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EVALUATING TAX EXPENDITURES: INTRODUCING OVERSIGHT INTO SPENDING THROUGH THE TAX CODE

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ABSTRACT

Increased demand for better use of evidence in policymaking has sparked bipartisan support for better evaluation of federal spending programs. Tax expenditures, spending-like subsidies embedded in the tax code, cost taxpayers roughly as much as domestic discretionary programs, yet receive little-to-no scrutiny from government evaluators. Many large tax expenditures have existed for decades with limited reform, despite independent research often finding them to be inefficient at achieving their purported goals. After a brief overview of tax expenditures, we review the evaluative tools and offices government has at its disposal and suggest options lawmakers could use to conduct regular evaluation of tax subsidies in pursuit of leaner, more effective government.

This paper was updated on July 26, 2018 to clarify the roles of the Joint Committee on Taxation and the Congressional Research Service in estimating and evaluating tax expenditures.

OVERVIEW

The principle behind evidence-based policy is simple: government programs should be evaluated so that resources can be allocated most effectively within and among programs. Against the backdrop of a $4 trillion federal budget, the implications of evidence-based policy are massive. Improving programmatic outcomes and directing federal dollars to the most effective programs can dramatically improve the well-being of Americans across the country.

To date, the bulk of programmatic evaluations have focused on direct spending, with less attention directed at "tax expenditures." Tax expenditures are considered "spending through the tax code" because they grant special tax preferences to individuals or corporations for particular activities. Economists consider most tax expenditures analogous to spending because the result often can be achieved through a targeted spending provision. For example, a $1,000 tax cut granted a homeowner in the form of deductible mortgage interest could be replicated with a $1,000 expenditure based on mortgage interest paid; the difference between an outlay and a tax expenditure is almost wholly semantic in this case.

There are important differences between tax expenditures and direct spending, but in this study, we focus on the differential evaluation received by each. The legislative and executive branches have some processes to evaluate discretionary spending (spending generally subject to annual appropriations) and, to a lesser extent, mandatory spending (more permanent spending programs). These processes are largely unavailable for tax expenditures. Indeed, although roughly equal in size to total discretionary spending, tax expenditures go largely unnoticed in the context of evidence-based policy.

Despite their prevalence, tax expenditures have never been subject to systematic oversight, let alone evaluations of whether they are achieving their intended goal. Thus, the economic or social impact of these expenditures is largely unknown, except for some academic evaluations that are not systemically applied. Policymakers also have limited information on whether automatic increases over time in many of those expenditures add much to their effectiveness. For instance, policymakers do not know if increasing the relative benefit to owner-occupied housing, which occurs automatically as people buy more expensive housing, increases the rate of homeownership.

Oversight is surprisingly limited, given the massive $1.5 trillion annual tax expenditure budget. There is no annual review of how Congress spends through the tax code, no program staff dedicated to tax expenditures' administration, no inspector general (IG) for tax expenditures, and no rigorous government evaluation of the effectiveness of most tax breaks. Although the Government Performance Results Act (GPRA) of 1993, as modified by the GPRA Modernization Act of 2010, aims to provide a performance planning and reporting framework, its implementation has been limited regarding tax expenditures. GAO (2017) recently found little progress in the executive branch toward systematically evaluating tax expenditures. In response, OMB (2018) provided a mere two pages describing a broad framework for evaluating tax expenditures in its *Analytical*

Perspectives accompanying the fiscal year 2019 budget, identifying few concrete steps toward meaningful evaluation. At this point we are unaware of any major initiative to provide the resources necessary to provide a serious and broad effort at evaluation.

Fortunately, the demand for congressional evaluation of public programs has been increasing. Two years ago, the bipartisan Evidence-Based Policymaking Commission Act of 2016 established a commission to study how data can improve government initiatives. Earlier this year, the commission released its final report, with smart recommendations including naming chief evaluation officers at every federal agency charged with evaluating federal programs (CEP 2017). In April 2018, the Ways and Means Committee began investigating ways to restructure the IRS, though little attention has been paid to evaluation issues. The Bipartisan Policy Center recently issued a report on the limited supply of evidence available to Congress and the need to increase it, though the report did not deal explicitly with tax expenditures (Hart, Davis, and Shaw 2018). And earlier this year, Congress established the Joint Select Committee on Budget and Appropriations Process Reform, which provides a unique opportunity for the evidence-based policy community to call on Congress to strengthen its oversight on the tax expenditure budget.

