For example, the carrying costs of tax-exempt State and local obligations and the premiums on certain life insurance policies are not deductible.

Tax liability

A corporation's regular income tax liability generally is determined by applying the following tax rate schedule to its taxable income.

Table 2.–Federal Corporate Income Tax Rates

If taxable income is:	Then the income tax rate is:
$0-$50,000	15 percent of taxable income
$50,001-$75,000	25 percent of taxable income
$75,001-$10,000,000	34 percent of taxable income
Over $10,000,000	35 percent of taxable income

The first two graduated rates described above are phased out for corporations with taxable income between $100,000 and $335,000. As a result, a corporation with taxable income between $335,000 and $10,000,000 effectively is subject to a flat tax rate of 34 percent. Also, the application of the 34-percent rate is gradually phased out for corporations with taxable income between $15,000,000 and $18,333,333, such that a corporation with taxable income of $18,333,333 or more effectively is subject to a flat rate of 35 percent.

In contrast to the treatment of capital gains in the individual income tax, no separate rate structure exists for corporate capital gains. Thus, the maximum rate of tax on the net capital gains of a corporation is 35 percent. A corporation may not deduct the amount of capital losses in excess of capital gains for any taxable year. Disallowed capital losses may be carried back three years or carried forward five years.

Corporations are taxed at lower rates on income from certain domestic production activities. This rate reduction is effected by the allowance of a deduction equal to a percentage of qualifying domestic production activities income. For taxable years beginning in 2007, 2008, and 2009, the deduction is equal to three percent of the income from manufacturing, construction, and certain other activities specified in the Code. Thereafter, the deduction is increased to nine percent.[10]

Like individuals, corporations may reduce their tax liability by any applicable tax credits. Tax credits applicable to businesses include credits for producing fuels from nonconventional

[10] At the fully phased-in nine percent deduction, a corporation is taxed at a rate of 35 percent on only 91 percent of qualifying income, resulting in an effective tax rate of 0.91 * 35, or 31.85 percent. A similar reduction applies to the graduated rates applicable to individuals with qualifying domestic production activities income.

sources, investment tax credits (applicable to investment in certain renewable energy property and the rehabilitation of certain real property), the alcohol fuels credit (applicable to production of certain alcohol fuels), the research credit, the low-income housing credit (applicable to investment in certain low-income housing projects), the enhanced oil recovery credit (applicable to the recovery of certain difficult-to-extract oil reserves), the empowerment zone employment credit (applicable to wages paid to certain residents of or employees in empowerment zones), and the disabled access credit (applicable to expenditures by certain small businesses to make the businesses accessible to disabled individuals). The credits generally are determined based on a percentage of the cost associated with the underlying activity and generally are subject to certain limitations.

Affiliated group

Domestic corporations that are affiliated through 80 percent or more corporate ownership may elect to file a consolidated return in lieu of filing separate returns. Corporations filing a consolidated return generally are treated as a single corporation; thus, the losses (and credits) of one corporation can offset the income (and thus reduce the otherwise applicable tax) of other affiliated corporations.

Minimum tax

A corporation is subject to an alternative minimum tax which is payable, in addition to all other tax liabilities, to the extent that it exceeds the corporation's regular income tax liability. The tax is imposed at a flat rate of 20 percent on alternative minimum taxable income in excess of a $40,000 exemption amount.[11] Credits that are allowed to offset a corporation's regular tax liability generally are not allowed to offset its minimum tax liability. If a corporation pays the alternative minimum tax, the amount of the tax paid is allowed as a credit against the regular tax in future years.

Alternative minimum taxable income is the corporation's taxable income increased by the corporation's tax preferences and adjusted by determining the tax treatment of certain items in a manner that negates the deferral of income resulting from the regular tax treatment of those items. Among the preferences and adjustments applicable to the corporate alternative minimum tax are accelerated depreciation on certain property, certain expenses and allowances related to oil and gas and mining exploration and development, certain amortization expenses related to pollution control facilities, and certain tax-exempt interest income. In addition, corporate alternative minimum taxable income is increased by 75 percent of the amount by which the corporation's "adjusted current earnings" exceeds its alternative minimum taxable income (determined without regard to this adjustment). Adjusted current earnings generally are determined with reference to the rules that apply in determining a corporation's earnings and profits.

[11] The exemption amount is phased out for corporations with income above certain thresholds, and is completely phased out for corporations with alternative minimum taxable income of $310,000 or more.

