

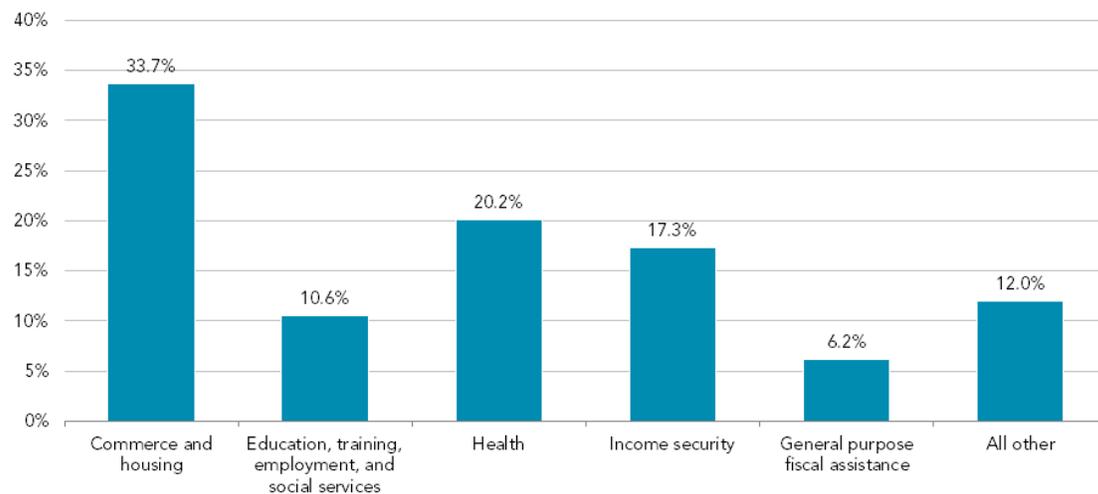
# What is the tax expenditure budget?

It displays the estimated revenue losses from special exclusions, exemptions, deductions, credits, deferrals, and preferential tax rates in federal income tax law.

Every year, the Office of Management and Budget (OMB) and the Congressional Joint Committee on Taxation (JCT) publish lists of tax expenditures. These lists, sometimes called the Tax Expenditure Budgets, enumerate the estimated revenue losses attributable to preferences in the tax code the agencies describe as exceptions to “normal” or “reference” provisions of the income tax law (figure 1).

FIGURE 1

## Tax Expenditure Budget 2016



Source: Office of Management and Budget, Fiscal Year 2016, Analytical Perspectives, Table 14.1.

Notes: The three largest expenditure categories in “Other” are: international affairs 5.5 percent, social security 2.9 percent, and national defense 1.0 percent.

Tax expenditures reduce the income tax liabilities of individuals and businesses that undertake activities Congress specifically encourages. For example, the deduction for charitable contributions reduces tax liability for people who donate to qualifying charitable organizations. Tax expenditures can also reduce tax liability for individuals Congress wishes to assist. For example, a portion of Social Security benefits received by retired or disabled people is exempt from federal income tax.

The Congressional Budget Act of 1974 requires that the budget include estimates for tax expenditures, but only for provisions that affect the federal income taxes of individuals and corporations. The government could, but does not, provide lists of tax expenditures for payroll taxes, excise taxes, and other taxes, although OMB does estimate (in footnotes) the effects on payroll tax receipts of income tax expenditures.

Both the Office of Tax Analysis (OTA) in the Treasury and the JCT estimate tax expenditures annually. The items included in each, along with their estimated values, are generally similar but do not always match. OMB publishes OTA’s estimates in its Analytical Perspectives volume that accompanies each year’s Budget of the U.S. Government.

The budget generally treats tax expenditures as revenue losses instead of as spending. An exemption is made for the portion of refundable tax credits that exceeds individuals' positive income tax liabilities. Here, the net refunds are counted as spending. OMB's tables show only the revenue losses of tax expenditures, while JCT's tables include both the revenue loss and outlay effects of refundable credits. Both OMB and JCT display the outlay effects in footnotes.

OMB's tax expenditures for fiscal 2016, including outlay effects, added up to more than \$1.4 trillion. The combined revenue loss for all provisions does not necessarily equal the sum of the losses for each provision because of how the provisions interact. For example, eliminating one exemption from taxable income would push taxpayers into higher rate brackets, thereby increasing revenue loss from remaining exemptions. Toder, Burman, and Geissler (2008) and Baneman and Toder (2012) thus estimate that the actual combined revenue loss from all individual tax expenditures is up to 10 percent larger than the amount computed by summing individual tax expenditures—though for one subcategory, itemized deductions, the total revenue loss is less than the sum of losses from the separate deductions.

Some tax expenditures effectively function like direct expenditures even though they appear as tax breaks, because programs with similar effects could be structured as outlays (Burman and Phaup, 2011). An example is the tax credit for renewable energy investment, which could be structured as grants from the Department of Energy. Other expenditures have no direct spending analogy, but can instead be viewed as departures from an income tax with a comprehensive base. Marron and Toder (2013) estimate that provisions that could be viewed as spending substitutes have recently amounted to over 4 percent of GDP.

Like mandatory programs (or entitlements) on the spending side of the budget, most tax expenditures do not go through a direct appropriations process each year and are available with no budget ceiling to all who qualify. Expenditure costs change with the growth of the economy, changes in the quantities and prices of subsidized activities, and—for some provisions—changes in marginal tax rates applied to individual and corporate income. For example, the cost of the mortgage interest deduction varies with the volume of home mortgage debt outstanding, the level of interest rates, and marginal tax rates applied to the taxable income of borrowers.

## Data Sources

Office of Management and Budget. *Budget of the U.S. Government, FY 2016*, [Analytical Perspectives](#), Table 14.1.

## Works Cited and Further Reading

Baneman, Daniel, and Eric Toder. 2012. "Distributional Effects of Individual Income Tax Expenditures: An Update." Washington, DC: Urban-Brookings Tax Policy Center.

Burman, Leonard E., and Marvin Phaup. 2011. "Tax Expenditures, the Size and Efficiency of Government, and Implications for Budget Reform." Working Paper 17268. Cambridge, MA: National Bureau of Economic Research.

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Toder, Eric J., Leonard E. Burman, and Christopher Geissler. 2008. "How Big Are Individual Income Tax Expenditures and Who Benefits from Them?" Discussion Paper 31. Washington, DC: Urban-Brookings Tax Policy Center.