The Tax Cuts and Jobs Act (TCJA) of 2017 also provides an opportunity to evaluate newly created tax expenditures. The legislation created two notable new expenditures in Opportunity Zones (targeted tax relief for investment in economically disadvantaged geographic areas) and a new 20 percent deduction for noncorporate businesses. These new expenditures are expected to cost roughly $7 billion and $203 billion, respectively, over the next five years. The cost of these programs begs evaluation, and policymakers should understand the impact of these reforms before committing to making them a permanent part of the tax system.

This paper initiates a conversation on the systematic evaluation of the tax expenditure budget. After reviewing the growth and nature of tax expenditures and describing the relative dearth of evaluations, we propose a series of reforms that would promote more thorough review of tax expenditures. In particular, we suggest more funding of evaluations by policy offices within the executive branch, increased oversight by nonpartisan agencies such as the Congressional Budget Office (CBO) and Joint Committee on Taxation (JCT), and independent evaluations by external evaluators. We also discuss organizational reforms, such as periodic review by Congress of each tax expenditure and restructuring the IRS to pay more attention to each tax expenditure. Ultimately, the goal of these reforms would be to promote a more effective government that achieves its desired social and economic goals in the most efficient way possible.

THE SIZE AND NATURE OF TAX EXPENDITURES

Tax expenditures give special treatment to certain economic activities by taxing them more lightly. Defining and measuring tax expenditures raises conceptual questions for scholars, but a tax expenditure typically subsidizes a favored activity by exempting it from taxable income, taxing it at a lower rate, providing it with a credit or an enhanced deduction, or deferring the related tax liability to some future time.[1] Deductions required to correctly measure income, such as write-offs for normal business expenses, are not considered tax expenditures.

Issues Raised by Tax Expenditures

Tax expenditures create differential outcomes among otherwise similar taxpayers, often simply because their financial lives are configured differently. For example, the tax code imposes higher taxes on a household that buys health insurance on its own than on one that receives it as an employment benefit.

Tax expenditures reduce revenues otherwise available to government or, for a given revenue level, require higher marginal tax rates on nonpreferred activities. This can distort economic behavior by encouraging people and businesses to shelter income in ways they would not otherwise find advantageous. For example, subsidies for retirement saving can induce workers to direct higher amounts to tax-deferred retirement accounts instead of taxable investment accounts; the new tax expenditure allowing a 20 percent deduction for pass-through businesses may incent wage earners to convert to self-employed contractors so they may claim the extra tax deduction. Moreover, subsidies created by tax expenditures can inflate prices, as with housing or health insurance, especially where supply or competition for a subsidized product is restricted by, say, land scarcity or patents (Burman and Gruber 2005).

But tax expenditures are not intrinsically good or bad. Like direct spending programs or regulations, they are one of many tools government can use toward its policy goals. If government wants to encourage a certain behavior, like work or saving, tax subsidies sometimes can be more cost-effective than administering a new government direct spending program, especially if the targets for the subsidy are already filing taxes. During the Great Recession, for example, the Making Work Pay tax credit modestly stimulated the economy in a quick, streamlined fashion by increasing working taxpayers' incomes through the existing tax filing and withholding process (CBO 2015). And tax expenditures can correct for economic distortions if they encourage more socially valuable behavior. For example, if charitable giving is determined to create a positive benefit for communities, the provision of deductions for charitable gifts can raise giving toward optimal levels. The appropriateness and effectiveness of tax expenditures thus depend on their purpose and design.

Many, if not most, tax subsidies were not initially crafted through a careful process with well-defined goals. Special tax treatment of retirement plans and the exclusion of employer-provided health insurance, for example, both arose as administrative decisions about the tax base back when only very high–income households paid income taxes and spending on retirement and health care was much lower than today.[2] Coinciding mid-20th-century expansions of the federal income tax and employer-provided benefits made these subsidies more visible, giving rise to political constituencies that defended them as vital pillars of middle-class economic life—even as they disproportionately benefited higher-income taxpayers and could have been designed better to help more households at the same or lower cost.

