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TRENDS IN TAX EXPENDITURES: AN UPDATE

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ABSTRACT

Over the period between 2013 and 2029, the sum of the estimated budgetary costs of all tax expenditures as a percentage of gross domestic product will range from approximately 8.5 percent in fiscal year 2017 to 6 percent in fiscal years 2024 and 2025. The Tax Cuts and Jobs Act of 2017 (TCJA) reduced the sum of tax expenditure costs between 2019 and 2025, but after 2025, when most provisions of the TCJA will expire, total costs will rebound to 7.6 percent of gross domestic product by 2029. The TCJA also altered the composition of tax expenditures.

The US federal budget defines tax expenditures as "revenue losses attributable to provisions of the federal tax laws which allow a special exclusion, exemption or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability." The word "special" in this definition implies that tax expenditures are provisions that are exceptions to general rules of a baseline tax system. This baseline system is meant to include provisions needed to implement a practical and broad-based income tax. Thus, for example, the baseline tax law allows deductions for ordinary and necessary business expenses needed to measure net income and for adjustments such as personal exemptions to account for the effect of family size on ability to pay. It also allows some departures from income measurement to account for practical administrative considerations, such as the exclusion of annual accruals of unrealized capital gains.

Many tax expenditures substitute for direct spending programs in promoting economic and social policy objectives and providing assistance to selected groups of taxpayers. They represent a significant share of federal support for homeownership, health insurance coverage for working families, retirement security, and incomes of low-income families with children. They also promote selected forms of saving and investment. Tax expenditures in fiscal year 2019 added up to 6.6 percent of gross domestic product (GDP) and reduced federal income and corporate tax receipts about 42 percent.[1] After the individual provisions of the Tax Cuts and Jobs Act of 2017, or TCJA, expire at the end of 2025, tax expenditures will increase, reaching a projected 7.6 percent of GDP by fiscal year 2029.

This brief updates an earlier brief on trends in tax expenditures between 1985 and 2016 (Rogers and Toder 2011). That brief found that the Tax Reform Act of 1986 reduced tax expenditures from nearly 9 percent of GDP in fiscal year 1985 to 6 percent in 1988 but that tax expenditures as a share of GDP subsequently rebounded to 7.4 percent in 2010 and a projected 7.3 percent in 2016. Rogers and Toder also found substantial changes in the composition of tax expenditures. Taken together, these two briefs reveal a long-run stability in tax expenditures as a share of GDP over the past few decades.

In this brief, we present tax expenditures as a share of GDP for every other year between 2013 and 2029. We then show how the composition of tax expenditures has changed in recent years and will likely change over the rest of this decade. We classify tax expenditures into the following categories: (1) individual versus corporate; (2) personal versus business; (3) tax structure provision versus spending substitute provision; and (4) form of incentive (deferral, exclusion, deduction, special rate, or credit). We also discuss trends in the refundable portion of credits (credits in excess of income tax liability), which the federal budget classifies as outlays instead of tax reductions.

1 In 2019, individual and corporate receipts added up to 9.2 percent of GDP. This is about 42 percent less than the sum of actual receipts plus the revenue losses from tax expenditures (15.8 percent of GDP).

METHODOLOGY

Our main data source is the estimates of tax expenditure costs reported in the budget of the United States government, which is issued annually by the Office of Management and Budget (OMB).[2] Each budget provides estimates of tax expenditure costs for the previous year as well as the projected 10-year budget period.[3] For example, the fiscal 2021 budget, released in February 2020, includes estimates for 2019 through 2029. The budgets also include estimates of GDP, which we use to present the sum of tax expenditure costs as a share of GDP.

We include all odd-numbered fiscal years from 2013 through 2029, using the most recent estimate of tax expenditure costs available for each year. Specifically, we use estimates from the 2015 budget for 2013, from the 2017 budget for 2015, from the 2019 budget for 2017, and from the 2021 budget for 2019 through 2029. We use the latest estimates for each year because they are likely the best available ones.

The OMB lists the outlay effects separately from its estimates of the revenue losses from tax expenditures. This brief shows the total costs of these provisions, computed by adding the revenue and outlay effects.[4] We include in our totals all tax expenditure provisions, except for net imputed rental income on owner-occupied housing, which we exclude to remain consistent with earlier estimates of tax expenditure costs (Rogers and Toder 2011).[5]

When estimating the cost of each tax expenditure, the OMB assumes that all other provisions of the federal individual and corporate income taxes remain unchanged. Because the elimination of some tax expenditures would change the cost of others, the sum of the cost of all tax expenditures is not equal to the revenue gain that would occur if all tax expenditures were eliminated simultaneously. Berger and Toder (2019) estimate that accounting for interactions among nonbusiness individual tax provisions makes the estimated cost of all these provisions about 6 percent larger than the sum of the separate provisions.

