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Six of the Largest Tax Breaks Explained

There are currently more than 200 tax expenditures, also known as tax breaks, which can take the form of exemptions, deductions, credits, and preferential rates written into the individual and corporate tax codes. In 2018, those breaks totaled nearly $1.5 trillion. To put that in perspective, that's more than the government spends on Social Security, Medicare, or defense.

Tax expenditures should be a key part of any discussion about tax reform. Many economists believe that eliminating some or all tax breaks would benefit the economy by removing market distortions and simplifying the code.

Here are six of the most expensive tax breaks for individuals; together, they account for more than half of the annual cost of tax expenditures:

1. **Exclusion of pension contributions and earnings ($251 billion in 2018)**.Contributions to pension or retirement plans — such as to 401(k)s and IRAs — are not taxed as income when they are received but instead taxed in the future when the employee withdraws the funds.
2. **Exclusion of employer contributions for medical insurance and care ($146 billion)**. The premiums that employers pay for their employees' healthcare are exempt from federal income and payroll taxes. While this tax break benefits a wide swath of Americans by reducing the after-tax cost of health insurance, it is worth more to taxpayers in higher tax brackets than to those in lower brackets.
3. **Preferential treatment of dividends and capital gains ($129 billion)**. Income from capital gains (the profit from the sale of a property or investment) and qualified dividends are taxed at a lower rate than other forms of income. Defenders argue that such preferential rates encourage the sort of investment and risk-taking that spur economic growth, but critics note that they disproportionately benefit the wealthy and encourage tax avoidance.
4. **Child Tax Credit ($104 billion)**. This tax credit is available to taxpayers with children under the age of 24. For children under the age of 17, a portion of the credit is refundable, which means that if the total value of the credit is more than a family's total tax liability, part of the difference is returned as a tax refund by the Internal Revenue Service. Research has shown that the child tax credit has a significant impact for low-income families.
5. **Earned Income Tax Credit ($70 billion)**. This tax credit is primarily available to low-income working parents and the credit is refundable. Research shows that the EITC encourages people to work and that recipients use the credit to cover essential costs.
6. **Subsidies for insurance purchased through health benefit exchanges ($49 billion)**. These tax credits reduce costs for those who purchase insurance plans through the Affordable Care Act marketplaces.

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