The Size of Tax Expenditures

Absent new legislation, many tax expenditures not only are permanent parts of the tax code, but they also permanently grow in cost. Unlike discretionary programs, no new laws are required to increase their value. The tax exclusion for employer-sponsored health insurance plans, for example, grows automatically with the price of health insurance, which grows with health costs that have for many years increased much faster than overall inflation.[3]

The complications of permanent autopilot can be seen in the mortgage interest deduction, which is part of a generous set of tax subsidies for homeownership. This deduction, often justified as a means of encouraging homeownership, has been part of the US income tax code since its inception in 1913. But the deduction was never based on evidence of its meritorious benefits for society; it was a byproduct of allowing interest to be deducted in the effort to measure net income. As deductions for other types of interest, such as credit card interest, were disallowed over time, the mortgage interest deduction persisted. Over the past century, the mortgage interest deduction has cost taxpayers trillions (in today's dollars) without a systematic review of whether this spending achieved its desired effect.

In 2017, taxpayers spent about $66 billion on the deduction, although the Tax Cuts and Jobs Act reduced at least temporarily the number of people receiving a home mortgage interest deduction—largely from an increase in the standard deduction and the corresponding drop in taxpayers itemizing their deductions. But, here again, the redesign was not based on evidence of its impact on housing policy or homeownership. Rather, by largely maintaining the traditional design of the mortgage interest deduction mainly for higher-income itemizers, the new law ended up excluding those low- and middle-income households that need the most help entering the market.[4]

Based on the most recent estimates published by the Office of Management and Budget (OMB), tax expenditures totaled nearly $1.5 trillion in fiscal year 2017 (about 7.7 percent of GDP), roughly what government collected in total individual income taxes that year.[5] About $1.2 trillion is attributed to individual income tax expenditures, and another $228 billion is attributed to corporate tax expenditures. A small number of tax expenditures related to health insurance, retirement saving, and housing make up the bulk of the tax expenditures' cost (table 1).

By contrast, annual discretionary spending totals around $1.2 trillion, with the largest proportions falling into the category of "public goods," such as military, justice, intelligence, and national parks. Mandatory spending, around $2.5 trillion, tends to dominate transfers to individuals through such programs as Medicare, Medicaid, and Social Security. Indeed, many tax expenditures dwarf the direct government spending for a similar goal. For example, before the Tax Cuts and Jobs Act of 2017, the tax expenditure associated with the mortgage interest deduction was valued at more than all the programs in the US Department of Housing and Urban Development budget.

TABLE 1

Ten Largest Tax Expenditures in 2017

Rank	Description	Millions of dollars
1	Exclusion of employer contributions for medical insurance premiums and medical care	214,280
2	Special treatment of retirement plans (defined contribution, defined benefit, individual, and self-employed)	191,311
3	Exclusion of net imputed rental income	121,350
4	Deferral of income from controlled foreign corporations (normal tax method)	107,200
5	Special treatment of capital gains	103,150
6	Deductibility of nonbusiness state and local taxes other than on owner-occupied homes	70,420
7	Mortgage interest deduction	65,600
8	Earned income tax credit (includes refundable portion)	63,830
9	Deductibility of charitable contributions	58,360
10	Child credit (includes refundable portion)	54,320

Source: Authors' tabulations from US Office of Management and Budget, Analytical Perspectives, Budget of the United States Government, Fiscal Year 2019 (Washington, DC: US Government Printing Office, 2018).
Note: OMB's FY 2019 tax expenditure estimates do not include the effects of the Tax Cuts and Jobs Act of 2017, but the effects of that law on FY 2017 tax expenditures are small. OMB's estimation methodology and assumptions differ from JCT's, resulting in different values for tax expenditures.

Over the past two decades, total tax expenditures ranged from 6 percent to just under 8 percent of GDP, depending on changes in tax policy and the economy. The tax cuts of the early 2000s, mainly by lowering the tax rates at which deductions would be taken, were the first action to slow tax expenditure growth since the Tax Reform Act of 1986, which significantly reduced tax expenditures after its enactment (Marples 2015). Because most tax expenditures are permanent or periodically renewed with little oversight, their growth in cost in the absence of legislation closely resembles that of mandatory spending. By contrast, domestic discretionary spending, with its more rigorous annual review and general lack of automatic growth, has declined relative to GDP and even grew slower than inflation in some years after the Great Recession.

Aside from the refundable portions of certain tax credits, tax expenditures are accounted for as a reduction in revenues instead of an increase in government spending. This hides the true size of government, whether measured by spending or revenues as a share of GDP.[6] Marron and Toder (2013) refined the measure of total tax expenditures by subtracting tax expenditures they found to be more driven by choices about the tax system's overall architecture (e.g., how to treat economic depreciation of business equipment). They found that the clear "spending substitutes" that remain still increase the federal government's size by about 4 percent of GDP.