2 Under the Congressional Budget Act of 1974, the OMB is required to release an annual list of tax expenditure costs. The list of tax expenditure costs is included in the "Analytical Perspectives" section of the budget. The cost estimates are performed by the Office of Tax Analysis of the US Treasury Department. The Congressional Budget Office (CBO) is required to perform similar estimates for the US Congress; these estimates are prepared by the Joint Committee on Taxation (JCT). We use the OMB estimates for this paper because JCT only projects tax expenditure costs forward for 5 years, while OMB shows them for 10 years. Using OMB data also enables comparison with earlier estimates of historical costs of tax expenditures by one of the authors. See Rogers and Toder (2011) and Toder (1999).

3 The fiscal 2015 budget, released in February 2014, includes estimates for only the five-year budget period of 2014 to 2018, but subsequent budgets include estimates for the prior year and the 10-year budget period. Thus, the most recent budget, published in February 2020, shows estimates for the prior year (fiscal year 2019) and projections for fiscal years 2020–29.

4 The federal budget counts net tax refunds that taxpayers receive in excess of the federal income taxes they owe as outlays instead of reduced receipts.

5 The JCT does not count net imputed rental income as a tax expenditure.

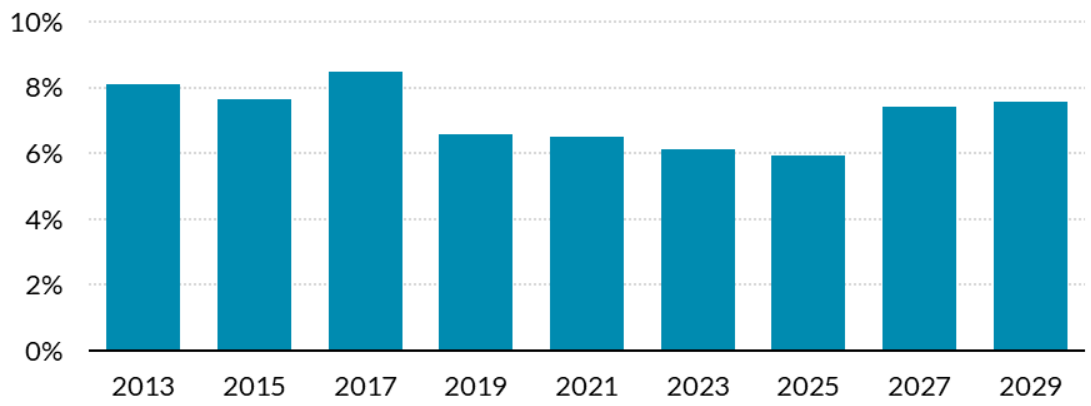
Because the projections used in this brief are based on estimates prepared for the fiscal year 2021 budget, they do not account for the COVID-19 pandemic and its resulting economic effects. The projections also assume no changes in current law, which means that all temporary provisions will expire as scheduled. Given the tremendous amount of uncertainty surrounding the pandemic as well as its effects on the economy, it is difficult to predict how this will change the trends we discuss. If, as appears likely based on 2020 experience, the OMB's projections of GDP for the first few years in the 2021 budget turn out to be overly optimistic, this may affect the sum of tax expenditure costs and their share of GDP, depending on how sensitive tax expenditures are to economic growth. Overly optimistic projections may also lead to future policy changes to address the larger federal debt that will remain after the health crisis is over. We briefly discuss possible effects of the COVID-19 pandemic in a separate section.

FINDINGS

All Tax Expenditures

FIGURE 1

Sum of Tax Expenditure Costs as a Share of GDP
2013 – 29



From 2013 to 2029, the sum of tax expenditure costs as a share of GDP peaked at 8.5 percent in 2017. The TCJA reduced the cost of tax expenditures significantly to 6.6 percent of GDP in 2019, with projected gradual declines through 2025, when it reaches 6.0 percent of GDP. In 2027, after most new provisions of the TCJA have expired, the sum of revenue losses from tax expenditures jumps to 7.4 percent of GDP, slightly below pre-TCJA levels.

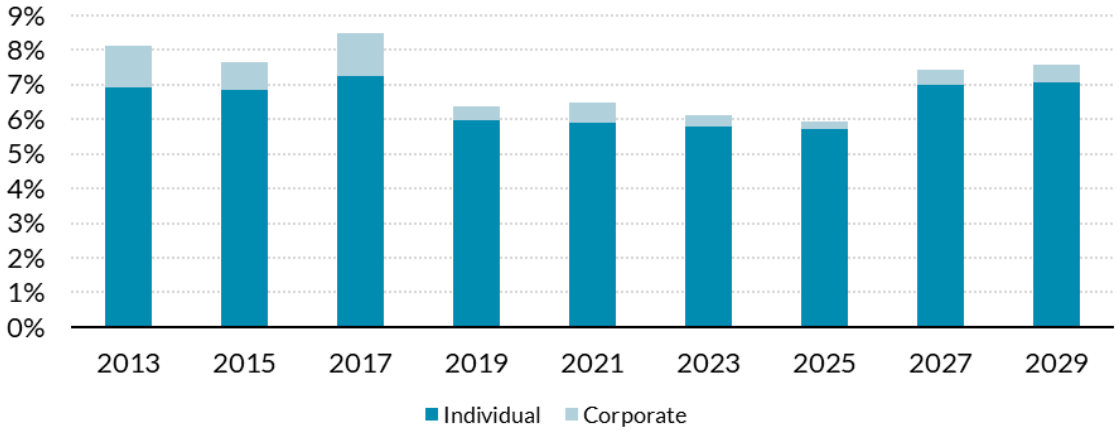
Individual and Corporate Tax Expenditures

