



Cut Spending in the Tax Code

Wasteful Spending in the Tax Expenditure Budget is Fertile Ground for Deficit Reduction

Seth Hanlon and Michael Ettlinger March 2011



Center for American Progress



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Introduction and summary

Our nation needs jobs, a strong and competitive economy, and deficit reduction. The way to win that trifecta is not the House of Representatives's continuing resolution for the remaining seven months of fiscal year 2011—a bill panned by a wide range of economists from across the political spectrum as a threat to economic recovery and a job destroyer. And the way to get deficit reduction is not as the House-passed bill does, to initiate immediate cuts concentrated in one narrow area of the budget that funds the most critical investments for long-term economic growth.

Instead, the focus should be on the waste found in the largest area of spending, an area of the budget larger than Social Security, Medicare, Medicaid, or national defense: the more than \$1 trillion of tax-code spending hidden in the federal tax code. Dollars spent through the tax code in the form of tax breaks, called tax expenditures, are widely recognized to be the functional equivalent of direct government spending. After all, give a company a \$1,000 check to subsidize an activity, or give it \$1,000 off its tax bill—the company doesn't care.

Yet the federal government treats tax-code spending very differently than it does direct spending. This keeps tax-code spending hidden, out of sight of budget cutters, and in a generally privileged position in the budget process. Yet the potential savings from cutting spending through the tax code are substantial. With the debate raging in Washington over spending cuts, tax-code spending should be on the table. In this report we identify individual tax-code spending cuts that could total \$64 billion in FY 2012 and \$502 billion over five fiscal years. If enacted, these cuts would be far less harmful than the \$60 billion of short-term direct spending cuts that have passed the House of Representatives.

Over the next several years getting the federal budget deficit under control is critical. Spending cuts should be part of the solution. But we need action to show the world of our commitment to fiscal responsibility now, but actual deficit reduction later. Cutting overall spending too much immediately would be dangerous, with

our economy in such fragile shape, and with unemployment so high. Nevertheless, it is clear that for the government to have a budget it can operate under—to keep its doors open and to keep public servants at work—the House of Representatives will insist that there be a cut in overall spending levels. So let's put some of the least effective government spending there is on the table—let's look at the savings available to taxpayers through reducing the spending in the tax code.

The House continuing resolution

The terms of the fierce debate in Washington over spending cuts have been set by the new Republican majority in the House of Representatives with its aggressive first marker—the roughly \$60 billion in cuts in its proposal for a continuing resolution for the remainder of FY 2011. The House bill, however, is fatally flawed. Its narrow targeting of non-security discretionary spending—a portion of the budget that comprises only one-seventh of total federal spending—would do great harm to the nation.¹

Extracting tens of billions of dollars in cuts from this narrow slice of the federal government requires that the cuts run deep—much deeper than is desirable or even practicable. These cuts would force sudden, dramatic, and dangerous reductions in the government services on which all Americans rely. As the Center for American Progress previously detailed, the cuts would do great harm to the economy, undermine our energy security and innovation, make our country less safe, severely damage our education system, and hurt the most vulnerable and least able to sacrifice in our society.

A wide range of economists from across the political spectrum, including Federal Reserve Chair Benjamin Bernanke, former McCain presidential campaign advisor Mark Zandi, and Goldman Sachs Group Inc. predict the House spending cut bill would cause the loss of hundreds of thousands of jobs and harm today's economic recovery. In sum, the cuts passed by the House could put the brakes on our economic recovery, hurt the health of America's communities, and damage our future competitiveness and growth.

Although budget balancing including spending cuts will indeed have to be addressed in the next few years, there is a serious question about whether policymakers should be considering immediate spending cuts with the economy as fragile it is and with unemployment so high, or instead be taking steps now but for future deficit reduction. Nevertheless, it is evident, given the views of the majority in the House of Representatives, that any agreement to keep the government up and running will indeed have to include cuts.

Extracting tens of billions of dollars in cuts from a narrow slice of the federal government requires that the cuts run deep.