The Tax Cuts and Jobs Act of 2017 (Pub. L. No. 115-97) temporarily eliminated some tax expenditures, removed the incentive to itemize for many taxpayers (most notably by roughly doubling the standard deduction), and lowered tax rates. These provisions may marginally decrease total individual tax expenditures in the short term, but growth is still built into the expenditures that remain.[7] Also, the TCJA created or expanded other tax expenditures, particularly a special deduction for so-called "pass-through" businesses such as partnerships and sole proprietorships. The long-term effects of the TCJA will depend on whether Congress allows major individual income tax provisions of the law to expire as scheduled after 2025. Long-term, future automatic growth will occur off of 2018 levels regardless of whether those provisions expire or not.

CURRENT EVALUATIONS OF GOVERNMENT SPENDING

Government spending, including tax expenditures, receives different oversight depending on the nature of the program. Certain programs are subject to multiple layers of evaluation, first by the offices administering them, then through potential audits by the Government Accountability Office (GAO) and review by agency inspectors general. Other programs, especially those administered through the tax code, are subject to much less, sometimes virtually zero, oversight and can continue indefinitely without a single serious review. This section summarizes the various oversight frameworks designed to ensure government spending is achieving its goals and identifies those areas where deficiencies exist.

Primary Evaluation of Discretionary and Mandatory Spending

Discretionary spending is automatically evaluated through an annual appropriations process. A full review of that process is beyond the scope of this paper, but several important aspects are worth noting.[8] The appropriations process typically begins in the first week in February when the administration submits its budget request for the following fiscal year. This budget request is the cumulative result of months of planning and review among the agencies and reflects the priorities of the President. This preliminary review gives agencies the opportunity to request more funding for programs deemed more effective at achieving goals, and it allows OMB to suggest which programs deserve less priority. As part of their review, agencies submit written justification for each budget request.[9]

Once the administration submits its budget request, Congress begins its appropriations process for discretionary spending.[10] This is designed to begin with the passage of the annual budget resolution, but in recent years, Congress has frequently failed to agree on a resolution and has instead taken up various appropriations bills to avert program shutdowns. Though budget resolutions are supposed to have important ramifications for overall spending and revenues, they have effectively no impact on oversight of individual programs.

Appropriations subcommittees then begin the process in earnest. These committees are organized to ensure staff and legislator expertise over administrative programs, with subcommittees organized in such areas as energy and water development, homeland security, interior, and environment. Appropriators hold extensive hearings that, coupled with information from the budget justifications and other sources, provide information on the efficacy of various programs. Appropriations bills then face a series of votes, starting with a subcommittee, then (if they pass) moving to the full committee and eventually the full congressional body. Unlike budget-related bills passed through the reconciliation process, appropriations bills voted on by the full Senate effectively require 60 votes for passage.

Mandatory spending typically receives an intermediate level of oversight—somewhat less than appropriations but substantially more than tax expenditures. The process for mandatory spending is idiosyncratic and depends on the characteristics of the program.[11] Much of mandatory spending is automatic or "mandatory," in that outlays will occur each year in the absence of congressional action. However, several mandatory programs—such as SNAP, flood insurance, and student loans—require periodic authorization. The vast majority of dollars in mandatory spending programs are automatically spent according to a predetermined formula or process. Thus, a primary difference between discretionary and mandatory oversight is how frequently Congress and OMB consider the merits of the spending programs as a natural part of the budget process.

Though permanent mandatory spending programs clearly have less oversight than programs subject to annual or periodic review, they too have offices that examine each program separately. For example, Medicare, Medicaid, and the Children's Health Insurance Program are administered through the Centers for Medicare & Medicaid Services, which is largely charged with administration but has some oversight responsibilities that inform policy as well. For example, the agency has an office of innovation, which identifies promising payment and service delivery models. Similarly, Social Security is administered by the Social Security Administration, which undertakes various activities—including funding research projects conducted internally and by academics—to determine whether its programs are working as intended and whether it can make the delivery of benefits more efficient. One example is the Social Security Administration's Promoting Opportunity Demonstration, a program that tests the impact of reduced disability benefits and stronger work incentives on labor market outcomes.

We do not want to exaggerate the prevalence of agency-based evaluation. After all, there is broad demand for these agencies also to expand the availability of evidence to inform policymaking, especially through cost-benefit analysis, randomized controlled trials, and integration of more evidence into congressional decisionmaking. Our goal here is to extend that demand to tax expenditures, the least-examined part of the federal budget.