The OMB separates the share of tax expenditures claimed on individual tax returns from the portion claimed on corporate tax returns. Most tax expenditures reduce either individual or corporate income tax receipts, but not both. For example, the earned income tax credit is claimed entirely on individual tax returns, while the deduction of foreign-derived intangible income is claimed only on corporate tax returns. However, the cost of other tax expenditures, such as the accelerated depreciation of machinery and equipment, is split between individual and corporate tax returns because many businesses that benefit from these provisions are organized as pass-throughs (partnerships, S corporations, and sole proprietors). These businesses do not pay a business-level income tax but instead report a share of their profit to each owner (shareholder or partner), who then reports that income on his or her individual income tax return.[6]

FIGURE 2

Sum of Tax Expenditure Costs as a Share of GDP

2013 – 29, Individual vs. corporate



The trend in tax expenditures claimed on individual tax returns looks very similar to the trend in all tax expenditures. As a share of GDP, the sum of their costs peaked at 7.2 percent in 2017 and subsequently dropped to 6.0 percent in 2019. The sum of individual tax expenditure costs is projected to remain low and relatively stable until 2027, when it jumps to 7.0 percent of GDP. This marks a return to pre-TCJA levels.

Several provisions of the TCJA contribute to the temporary drop in the sum of individual tax expenditure costs. Under the TCJA, most individuals are subject to lower marginal income tax rates, which causes a reduction in the cost of many tax expenditures. This is because lower tax rates reduce the tax benefit from

6 We account for the distinction between personal and business tax expenditures in the following section.

exclusions, deductions, and deferral of reported income.[7] Further, the TCJA placed a $10,000 cap on the state and local tax deduction, directly reducing the cost of this tax expenditure. This cap, combined with the increase in the standard deduction, also significantly reduced the number of taxpayers who claim itemized deductions and the value of deductions the remaining itemizers claim.

In the other direction, the TCJA increased some tax expenditures. It introduced a new 20 percent deduction for certain income from pass-through businesses (qualified business income) and increased the child credit. All of these changes affecting individual income tax expenditures are set to expire at the end of 2025, which explains the projected return to pre-TCJA levels of individual income tax expenditures in 2027.

The sum of the costs of corporate tax expenditure provisions reached 1.3 percent of GDP in 2017 but then dropped sharply to 0.4 percent of GDP in 2019. It is projected to remain low and relatively stable through 2025, increasing only slightly thereafter. The sum of corporate tax expenditure costs remains well below pre-TCJA levels, reaching a projected value in 2029 of only 0.5 percent of GDP.

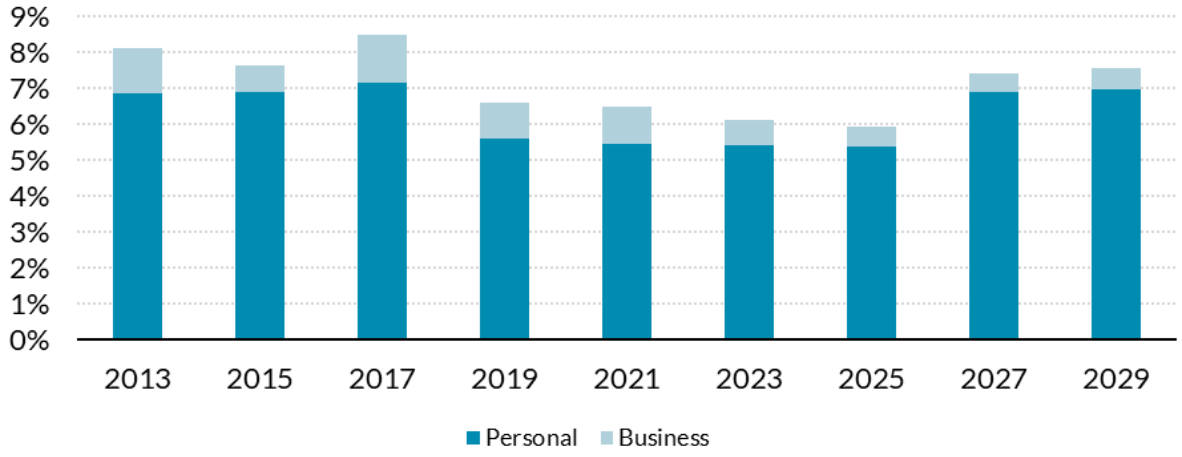
The main cause of the drop in corporate tax expenditures after the enactment of the TCJA was the reduction in the top marginal income tax rate for corporations from 35 to 21 percent. Because this tax rate reduction is permanent, corporate tax expenditures, unlike individual tax expenditures, remain much lower than their pre-TCJA amounts throughout the budget period.