But there is no reason why those cuts should be so narrowly targeted at one particular area of spending. In particular, the discussion should include a type of spending known as tax-expenditure spending, which often escapes the scrutiny it deserves, is mostly allowed to continue year-after-year untouched, and is particularly likely to function as unjustified subsidies for special interests.

What they are saying about tax expenditures

[C]utting annual domestic spending alone won't be enough to meet our long-term fiscal challenges. . . . [I]f you're really serious about the deficit—not just spending, but you're serious about the deficit overall—then part of what you have to look at is unjustifiable spending through the tax code, through tax breaks that do not make us more competitive, do not create jobs here in the United States of America.

— President Barack Obama, February 15, 2011

We need to take a long and hard look at the undergrowth of deductions, credits and special carve-outs that our tax code has become. And yes, we need to acknowledge that what Washington sometimes calls tax cuts are really just poorly disguised spending programs that expand the role of government in the lives of individuals and employers.

— Speaker John Boehner (R-OH), August 24, 2010

In the quarter century since the last comprehensive tax reform, Washington has riddled the system with countless tax expenditures, which are simply spending by another name.

— *The National Commission on Fiscal Responsibility and Reform, The Moment of Truth (Report of the Chairmen of the President's fiscal commission: Erskine Bowles and former Sen. Alan Simpson, Dec. 2010).*

Many tax expenditures substitute for programs that easily could be structured as direct spending. When structured as tax credits, they appear as reductions of taxes, even though they provide the same type of subsidy that a direct spending program would, and like a spending program, must be financed either by tax increases, cuts in other spending programs, or increases in the deficit that pass the cost to future generations.

— *Bipartisan Policy Center, Restoring America's Future (Report of the Debt Reduction Task Force chaired by former Senator Pete Domenici and Dr. Alice Rivlin, November 2010).*

[W]e must admit that not all of [recent] spending has been through increased appropriations or expanded entitlements; much of it has been through the backdoor proliferation of "tax expenditures"—provisions that technically reduce someone's tax liability, but that in reality amount to spending through the tax code.

— *House Ways and Means Chairman Dave Camp (R-MI), November 16, 2010*

[A]ll of the deductions, exclusions, credits, and set-asides in the tax code . . . are costing the Treasury more than a trillion dollars in revenue a year. That matches all of domestic discretionary spending. And many are no different than traditional spending programs—they are simply spending through the tax code.

— *Senate Budget Committee Chairman Kent Conrad (D-ND), February 2, 2011*

"When it comes to spending cuts, Congress is looking in the wrong place. Most federal nondefense spending, other than Social Security and Medicare, is now done through special tax rules rather than by direct cash outlays. These tax rules—because they result in the loss of revenue that would otherwise be collected by the government—are equivalent to direct government expenditures. . . . If Congress is serious about cutting government spending, it has to go after many of them. . . . Cutting tax expenditures is really the best way to reduce government spending.

— *Dr. Martin Feldstein, The 'Tax Expenditure' Solution for Our National Debt, Wall Street Journal, July 20, 2010.*

Moving to tax expenditures

The savings to taxpayers available by cutting “tax expenditures” are substantial. Whether in the form of special exemptions, deductions, or credits, tax expenditures are essentially federal-spending programs administered by the Internal Revenue Service. While most government programs promote policy goals by spending taxpayer money directly, IRS programs promote many of the same goals by distributing special tax breaks.

The federal government, for example, could subsidize oil drilling by providing \$4 billion in direct grants or contracts to oil and gas companies for drilling this year, or \$40 billion over the entire decade. Or, it could—as the federal government does today—provide that same \$4 billion-a-year, \$40 billion-a-decade through tax breaks worth the same amount and available to those companies engaged in oil and gas production.

Economists have recognized for decades that there is no meaningful difference between tax expenditures and programs that spend money directly: Whether that annual \$4 billion subsidy for oil and gas—at a time when oil companies are again posting record profits—is spent directly or through a special tax code provision, the end result is that the oil companies are \$4 billion better off every year. And the public purse is out the exact same amount, which in turns means that the federal budget deficit is that much bigger.