Treatment of corporate distributions

The taxation of a corporation generally is separate and distinct from the taxation of its shareholders. A distribution by a corporation to one of its shareholders generally is taxable as a dividend to the shareholder to the extent of the corporation's current or accumulated earnings and profits.[12] Thus, the amount of a corporate dividend generally is taxed twice: once when the income is earned by the corporation and again when the dividend is distributed to the shareholder.[13] Conversely, amounts paid as interest to the debtholders of a corporation generally are subject to only one level of tax (at the recipient level) since the corporation generally is allowed a deduction for the amount of interest expense paid or accrued.

Amounts received by a shareholder in complete liquidation of a corporation generally are treated as full payment in exchange for the shareholder's stock. A liquidating corporation recognizes gain or loss on the distributed property as if such property were sold to the distributee for its fair market value. However, if a corporation liquidates a subsidiary corporation of which it has 80 percent or more control, no gain or loss generally is recognized by either the parent corporation or the subsidiary corporation.

Accumulated earnings and personal holding company taxes

Taxes at a rate of 15 percent (the top rate generally applicable to dividend income of individuals) may be imposed upon the accumulated earnings or personal holding company income of a corporation. The accumulated earnings tax may be imposed if a corporation retains earnings in excess of reasonable business needs. The personal holding company tax may be imposed upon the excessive passive income of a closely held corporation. The accumulated earnings tax and the personal holding company tax are designed to ensure that both a corporate tax and a shareholder tax are effectively imposed on corporate earnings.

[12] A distribution in excess of the earnings and profits of a corporation generally is a tax-free return of capital to the shareholder to the extent of the shareholder's adjusted basis (generally, cost) in the stock of the corporation; such distribution is a capital gain if in excess of basis. A distribution of property other than cash generally is treated as a taxable sale of such property by the corporation and is taken into account by the shareholder at the property's fair market value. A distribution of stock of the corporation generally is not a taxable event to either the corporation or the shareholder.

[13] This double taxation is mitigated by a reduced maximum tax rate of 15 percent generally applicable to dividend income of individuals.

C. Estate and Gift and Generation-Skipping Transfer Taxes

The United States imposes a gift tax on any transfer of property by gift made by a U.S. citizen or resident, whether made directly or indirectly and whether made in trust or otherwise. Nonresident aliens are subject to the gift tax with respect to transfers of tangible real or personal property where the property is located in the United States at the time of the gift. The gift tax is imposed on the donor and is based on the fair market value of the property transferred. Deductions are allowed for certain gifts to spouses and to charities. Annual gifts of $12,000 (for 2007) or less per donor per donee generally are not subject to tax.

An estate tax also is imposed on the taxable estate of any person who was a citizen or resident of the United States at the time of death, and on certain property belonging to a nonresident of the United States that is located in the United States at the time of death. The estate tax is imposed on the estate of the decedent and generally is based on the fair market value of the property passing at death.[14] The taxable estate generally equals the worldwide gross estate less certain allowable deductions, including a marital deduction for certain bequests to the surviving spouse of the decedent and a deduction for certain bequests to charities.

The gift and estate taxes began as separate taxes but were partially unified in 1976 so that a single graduated rate schedule applied to an individual's cumulative taxable gifts and bequests. Changes in 2001 decoupled the estate and gift taxes in certain ways, but a single rate schedule still applies to gifts and bequests. Under this rate schedule, for 2007 the unified estate and gift tax rates begin at 18 percent on the first $10,000 in cumulative taxable transfers and reach 45 percent on cumulative taxable transfers over $2 million. A unified credit of $345,800 is available with respect to taxable transfers by gift, and a unified credit of $780,800 is available with respect to taxable transfers at death. These credits effectively exempt a total of $1 million in cumulative taxable gifts from gift tax and $2 million in cumulative taxable transfers (by gift and at death) from the estate tax. The unified credit also has the effect of rendering all rates below 41 percent inapplicable to any taxable transfer by gift or bequest.[15]

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[14] In addition to interests in property owned by the decedent at the time of death, the Federal estate tax also is imposed on (1) life insurance that was either payable to the decedent's estate or in which the decedent had an incident of ownership at death, (2) property over which the decedent had a general power of appointment at death, (3) annuities purchased by the decedent or his employer that were payable to the decedent before death, (4) property held as joint tenants, (5) property transferred by the decedent before death in which the decedent retained a life estate or over which the decedent had the power to designate who will possess or enjoy the property, (6) property revocably transferred by the decedent before death, and (7) certain transfers taking effect at the death of the decedent.