Personal and Business Tax Expenditures

FIGURE 3

Sum of Tax Expenditure Costs as Share of GDP

2013 – 29, Personal vs. business



7 Because exclusions and deductions reduce taxable income, the tax benefits from these provisions depend on the rate at which the excluded and deducted income would have been taxed in the absence of these provisions.

We also categorize tax expenditures as either personal or business tax expenditures. We define business tax expenditures as preferences that affect the measurement of business income or otherwise reduce the tax liability of businesses regardless of whether those preferences are claimed on individual or corporate tax returns. The category of business tax expenditures is broader than corporate tax expenditures because it also includes tax preferences for income of pass-through businesses that are claimed on individual income tax returns.[8] An example of a business tax expenditure is the 20 percent deduction for qualified business income, which can be claimed only by individuals with income from domestic pass-through businesses. In contrast, the mortgage interest deduction is a personal tax expenditure because it applies to personal residences.

The sum of personal tax expenditure costs as a share of GDP trends almost identically to that of individual tax expenditures. It hovered around 7 percent of GDP during the pre-TCJA years and fell to 5.6 percent in 2019. It is projected to remain nearly constant as a share of GDP while the TCJA is in effect before returning to pre-TCJA levels after most TCJA provisions expire. Like individual tax expenditures, the reduced cost of personal tax expenditures from 2019 through 2025 is largely driven by lower individual tax rates, the increase in the standard deduction (which reduced the value of itemized deductions), and the cap on state and local tax deductions under the TCJA.

Business tax expenditures as a share of GDP have remained relatively stable, staying around 1 percent, from 2013 through 2021. From there, the sum of business tax expenditure costs is projected to slowly decline as a share of GDP through 2027, when it reaches 0.5 percent of GDP. This overall decline is partially because bonus depreciation will phase out after 2022. The enactment in the TCJA of bonus depreciation (100 percent expensing) increased the tax expenditure for accelerated depreciation of machinery and equipment. However, its value will become negative in later years as bonus depreciation is phased out between 2023 and 2027 and businesses are unable to claim deductions for the depreciation of equipment they have already expensed.[9] The expiration of the qualified business income deduction at the end of 2025 also reduces the total cost of business tax expenditures.

8 As of 2015, more than 80 percent of businesses were organized as pass-through entities. They accounted for more than 50 percent of total business net income. See "What are Pass-Through Businesses?" Tax Policy Center Briefing Book, accessed March 19, 2021, https://www.taxpolicycenter.org/briefing-book/what-are-pass-through-businesses.

9 The cash value of the tax expenditure for accelerated depreciation in any year does not measure correctly its incentive for investment because the provision changes the timing, not the sum, of deductions from any investment. The incentive effect comes from the increase in the present value of deductions because businesses can claim them sooner, making them in effect equivalent to a zero-interest loan from the government to businesses. The incentive effect of the tax expenditure for accelerated depreciation is positive in all years. The revenue cost of the tax expenditure is greater than the incentive effect when bonus depreciation increases the preference in 2018–22 and is less than the incentive effect as bonus depreciation is phasing out. In some years, the revenue cost turns negative because bonus depreciation deductions in 2018–22 come at the expense of deductions that would have been claimed later.

Tax Structure versus Spending-Substitute Tax Expenditures

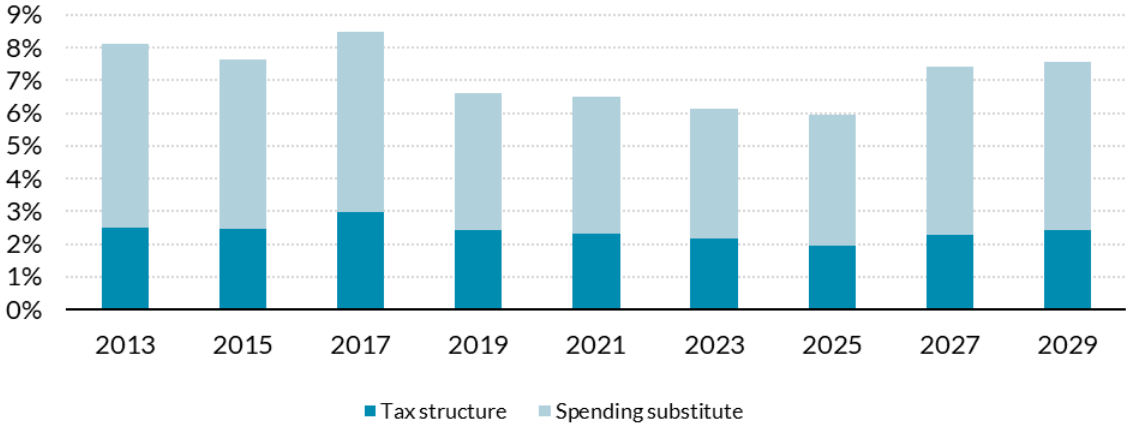
Following Marron and Toder (2012), we classify tax expenditures as either "tax structure" or "spending-substitute" provisions. Most tax expenditures are spending-substitute provisions because they are alternatives to direct spending in subsidizing selected activities or assisting selected taxpayers. For example, the credits and deductions for postsecondary education expenses clearly subsidize higher education and could be designed as a spending program that would produce the same incentives and produce the same allocation of resources. Another example is the home mortgage interest deduction, which supports more spending on owner-occupied housing. If these tax expenditure programs were reconfigured as direct spending, the budget would show higher levels of tax collections and spending even though the real impact of government would not change.