Fortunately, the fact that tax expenditures are government spending is more and more widely recognized by leaders of all political stripes, inside and outside of government. (see box on page 4)

With a combined cost in FY 2010 of \$1.02 trillion, tax expenditures constitute a bigger part of the budget than Social Security, Medicare, Medicaid, or national defense.² They are more than twice as large as all non-security discretionary programs combined. (See table on page 6)

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Breaking down the federal budget

Federal spending, fiscal year 2010 in \$ billions

Defense and security	815
Medicare and Medicaid	719
Social Security	701
Other mandatory programs	644
Discretionary programs	491
Interest on the debt	196
Tax expenditures	1,025

Source: Budget of the United States Government, Fiscal Year 2012, Tables S-4 and 17-1.

Still, they receive far less scrutiny than direct-spending programs. As the Center for American Progress emphasized in its report “[Government Spending Undercover](#),” there are several reasons why tax expenditures often fly under the radar.

First, tax expenditures are not periodically reviewed, unlike the budgets of individual federal government departments and agencies, which are set by Congress annually through the appropriations process. Most tax expenditures are permanent fixtures of the tax code with costs that tend to drift upwards over time. In this sense, most tax expenditures are comparable to entitlement spending because the overall budget cost is not set periodically by Congress once the provision is in law but instead determined by factors beyond Congress’s control, such as the number of people qualifying for benefits (in this case tax benefits) in any given year.

In reality, Congress typically exercises little control over tax expenditure costs. Some tax expenditures “sunset,” meaning they expire after a certain time period, but Congress has typically packaged these provisions together and renewed them every year with no formal review process. (These so-called “tax extenders” are discussed further below.)

Second, tax expenditures do not have to compete against other spending priorities of the relevant congressional committees. Appropriations committees must work within the constraints of the budget resolution, which provides allocations, divided into sub-allocations according to subcommittee. Authorizing committees must receive a budget to pass legislation increasing spending in their areas. In contrast, tax expenditures need only be approved by the two tax-writing committees (the House Ways and Means Committee and Senate Finance Committee). The tax-writing committees have the singular authority to spend money without a budget allocation.

Finally, because tax expenditures are often sold as tax cuts, they enjoy a politically favored status. Despite there being no meaningful substantive difference between spending through the tax code and direct spending, tax expenditures are not counted as spending in the budget; their effects are hidden as reductions in revenues. Fiscal cost estimates are published only for informational purposes in the Analytical Perspectives section of the budget.³

Not surprising, given its privileged status in the budget process, tax-code spending has proliferated over time. The last time Congress significantly reduced tax-code spending was in the Tax Reform Act of 1986. A recent analysis by the Joint Committee on Taxation found that the number of tax expenditures increased by

60 percent since then. Some tax expenditures have come and gone in the intervening time, but as the Joint Committee observed, “in general, tax expenditures, once adopted, tend to stay in place.”⁴

Tax expenditures have not only proliferated in number, but also in cost. The fiscal cost of tax expenditures roughly doubled from \$508 billion in 1988 (the first full fiscal year after tax reform) to \$1.025 trillion in 2010 (in constant 2010 dollars).⁵

In this hidden \$1 trillion world of tax expenditures, there are many tax-spending programs that serve little policy purpose or have long outlived their effectiveness. The following examples only scratch the surface.

Oil and gas subsidies

The oil and gas industry is one of the most profitable industries on earth. The top five multinational companies have reported nearly \$1 trillion in profits this decade. And yet the oil and gas industry stands to collect about \$4 billion in tax-code subsidies in the coming year and nearly \$40 billion over the rest of the decade.

Two of the major subsidies in the tax code—expensing of intangible drilling costs and “percentage depletion”—were enacted in 1916 and 1926, respectively, at a time when oil exploration was a fledgling industry. Today, the oil and gas industry is a mature, extremely profitable industry enjoying windfalls from oil prices exceeding \$100 per barrel. The industry simply does not need \$4 billion in special tax breaks as an incentive to do what it already does.⁶

Moreover, our country simply cannot afford to continue this wasteful spending at a time when Congress is considering cutting critically important public services including energy assistance for low-income families.⁷ Cutting tax spending can yield savings to taxpayers now and continually over the coming decade to help reduce our federal budget deficit.