More Layers of Oversight for Discretionary and Mandatory Spending

Additional program review sometimes comes from Congressional offices or actors within the administrative agencies that are not charged with their direct administration but with other oversight responsibilities. One such entity is the Government Accountability Office, which has seen increased demand for its audits over time. As a congressional agency, it is independent from the executive branch but has jurisdiction to perform performance evaluations. The bulk of GAO oversight is driven by requests from Congress.

In addition to GAO, OMB is charged with increasing efficiency, reducing waste and fraud, and overseeing programmatic expenditures. OMB is also responsible for monitoring the performance of various government agencies; relating agency requests, spending, and taxes to the overall budget; and managing the procurement process.

Inspectors general at federal agencies also have significant oversight responsibilities. They are charged with rooting out waste, fraud, and abuse through independent audits and investigations and with promoting efficiency and best practices. Thus, inspectors general have a dual mandate of determining whether inappropriate action has occurred within a certain program and whether a program can be run more efficiently. Inspectors general report their findings to Congress semiannually, with more frequent reports in the event of blatant abuse.

Some direct spending departments and agencies have recently employed chief evaluation officers, who encourage evaluations in many of the agencies' programs. For example, the Department of Labor's Chief Evaluation Office reported roughly 30 planned or ongoing evaluations, including evaluations of programs to raise employment among urban youth and the provision of trade adjustment assistance (DOL 2017). No such office exists within IRS or at the Treasury Department under their current structure.

Specially created entities can also play a role in oversight. For example, the American Recovery and Reinvestment Act created the Recovery Act Transparency Board, consisting of at least 10 inspectors general, to oversee the actions taken under the Act.[12] Similarly, the program designed in the Great Recession to quell financial sector turmoil—the Troubled Asset Relief Program (TARP)—created a special inspector general for TARP to oversee the actions taken by Treasury and other government agencies. Both the Recovery Act Transparency Board and the special inspector general for TARP received funding and authority to serve as auditors for these large-scale programs.

The Contrast with Tax Expenditure Evaluation

In practice, tax expenditures are administered by IRS, which, in addition to many processing activities, organizes its functions mainly around (1) examination and audit of taxpayers and (2) taxpayer service in helping taxpayers comply with the tax law. Few individual programs or tax expenditures have dedicated IRS staff, and for the ones that do, analysis tends to derive indirectly from the agency's major compliance efforts, not the broader issues surrounding effectiveness of spending-like programs. Tax policy is separated from tax administration and centered in the Treasury Department's Office of Tax Policy (OTP), but the department's resources are so thin that evaluation is limited. Importantly, just like the IRS, the Treasury does not have staff dedicated individually to most tax expenditures.

Unlike appropriations but like most mandatory spending, many tax expenditures continue indefinitely unless they expire. Expiration occurs only for tax expenditures passed on a temporary basis, either because Congress does not want the expenditures to be permanent, or it doesn't have the available resources to permanently provide for the tax expenditure.

Thus, Congress periodically passes a few dozen tax expenditures, known as extenders. These expenditures tend to be small, ranging from depreciation preferences for race horses to renewable energy tax credits. They make up less than 10 percent of the annual tax expenditure budget. Congress may periodically hold hearings on tax extenders, but extension is often perfunctory. The recent TCJA reduced the number of temporary provisions, but new ones can easily be enacted.

Congress may, at its discretion, hold hearings on various aspects of the tax code, including particular tax expenditures. When Congress is considering tax reform, such hearings can become more frequent; for example, former Ways and Means chairman Dave Camp held dozens of hearings in preparation for his tax reform plan released in 2014.

Tax expenditures are also analyzed by both the JCT and the Treasury Department. The JCT annually releases a tax expenditure report that includes the fiscal cost of each expenditure and a discussion of the concepts surrounding tax expenditures. In addition to annual reports, JCT publishes periodic reports on various tax expenditure topics, such as the distribution of some expenditures by income class. For example, in 2011, JCT released a historical survey of tax expenditure estimates, and in 2008, it published a report on tax expenditures for health care (JCT 2008, 2011).

Like JCT, the Treasury issues a series of estimates of tax expenditure costs. These estimates are traditionally published in OMB's *Analytical Perspectives* volume, which supplements the administration's budget. The volume provides framing information around tax expenditure concepts, but, like JCT, does not specifically evaluate the tax expenditures. In addition, there is no inspector general for tax expenditures, although the Treasury inspector general technically could engage in an analysis of tax expenditures. The result of this lack of evaluation is a piecemeal system of expenditures with limited efficacy.