Tax structure provisions represent departures from a comprehensive income tax but do not subsidize a narrow form of activity and could not easily be replaced by a spending program. For example, preferential tax rates for capital gains tax income are a tax structure tax expenditure. They are a choice in income tax design meant to strike a balance between two competing considerations: that all income should be taxed equally and that taxing realized capital gains creates a "lock-in effect" because unrealized capital gains are not taxed.

FIGURE 4

Sum of Tax Expenditure Costs as Share of GDP

2013 – 29, Tax structure vs. spending substitute



The sum of the costs of spending-substitute provisions as a share of GDP remained relatively stable, in the range of 5 to 6 percent of GDP, between 2013 and 2017. Following the enactment of the TCJA, they dropped to 4.2 percent of GDP in 2019 and remain near 4 percent of GDP through 2025. The decline in the value of itemized deductions, including the state and local tax deduction and the mortgage interest deduction, contributes to the lower level of spending subsidy tax expenditure costs during this period. After most TCJA individual provisions expire, projected spending-subsidy tax expenditure costs return almost to pre-TCJA levels, around 5 percent of GDP for 2027 and 2029.

The sum of the costs of tax structure tax expenditures declined from 3.0 percent of GDP to 2.4 percent of GDP in 2019, mostly because of the decreased cost of tax expenditures related to income from controlled foreign corporations. More than 100 percent of the decline in those tax expenditure provisions is because TCJA reduced the top corporate tax rate from 35 to 21 percent.[10] The sum of tax structure tax expenditure costs is projected to continue to decline as a share of GDP through 2025, reaching a minimum of 1.9 percent of GDP, before increasing slightly to 2.3 percent of GDP in 2027.

Tax Expenditures by Type of Incentive

We also categorize tax expenditures by the form that they take: deferral of tax liability, exclusion, deduction, special rate, or credit.

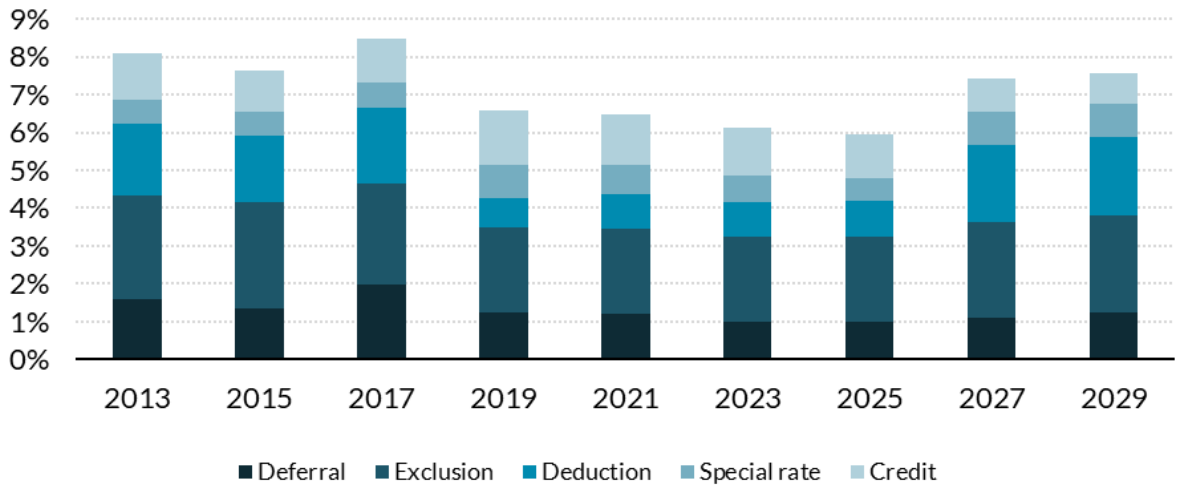
Deferrals

Deferrals are tax expenditures that allow taxpayers to postpone certain tax payments. This reduces the present value of these tax payments, and some taxpayers may fall into a lower tax bracket at the time of payment. One example is the accelerated depreciation of machinery and equipment, which allows businesses to deduct the costs of equipment faster than its value declines (economic depreciation).