[15] The unified credit against estate tax is scheduled to increase in 2009 (so that the effective estate tax exemption in that year will be $3.5 million). As a result of these changes, in 2007 through 2009 the estate tax exclusion amount equals or exceeds the level at which the highest tax rate begins. Effectively, the highest rate is the only estate tax rate. The unified credit against gift tax will remain at $345,800 through 2009 (and the effective exemption will therefore remain at $1 million). The estate tax is scheduled to be repealed in 2010 but reinstated (under the rules in effect before the 2001 changes) in 2011.

A separate transfer tax is imposed on generation-skipping transfers in addition to any estate or gift tax that is normally imposed on such transfers. This tax is generally imposed on transfers, either directly or through a trust or similar arrangement, to a beneficiary in more than one generation below that of the transferor. For 2007, the generation-skipping transfer tax is imposed at a flat rate of 45 percent on generation-skipping transfers in excess of $2 million.

D. Employment Taxes

Social security benefits and certain Medicare benefits are financed primarily by payroll taxes on covered wages. The Federal Insurance Contributions Act ("FICA") imposes tax on employers based on the amount of wages paid to an employee during the year. The tax imposed is composed of two parts: (1) the old age, survivors, and disability insurance ("OASDI") tax equal to 6.2 percent of covered wages up to the taxable wage base ($97,500 in 2007); and (2) the Medicare hospital insurance ("HI") tax amount equal to 1.45 percent of covered wages.[16] In addition to the tax on employers, each employee is subject to FICA taxes equal to the amount of tax imposed on the employer. The employee level tax generally must be withheld and remitted to the Federal government by the employer.

As a parallel to FICA taxes, the Self-Employment Contributions Act ("SECA") imposes taxes on the net income from self employment of self employed individuals. The rate of the OASDI portion of SECA taxes is equal to the combined employee and employer OASDI FICA tax rates and applies to self employment income up to the FICA taxable wage base. Similarly, the rate of the HI portion is the same as the combined employer and employee HI rates and there is no cap on the amount of self employment income to which the rate applies.[17]

In addition to FICA taxes, employers are subject to a Federal unemployment insurance payroll tax equal to 6.2 percent of the total wages of each employee (up to $7,000) on covered employment. Employers are eligible for a Federal credit equal to 5.4 percent for State unemployment taxes. The current 0.8 percent effective tax rate is composed of a permanent tax rate of 0.6 percent and a temporary surtax rate of 0.2. The temporary surtax is scheduled to expire on December 31, 2007. Federal unemployment insurance payroll taxes are used to fund programs maintained by the States for the benefit of unemployed workers.

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[16] Since 1994, the HI payroll tax has not been subject to a wage cap.

[17] For purposes of computing net earnings from self employment, taxpayers are permitted a deduction equal to the product of the taxpayer's earnings (determined without regard to this deduction) and one-half of the sum of the rates for OASDI (12.4 percent) and HI (2.9 percent), i.e., 7.65 percent of net earnings. This deduction reflects the fact that the FICA rates apply to an employee's wages, which do not include FICA taxes paid by the employer, whereas a self-employed individual's net earnings are economically equivalent to an employee's wages plus the employer share of FICA taxes.

E. Major Excise Taxes

The Federal tax system imposes excise taxes on selected goods and services. Generally, excise taxes are taxes imposed on a per unit or ad valorem (i.e., percentage of price) basis on the production, importation, or sale of a specific good or service. Among the goods and services subject to U.S. excise taxes are motor fuels, alcoholic beverages, tobacco products, firearms, air and ship transportation, certain environmentally hazardous activities and products, coal, telephone communications, certain wagers, and vehicles lacking in fuel efficiency.[18] The largest excise taxes in terms of revenue (for fiscal year 2005) are those for gasoline motor fuels ($23.7 billion), diesel motor fuel ($9.4 billion), and domestic cigarettes ($7.2 billion).

Revenues from certain Federal excise taxes are dedicated to trust funds (e.g., the Highway Trust Fund) for designated expenditure programs and revenues from other excise taxes (e.g., alcoholic beverages) go to the General Fund for general purpose expenditures.

[18] See, Joint Committee on Taxation, *Study of the Overall State of the Federal Tax System and Recommendations for Simplification, Pursuant to Section 8022(3)(B)of the Internal Revenue Code of 1986*, (JCS-3-01), April 2001, pp. 478-516 for a description the various Federal excise taxes.