The bottom line is that tax expenditures face much less oversight and evaluation than discretionary and mandatory spending, despite comparable budget sizes. Tax expenditures lack the systematic and multilayered review established for other types of spending. They are often neglected when demands are made for improved use of economic evidence throughout government. In the next section, we consider reforms that can introduce better oversight to the tax expenditure budget.

AVENUES FOR IMPROVING OVERSIGHT OF TAX EXPENDITURES

Increased transparency and oversight could lead to more efficient and targeted use of tax expenditures to achieve economic and social goals. We are not naïve about the complications of improving such oversight, including opposition from special interests that don't want such information revealed to the public, jurisdictional squabbles among both congressional committees and executive branch departments, and costs including government staff resources.

Despite these obstacles, we present several options that should be considered if progress is to be made. The first set involves funding of evaluations by policy offices within the executive branch, particularly Treasury and the Office of Management and Budget, but also inspectors general. The second set consists of opportunities in nonpartisan congressional agencies, particularly the JCT, CBO, GAO, and the Congressional Research Service. A third set would involve independent evaluations by external evaluators.

A fourth way to enhance accountability is organizational reform, which would set certain processes in motion, perhaps permanently. This would require the participation of some of the actors listed in the first three sets of options. Organizational reform could include congressional budget process reform that would require tax expenditures to be subject to a process like periodic appropriation, particularly for any provisions that otherwise lead to automatic growth; periodic commissions to review tax expenditures, with appointees from both sides of the aisle; and a modest reorganization of IRS to devote more attention to specific programs or tax expenditures under its administrative mandate.

We are less sanguine about giving various public-sector agencies a simple written mandate with no additional resources—the type often ignored or performed weakly. With most of the options below, transparency can be achieved over time with limited additions to resources, for instance, by not requiring that every program be studied or addressed every year. A rotating process is also viable.

We refer to studying "programs" and "tax expenditures" individually rather than collectively, bearing in mind that many with similar purposes might be studied better together. For instance, the tax breaks for homeownership are contained in four separate line items—mortgage interest, property tax, capital gains, and exclusion of net imputed rental income—so that efforts to efficiently reform homeownership ideally would address all at the same time.

Evaluations by Policy Offices within the Executive Branch

The executive branch already has the authority to produce and fund studies and evaluations of tax expenditures. A president or Treasury secretary could demand that such studies be undertaken, or Congress could appropriate money directly for such studies or mandate their undertaking.

Treasury's OTP has by far the most expertise on these tax expenditure issues and contains the largest group of public finance economists with extensive graduate training anywhere in the executive branch. This office, along with the JCT and IRS, has access to IRS data unavailable (because of privacy concerns) to private sector agents and most other government agencies. It also has the most extensive ability within the executive branch to model tax subsidies and related public finance issues. OTP prepares the Treasury's annual estimates on the size of tax expenditures, issued each year by the Office of Management and Budget.

OMB, in our view one of the most capable and influential executive branch agencies, has few highly trained economists and sometimes few to no tax experts, and it depends upon executive branch departments to model programs. Thus, without fundamental reorganization, OMB has limited ability to research and study the design of policy alternatives. It does, however, have great power to require cross-departmental cooperation.

This leads us to conclude that the Office of Tax Policy would be best equipped to prepare such studies, but that OMB should direct and manage cooperation among related agencies. OTP is relatively small, with about 100 professional staff, and those resources already are heavily committed to responding to the short-run concerns of the administration, so resource availability will be a major constraint.

New responsibilities must be structured to ensure that studies are performed and released on a regular and continuing basis, given that executive branch agencies also work to advocate for presidential policies. No matter where evaluations are conducted, they must be sufficiently insulated from the political process. In some ways, the annual release of the tax expenditure budget serves as a model because it has been performed for so long that any attempt to prevent its publication would cause serious political problems.

Expanding responsibilities for IGs would entail a somewhat different approach within the executive branch, but this would also work best if supported by additional resources and some bipartisan agreement. Most work by IGs has been widely regarded as independent. But each IG has a small staff, mainly performs audits (broadly defined), and often doesn't have enough expertise to tackle many issues. Still, because IGs sit in the many direct spending and regulatory agencies, they could report on areas of overlap between their agencies' programs and various expenditures. Their reports could tell us about the relative efficiency or enforceability of programs such as rental vouchers and low-income housing tax credits, mortgage lending regulations and the mortgage interest deduction, Department of Labor and Treasury regulations on pensions and retirement plans, and direct spending and indirect tax subsidies for energy production.