FIGURE 5

Sum of Tax Expenditure Costs as a Share of GDP

2013 – 29, Type of expenditure



10 The TCJA replaced the deferral of income from controlled foreign corporations with a reduced tax rate on active income of controlled foreign corporations. In isolation, this change would have led to an increase in the cost of the preferential treatment of foreign source income. However, the reduced corporate tax rate lowered the cost of the preferential treatment of foreign-source income tax more than the change in the form of the preference increased it (Sammartino and Toder 2020).

From 2013 to 2029, deferrals make up between 15 percent and 23 percent of the sum of the costs of all tax expenditures. As a share of GDP, the sum of deferral costs reached a peak of 2.0 percent in 2017. It fell to 1.2 percent of GDP in 2019, and it is expected to remain around 1 percent through 2029. The small but persistent drop in the cost of deferrals after 2017 is largely driven by the elimination of the deferral of income from controlled foreign corporations, which was replaced by the reduced tax rate on active income of controlled foreign corporations.

Exclusions

Exclusions reduce the amount of taxpayers' income that is subject to taxation by excluding specific sources of income from the tax base. The largest exclusion is the exclusion of employer contributions for medical insurance premiums and medical care, which allows employees to exclude payments their employers make for their health insurance premiums and other medical expenses from their gross income.

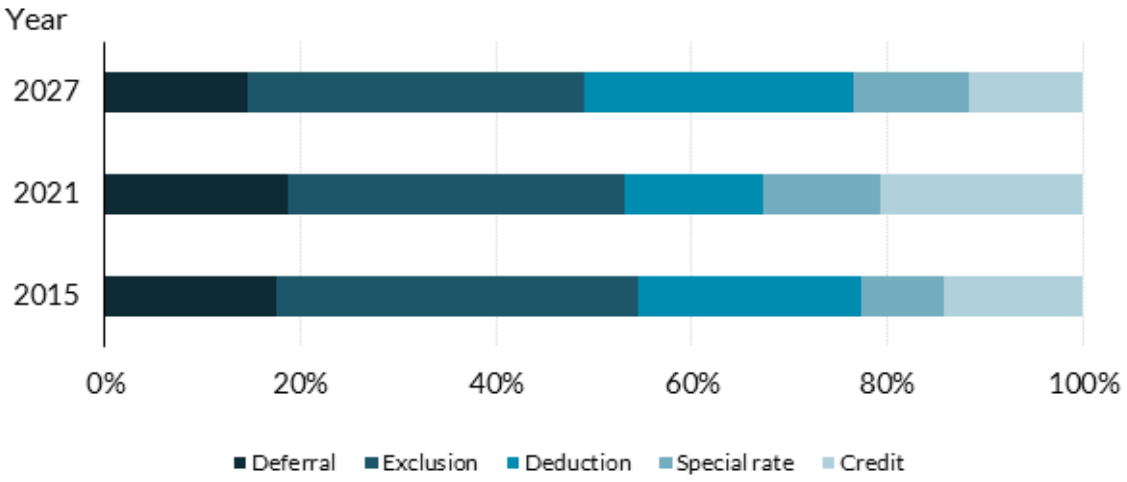
Exclusions consistently make up the largest share, between 32 and 38 percent, of tax expenditure costs. During the pre-TCJA period, exclusion costs were between 2.7 and 2.8 percent of GDP. In 2019, that share dropped to 2.2 percent. It is projected to remain constant through 2025, before rising slightly to 2.5 percent in 2027. This small increase is partially caused by a projected increase in the cost of the exclusion of employer contributions for medical insurance premiums and medical care after 2025, when the lower marginal tax rates for individuals expire.

Deductions

Deductions also reduce taxable income by designating certain uses of income that taxpayers can subtract in computing it. One example is the mortgage interest deduction, which allows homeowners to deduct mortgage interest paid on their primary and second homes.

FIGURE 6

Share of Expenditures by Type



The sum of the cost of deductions relative to all tax expenditures changes significantly between 2013 and 2029, ranging from 12 percent to 27 percent. More specifically, deductions become relatively smaller between 2019 and 2025, the period when most TCJA provisions are in effect. The trend in the sum of deduction costs as a share of GDP is similar. During the pre-TCJA years, the sum of deduction costs hovered around 2 percent before dropping to 0.8 percent in 2019. It is expected to remain relatively stable through 2025; in 2027, it returns to 2.0 percent.

The cap on the state and local tax deduction directly reduces the sum of deduction costs and, as mentioned, the combination of this provision and the increase in the standard deduction reduces the number of taxpayers who itemize their deductions. These TCJA provisions, which are set to expire after 2025, help account for the lower sum of deduction costs from 2019 through 2025.