II. HISTORICAL RECEIPTS DATA

Table 1.−Aggregate Federal Receipts by Source, 1950-2005
[millions of dollars]

Year	Individual Income Tax	Corporate Income Tax	Employment[1] Taxes	Excise Taxes	Estate and Gift Taxes	Other[2] Receipts
1950	15,755	10,449	4,338	7,550	698	653
1951	21,616	14,101	5,674	8,648	708	870
1952	27,934	21,226	6,445	8,852	818	892
1953	29,816	21,238	6,820	9,877	881	976
1954	29,542	21,101	7,208	9,945	934	971
1955	28,747	17,861	7,862	9,131	924	926
1956	32,188	20,880	9,320	9,929	1,161	1,109
1957	35,620	21,167	9,997	10,534	1,365	1,307
1958	34,724	20,074	11,239	10,638	1,393	1,568
1959	36,719	17,309	11,722	10,578	1,333	1,588
1960	40,715	21,494	14,683	11,676	1,606	2,317
1961	41,338	20,954	16,439	11,860	1,896	1,900
1962	45,571	20,523	17,046	12,534	2,016	1,985
1963	47,588	21,579	19,804	13,194	2,167	2,228
1964	48,697	23,493	21,963	13,731	2,394	2,337
1965	48,792	25,461	22,242	14,570	2,716	3,037
1966	55,446	30,073	25,546	13,062	3,066	3,642
1967	61,526	33,971	32,619	13,719	2,978	4,009
1968	68,726	28,665	33,923	14,079	3,051	4,529
1969	87,249	36,678	39,015	15,222	3,491	5,227
1970	90,412	32,829	44,362	15,705	3,644	5,855
1971	86,230	26,785	47,325	16,614	3,735	6,450
1972	94,737	32,166	52,574	15,477	5,436	6,919
1973	103,246	36,153	63,115	16,260	4,917	7,109
1974	118,952	38,650	75,071	16,844	5,035	8,702
1975	122,386	40,621	84,534	16,551	4,611	10,387
1976	131,603	41,409	90,769	16,963	5,216	12,101
1977	157,626	54,892	106,485	17,548	7,327	11,681
1978	180,988	59,952	120,967	18,376	5,285	13,993
1979	217,841	65,677	138,939	18,745	5,411	16,690
1980	244,069	64,600	157,803	24,329	6,389	19,922
1981	285,917	61,137	182,720	40,839	6,787	21,872
1982	297,744	49,207	201,498	36,311	7,991	25,015
1983	288,938	37,022	208,994	35,300	6,053	24,256
1984	298,415	56,893	239,376	37,361	6,010	28,430
1985	334,531	61,331	265,163	35,992	6,422	30,650
1986	348,959	63,143	283,901	32,919	6,958	33,334
1987	392,557	83,926	303,318	32,457	7,493	34,602
1988	401,181	94,508	334,335	35,227	7,594	36,457
1989	445,690	103,291	359,416	34,386	8,745	39,662
1990	466,884	93,507	380,047	35,345	11,500	44,686
1991	467,827	98,086	396,016	42,402	11,138	39,572
1992	475,964	100,270	413,689	45,569	11,143	44,644
1993	509,680	117,520	428,300	48,057	12,577	38,267
1994	543,055	140,385	461,475	55,225	15,225	43,262
1995	590,244	157,004	484,473	57,484	14,763	47,862
1996	656,417	171,824	509,414	54,014	17,189	44,204
1997	737,466	182,293	539,371	56,924	19,845	43,393
1998	828,586	188,677	571,831	57,673	24,076	50,955
1999	879,480	184,680	611,833	70,414	27,782	53,265
2000	1,004,462	207,289	652,852	68,865	29,010	62,740
2001	994,339	151,075	693,967	66,232	28,400	57,181
2002	858,345	148,044	700,760	66,989	26,507	52,528
2003	793,699	131,778	712,978	67,524	21,959	54,404
2004	808,959	189,371	733,407	69,855	24,831	53,856
2005	927,222	278,282	794,125	73,094	24,764	56,372

[1] Employment taxes comprise old-age and survivors insurance, disability insurance, hospital insurance, railroad retirement, railroad social security equivalent account, employment insurance, employee share of Federal employees retirement, and certain non-Federal employees retirement.

[2] Other receipts are primarily composed of [1] customs duties and fees, and [2] deposits of earnings by the Federal Reserve system.

Source: Office of Management and Budget, *Historical Tables, Budget of the U.S. Government, Fiscal Year 2007*

Figure 1.−Aggregate Receipts by Source, 2005