Evaluations by Nonpartisan Congressional Agencies

Congress has at its service several well-respected nonpartisan agencies, including the JCT, CBO, GAO, and the Congressional Research Service. Each has a different mandate and different expertise but, if engaged, could absorb the task of reporting more thoroughly on tax expenditures. Like the offices listed above that are housed in major executive branch agencies, each of these offices is relatively small, limiting how much more they could accomplish without additional resources—and even with more resources, these offices may not consider additional reporting on tax expenditures the next best use of that money.

The JCT is the smallest of these four offices but the only one with direct responsibility for taxes. Its revenue estimates are used in congressional legislation and, to avoid confusion, are seldom disputed by other agencies engaged in revenue estimation.

Like OTP within the executive branch, JCT spends most of its time working on active tax legislation. It engages even less than OTP on studies not of immediate interest to committee leadership—in this case, the chairs of the House Ways and Means and Senate Finance committees. However, as discussed below, periodic reauthorization of tax expenditures would naturally require the JCT to report regularly on those tax expenditures up for reauthorization.

CBO produces options for Congress to consider, but mainly as a menu of strategies to reduce the deficit. Options on some tax expenditures are included, but CBO's tax staff is usually busy with other requirements, including those surrounding congressional budgets. CBO is the newest of the four nonpartisan congressional agencies, and its early leaders took advantage of new resources to encourage more staff-led analyses of budget options than was traditional in other agencies. But the agency, in trying to strike a nonpartisan balance, almost always provides pros and cons and avoids providing recommendations of any sort. It treads very lightly in developing alternatives when it examines existing policies. Despite these limitations, CBO stands out for its expertise on budget matters that include tax subsidies. But it only has a modest staff of a few hundred people, so resource constraints are crucial.

Two other Congressional agencies, the Congressional Research Service (CRS) and the GAO, perform some analysis of taxes and tax expenditures, though, unlike the two just mentioned, GAO has only limited, project-by-project access to tax data and the Congressional Research Service currently has none.[13] While the Congressional Research Service provides reports on a variety of tax policy issues and assists members and committees in their legislative work, it also devotes some resources to answering specific questions of individual members, sometimes in response to constituent inquiries.

The Government Accountability Office is the largest of these nonpartisan congressional agencies and, in recent decades, has expanded significantly the definition of "accounting" for and "auditing" various government programs. It has a long-standing reputation for reporting on the inefficiency of programs and so far has managed to avoid some of the attacks made against other agencies when their reports rankled a member of Congress. While GAO has a broad mandate, it generally defers to the expertise of JCT staff on tax policy issues.

To pull any of these agencies into a much broader effort to report on tax expenditures would require significant reorganization and expansion of capability. These agencies maintain very limited staff for all their current tax work, ranging from about 10 at CRS to about 65 at JCT, and the share of time devoted to systematic evaluation of specific tax expenditures is limited by other demands that take priority.

Evaluations by Independent Actors

The government could also finance independent evaluations by external evaluators or study groups. External evaluators would still be monitored by the agencies under whose budgets they work. But two major issues that we've discussed for different actors would still arise here: Would the evaluations be accepted as independent? And even so, would they receive enough financing?

Any external evaluator would face challenges and scrutiny over their perceived independence, and extensive evaluation does not always produce consensus among evaluators. For example, the academic literature shows much disagreement among researchers on the value of some tax expenditures, particularly those that surround the taxation of capital income. This calls for some attention to how independent actors would be engaged and how their results would be interpreted. One approach would be to fund research on aspects of tax expenditures that are less politically charged or where additional analyses would have bipartisan support.

Organizational Reform

Tax expenditures should be addressed more regularly. Thus, each of the options we've laid out could be put into a law requiring periodic evaluations of tax expenditures.

In this section, we go a step further to examine three ways in which the budget process and IRS could be reorganized to give tax expenditures the attention they deserve: periodic reauthorization of tax expenditures; joint commissions of Congress on tax expenditures; and a fundamental restructuring of the way the IRS tracks and reports on administrative aspects of the programs under its mandate.