Special Rates

Certain forms of income are subject to lower tax rates. For example, long-term capital gains are taxed at lower rates than ordinary income.

As a share of GDP, the sum of the cost of special rates remains relatively steady from 2013 through 2029, ranging from 0.6 percent to 0.9 percent. However, the sum of special rates costs grew as a share of all tax expenditure costs after the TCJA took effect, rising from 8 percent in 2017 to 13 percent in 2019. This increase is partially driven by the introduction of the reduced tax rate on active income of controlled foreign corporations, which replaced the deferral of income from controlled foreign corporations. The sum of special rates costs is projected to remain between 10 percent to 13 percent of all tax expenditure costs through 2029.

Credits

Credits are tax expenditures that lessen tax liability by a specified dollar amount. Unlike other tax expenditures, the marginal tax rate does not directly affect the value of a credit. Two examples are the earned income tax credit, which is available to low-income workers, and the credit for research activities, which reduces the tax liability of businesses whose research expenditures exceed a base amount.

Like special rates, the sum of tax credit costs as a share of GDP stays reasonably stable from 2013 through 2029, hovering between 0.8 percent and 1.3 percent. Examining the sum of credit costs as a share of all tax expenditure costs, however, reveals that credits will become more costly relative to other tax expenditures between 2019 and 2025. The sum of credit costs rose from 14 percent of all tax expenditure costs in 2017 to 22 percent in 2019. It is projected to stay around 20 percent until 2027, when it falls to 12 percent. Credits' larger share of all tax expenditure costs from 2019 to 2025 is largely explained by the expansion of the child tax credit under the TCJA. The TCJA doubled the maximum credit, increased the refundable portion, raised the income threshold for the phase-out of the credit, and created a new credit for dependents not covered by the pre-TCJA law child tax credit, while eliminating personal exemptions (which are not counted as a tax expenditure). These provisions went into effect in 2018 and are set to expire in 2025.

Outlay Effects

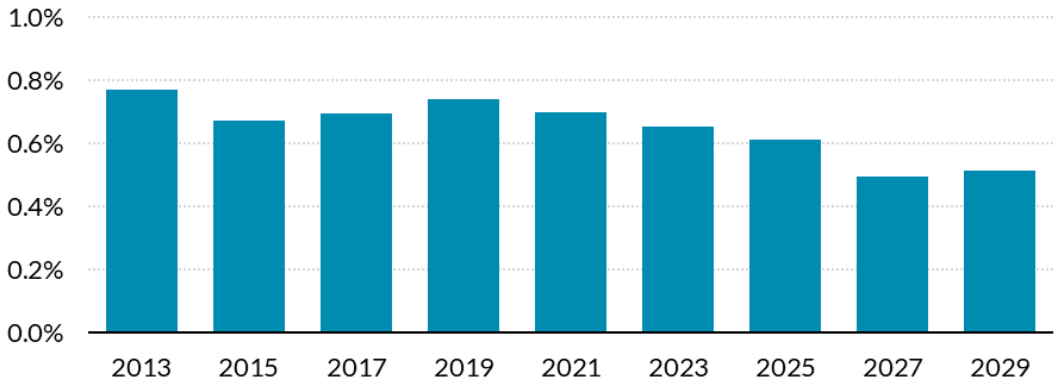
Some tax credits are refundable, meaning that taxpayers can receive the portion of the credit that exceeds their tax liability as a payment from the government. These payments are scored in the budget as outlays. The refundable credits with the largest outlay effects are the earned income tax credit, the premium assistance tax credit, and the child tax credit.

Outlay effects were largest in 2013, at nearly 0.8 percent of GDP, and they have hovered around 0.7 percent of GDP since. Over the next few years, they are projected to slowly decline, reaching approximately 0.6 percent of GDP in 2025. When the expansion of the child tax credit under the TCJA expires after 2025, outlay effects are projected to drop more drastically, falling to less than 0.5 percent of GDP in 2027.

FIGURE 7

Outlay Effects as a Share of GDP

2013 – 29



EFFECTS OF THE COVID-19 PANDEMIC ON TAX EXPENDITURES

The COVID-19 pandemic led to a sharp contraction of economic activity in the second quarter of 2020, followed by only a partial recovery. Although an economic recovery is anticipated once vaccines are widely available and the pandemic subsides, economic output is expected to be lower than previously projected for much of the coming decade.

Lower economic activity will reduce tax expenditures that are conveyed in the form of deductions, exemptions, and deferrals of income recognition for two reasons. First, lower economic activity will reduce the amount of income subject to preferential tax treatment. Second, lower incomes will reduce the average marginal income tax rates individuals pay and thereby lower the value of exemptions and deductions. Lower economic activity, however, will have a smaller effect on the cost of credits, which are not affected by changes in average marginal income tax rates. Other changes in economic variables will have effects on specific provisions. For example, lower projected interest rates will reduce the cost of the mortgage interest deduction, and reduced investment in machinery will reduce the cost of bonus depreciation enacted in the TCJA.

