

Tax Expenditures

Jun 14, 2019

Tax expenditures are a significant part of America's tax code, playing a major role in our economy. Sometimes referred to broadly as "loopholes," tax expenditures are preferences built into the code that individuals and businesses can take advantage of. Tax expenditures come in a variety of forms including:

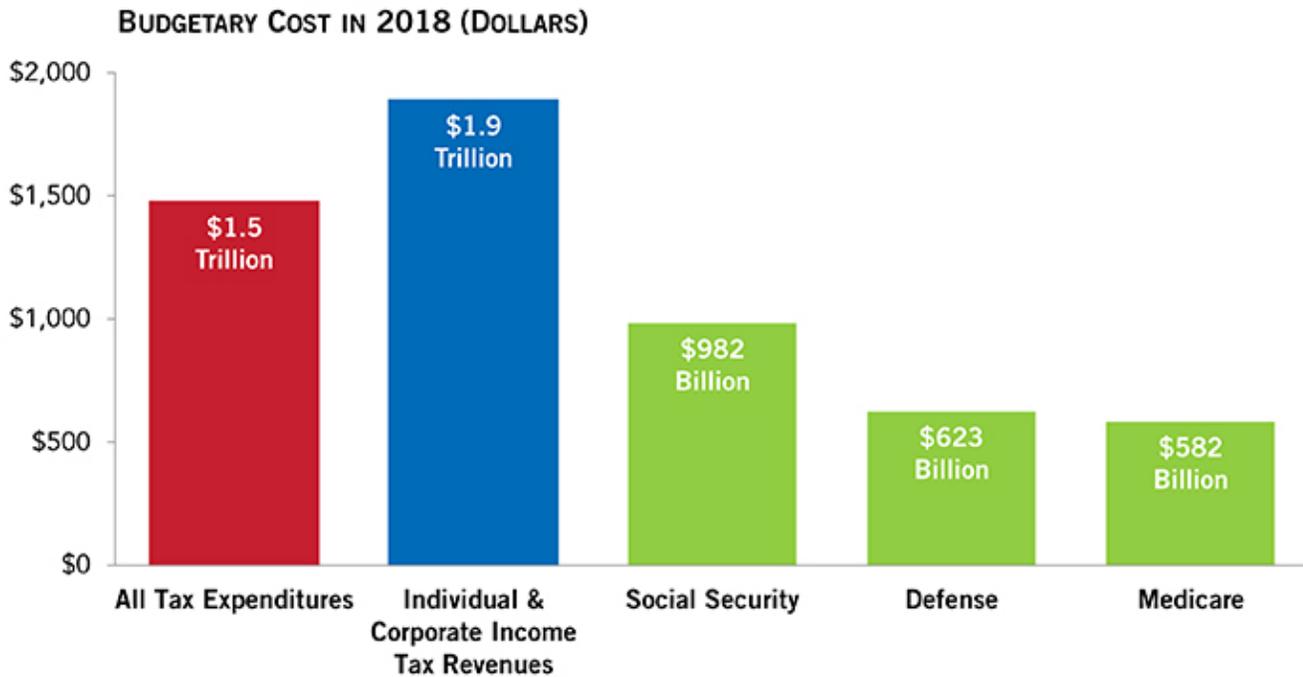
- **Tax exclusions** allow certain categories of income to go untaxed (e.g., active duty pay earned by military personnel in a combat zone is not subject to taxation).
- **Tax exemptions** shield certain assets, or the income taxpayers earn from certain assets, from taxation (e.g., individuals can exempt interest earned from some state or local bonds, and some charitable organizations are exempt from paying income and property taxes).
- **Tax deductions** allow taxpayers to deduct expenses from their taxable income (e.g., deduction on medical expenses in excess of 7.5 percent of individual income).
- **Tax credits** reduce the amount of taxes owed. Refundable credits provide cash back to the taxpayer when taxes owed are less than the credit due.

From an economic standpoint, tax expenditures are very similar to government spending. They are policy choices intended to encourage certain behaviors, and have significant influence over decisions made by individuals and businesses in our economy. For example, the mortgage interest deduction was intended to support homeownership, and the exclusion of employer-sponsored health insurance was meant to support companies covering their employees' health care. In this way, expenditures are, in essence, spending through the tax code.

It is difficult to precisely track and evaluate the efficiency of tax expenditures, as many beneficiaries might have engaged in the desired behavior (e.g., buying a home) without the added tax incentive. But like spending, tax expenditures result in lost revenues and higher deficits for the government. In 2018, tax expenditures totaled \$1.5 trillion – which is more than we spend on many major government programs, and almost as much as we actually collect in individual income taxes.



Total tax expenditures are large in comparison to annual income taxes collected and to the government's major programs



SOURCES: Congressional Budget Office, *Updated Budget Projections: 2019 to 2029*, May 2019; and The Joint Committee on Taxation, *Estimates of Federal Tax Expenditures for Fiscal Years 2018–2022*, October 2018. Compiled by PGPF.

NOTE: Tax expenditures are deductions, credits, exclusions, and preferential rates. The estimates for tax expenditures do not account for any interactive effects of combining various provisions. Medicare spending is net of premiums and payments from the states. Defense represents discretionary defense spending.

© 2019 Peter G. Peterson Foundation

[PGPF.ORG](https://www.pgpf.org)

TWEET THIS

In 2018, six popular tax provisions accounted for \$749 billion – which is more than the government spent on Medicare or defense that year. These tax expenditures include:

- Exclusion of pension contributions and earnings (\$251 billion in 2018)
- Exclusion of employer contributions for medical insurance and care (\$146 billion)
- Preferential treatment of dividends and capital gains (\$129 billion)
- Child Tax Credit (\$104 billion)
- Earned Income Tax Credit (\$70 billion)
- Subsidies for insurance purchased through health benefit exchanges (\$49 billion)

Other Helpful Resources:

What are tax expenditures and how are they structured? Tax Policy Center — <https://www.taxpolicycenter.org/briefing-book/what-are-tax-expenditures-and-how-are-they-structured>

What Are Tax Expenditures — Tax Foundation <https://taxfoundation.org/what-are-tax-expenditures-0/>

Tax Expenditures — Congressional Budget Office <https://www.cbo.gov/publication/52493>

- [Careers](#)
- [Terms of use](#)
- [Copyright policy](#)
- [Permissions](#)
- [Privacy policy](#)
- [Sitemap](#)

© 2019 Peter G. Peterson Foundation. All rights reserved.

Source URL: <https://www.pgpf.org/budget-basics/tax-expenditures>