PERIODIC REAUTHORIZATION

Beyond mandates for studies by agencies or independent researchers, perhaps the strongest way to ensure that Congress addresses tax expenditures periodically is to put them into a process that requires legislation on each program or tax expenditure over time. Annual sunsetting of tax provisions has earned a poor reputation, but, if done well, periodic sunsetting need not be more difficult than the effective "sunsetting" currently applied to direct appropriations. Even some mandatory programs or entitlements, such as farm subsidies, must be renewed occasionally.

It is particularly important for Congress to control the automatic growth in all programs, whether through direct spending or tax expenditures. Automatic growth in these programs today exceeds by a significant factor all the revenue growth that the economy produces over time as it grows. (This problem exists even in the absence of tax cuts that reduce revenues, such as the TCJA.) Thus, one could "sunset" program growth in the absence of new legislative authority through various formulas, such as caps, that keep the budget in line with desired targets.

A corollary to periodic reauthorization would be a cap on tax expenditures—either a separate cap like the one placed on discretionary spending (and a small share of mandatory spending) through the Budget Control Act of 2011, or the expansion of that cap to include tax expenditures. Thus, tax expenditures would be treated like outlays. But an indiscriminate cap, though effective at holding down spending and perhaps rationing scarce government resources, is at odds with the premise that government programs should be subject to evaluation on their own merits, not whether they fit under an arbitrary cap. Each program ideally should be examined in turn and addressed or reformed appropriately.

JOINT COMMISSIONS

One simple but limited option is the convening of a periodic commission or study group to review tax expenditures, with appointees from both sides of the aisle. Even here there is some difficulty: unelected research appointees to commissions are often the most political members of the research community, identified as Democrat or Republican and seldom independent. US presidents have at times appointed their own commissions—with mixed results, but that doesn't mean this shouldn't be tried. The responsibilities can be defined broadly, or more specifically geared to the pressing needs of policymakers. Simply setting up a process doesn't obviate the need for intentional efforts to ensure the process will work.

But studying all tax expenditures is a formidable task, analogous to studying one-quarter to one-third of all direct expenditures. No such extensive analysis has ever been done with that many direct spending programs, perhaps outside of the Grace Commission's still limited effort to identify "waste."[14] Despite these potential limitations, an occasional commission could give new attention to tax expenditure issues, note where agencies are failing to provide useful input, and recommend more studies along the lines suggested in this paper.

A joint commission could be particularly valuable for examining reform in various areas where direct spending and tax expenditures overlap, such as housing or welfare. Broad health reform almost always involves some sort of joint committee structure to deal with overlapping committee jurisdictions, but it might be best to make such joint structures automatic, if periodic. With such arrangements, programs like the earned income tax credit could be considered along with welfare reform. Programs serving the same constituents could be considered together as well.

RESTRUCTURING OF THE IRS

IRS could reorganize itself in part around the "programs" under its jurisdiction, rather than almost exclusively on tax collection itself.[15] We recognize that IRS is severely understaffed with all the programs and responsibilities under its jurisdiction, and its staffing has been cut substantially in recent years. The staffing problem could be addressed by (1) investing more resources; and (2) reforming programs so that IRS requires fewer resources to fulfill its responsibilities. Legislative reforms could make programs easier to administer and reduce compliance burdens for taxpayers and the IRS. Our suggestion could be achieved modestly, with designated staff of less than 1 percent of IRS total staff that at times has exceeded 100,000.

We do not suggest that IRS unduly devote its efforts to broader policy issues on which it may have less expertise than offices like OTP. Rather, we suggest that IRS more clearly identify issues derived from administering and enforcing the law: the size and distribution of benefits from each program and error rates from both underreporting and overreporting. At least a few staff members should be devoted to tax expenditures in each major spending area (e.g., housing). Compliance studies are only a subset of the work required, though IRS can do a much better job of gleaning information from its audits and examination process.

As a narrow example, a sample of returns could be examined for charitable contributions claimed for clothes donations, and the estimates derived from these data used to make an estimate of the costs of these deductions for the population. The report should indicate the amount that can be verified as reported correctly or reported incorrectly, and the residual amount for which examination cannot determine compliance. The report should also note whether additional audit or examination resources could ever productively address known or potential noncompliance as long as the law was maintained in its current form. Given scarce resources, some items would be examined periodically, not yearly.

In sum, Congress and the executive branch can better address tax expenditures through additional study, budget process reforms, and organizational efforts. Not all require new legislation, but almost all require additional resources and staff time to be effective. At the end of the day, however, such reforms are only likely to work well when elected officials buy into the effort, at time both of adoption and implementation.

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