Although the pandemic will likely reduce the total cost of tax expenditures, the reduction will probably be less than proportionate to the reduction in GDP because some tax expenditures are relatively insensitive to income levels. Therefore, the pandemic could increase tax expenditures as a share of GDP.

One source of data now available that provides some indication of the effects of the pandemic on tax expenditures is the most recent report of tax expenditures by the Joint Committee on Taxation, or JCT. JCT's latest report (JCT 2020), shows tax expenditures for fiscal years 2020 to 2024, while the 2019 report (JCT 2019) showed tax expenditures for fiscal years 2019 to 2023. Comparing the last available year in both reports, we find that positive tax expenditures in 2023 added up to $1.745 trillion compared with $1.786 trillion in the

previous year's report, a decline of 2.3 percent.[11] At the same time, between January 2020 and September 2020 (Congressional Budget Office 2020a, 2020b), CBO reduced its projection of 2023 GDP from $24.809 trillion to $22.975 trillion, a decline of 7.4 percent. As a result, COVID-19 raised projected tax expenditures for 2023 by Congressional agencies from 7.2 percent of GDP to 7.6 percent of GDP. Subsequent to JCT's most recent tax expenditure estimates, CBO released its 2021–31 economic projections in February 2021 (Congressional Budget Office 2021). These latest CBO projections show GDP in 2023 rebounding to $24.066 trillion, about 4.7 percent higher than in their September 2020 projections and only 3.0 percent lower than their January 2020 projection.

The projected changes in tax expenditures between the two JCT reports are largely the result of changes in economic projections following the onset of the pandemic, but they could also reflect updates in JCT assumptions or methodologies that are unrelated to economic changes. The four tax expenditure projections for 2023 that declined the most between the two JCT reports were for (1) the reduced tax rate on active income of controlled foreign corporations ($22.9 billion); (2) the exclusion of employer contributions for health care, health insurance premiums, and long-term care premiums ($16.1 billion); (3) reduced rates of tax on dividends and capital gains ($15.7 billion); and (4) the deduction of mortgage interest on owner-occupied residences ($11.7 billion). The latter three could be attributable to a reduction in earnings, marginal tax rates, capital gains, and interest rates; the former could simply reflect revised projections of foreign profits of US multinational corporations that are unrelated to to the pandemic. JCT also projected a substantial increase in the tax expenditure for net exclusion of pension contributions and earnings (about $47 billion for defined contribution plans and another $9 billion for defined benefit plans), which may be attributable to increases in household saving but may also simply reflect changes in the JCT staff's assessment of the effects of these provisions.

In conclusion, the preliminary data confirm our expectation that the COVID-19 pandemic would reduce the absolute value of tax expenditures and increase their value as a share of GDP. But these figures are very preliminary. We cannot disentangle changes in response to fluctuations in the level and composition of economic activity caused by the pandemic from other sources of changes in JCT estimates.

[11] Unlike OMB, JCT also reports some provisions that provide punitive treatment (either by denying deductions needed to measure income properly or applying selective taxes to some forms of income) as negative tax expenditures. To facilitate a closer (though still inexact comparison) with the OMB estimates, we count only positive tax expenditures in the totals reported here.

CONCLUSIONS

Rogers and Toder (2011) found that tax expenditures had "composed a significant component of the cost of government for decades." This remains true nearly 10 years later. Tax expenditures still make up a considerable portion of government costs, and the most recent budget projections indicate that this will continue to be the case for at least the next decade.

Overall, the TCJA caused a moderate but temporary reduction in the sum of tax expenditure costs after 2017. It is expected to rebound after 2025, when most TCJA provisions expire.

This general trend applies to many subsets of tax expenditures. Individual, personal, spending subsidy, and tax structure tax expenditures are all affected similarly by the TCJA; projections show a temporary drop in the sum of their costs during the TCJA years. Corporate tax expenditures are a notable exception to this pattern. Because key provisions of the TCJA affecting corporate income tax liability do not expire, especially the reduced corporate tax rate, there is a projected permanent reduction in the sum of corporate tax expenditure costs after 2017.

Turning to types of tax expenditures, deduction costs become a smaller share of the sum of all tax expenditure costs between 2019 and 2025, while most TCJA provisions are in effect. During this period, credits become relatively more important. Outlay effects of refundable credits remain small relative to the total cost of tax expenditures, and they generally decline over the period from 2013 to 2029.

Finally, we anticipate that the decline in economic activity caused by the COVID-19 pandemic will reduce tax expenditures, but by a smaller percentage than the reduction in GDP, causing tax expenditures to increase as a share of GDP. Preliminary data based on updated CBO economic projections and JCT tax expenditure estimates are consistent with this expectation, but it is too early to reach firm conclusions.

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