Tax breaks for vacation homes and yachts

The tax code currently allows a tax break for interest paid on mortgages used to buy vacation homes and, incredibly, loans for the purchase of yachts. The deduction that the tax code allows for mortgage interest is intended to promote homeownership, but allowing taxpayers to claim it on both a primary residence and

a vacation property or yacht does not, by definition, expand homeownership. It simply does not serve an important public purpose—it just arbitrarily favors certain industries and people over others.

This is also a prime example of an inequitable tax subsidy—giving the wealthiest an extra tax break on their vacation properties or yachts while regular homeowners who can't afford such luxuries can claim only a deduction on one home and renters receive no deduction at all. The allowance of the deduction for boat loans is particularly appalling. Under current tax rules, boats can qualify as second homes eligible for the tax break only as long as they contain basic living accommodations including sleeping spaces, bathrooms (heads), and kitchens (galleys)—so, in other words, only large boats qualify. At a time of serious fiscal challenges, policymakers must ask what possible public purpose is served by spending public funds to subsidize boat loans for sizable yachts over other public purposes.

The carried-interest loophole

A special loophole permits the managers of hedge funds and private equity funds to pay preferential capital gains rates on much of their compensation. This subsidy for certain occupations results in some of the richest people in America enjoying huge tax benefits that are unavailable to middle-class Americans with other jobs. The carried-interest loophole is an egregious tax subsidy, and represents wasteful spending through the tax code at its worst.

These are only the most striking examples of wasteful tax spending. Buried in the tax code are scores of other questionable provisions, as we detail further below in this report. If policymakers are looking to cut wasteful spending, they should bring some long overdue budget scrutiny to tax expenditures.

Tax expenditures and the current budget debate

Unfortunately, tax expenditures have largely been ignored by the current budget debate, which has focused almost exclusively on nonsecurity discretionary spending. Granted, reining in tax expenditures halfway through the year poses logistical challenges. Amending tax provisions designed to last an entire tax year, to be reconciled on an annual tax form, is complicated. Yet in many cases savings could be obtained simply by making the subsidy in question available only for activity up to a certain date.

Furthermore, mid-year cuts in direct spending also pose daunting practical and logistical challenges. It is difficult to cut off any public-spending program on a dime—there are contracts that must be fulfilled, projects in mid-stream, and workforces in place. In fact, according to the Congressional Budget Office, the “\$60 billion” in cuts that the House Republicans propose would only save \$5 billion in 2011—with additional savings not realized until 2012.⁸ Thus, the timing of budget savings should not preclude putting tax expenditures on the table as part of the current budget discussion for FY 2011.

This report offers a menu of tax expenditures that are much better candidates for reduction or elimination than many of the vital public services targeted by the House continuing resolution, H.R. 1. The full-year savings would amount to about \$64 billion in FY 2012 if fully phased in. It is likely, however, that transition rules would have to be put in place in fairness to taxpayers who had acted in reliance on the existing rules and to make compliance possible.

The five-year savings would be \$502 billion (also less than the cost of transition rules, which would be less significant over the longer period). Unlike the proposed cuts to federal government department and agency budgets for the current fiscal year that the House has passed, the cuts to tax expenditures would be permanent, with budget savings stretching over many years.

The savings from these tax expenditures could be used for either deficit reduction or higher priority spending. Given the state of the economy we would strongly

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recommend that the bulk of the savings in the near term be used for higher priority, job-creating investments—and only later, after the economy is more firmly on its feet and unemployment is down, for deficit reduction. Nevertheless, if net spending cuts are the order of the day now, better these wasteful provisions than most of the programs targeted in H.R. 1.

We have selected the tax expenditures listed below as sources of taxpayer savings because they serve little or no public purpose or are poorly designed. Note that this is, by no means, a complete list of tax-code spending provisions that deserve close scrutiny. We have focused on a narrower list of provisions where savings could start to be realized relatively quickly. These are also mostly provisions that are either included in the president’s budget proposal or in the prior CAP publication [“A Thousand Cuts: What Reducing the Federal Budget Deficit Through Large Spending Cuts Could Really Look Like.”](#)

To be sure, not all tax expenditures are created equal. Some serve important purposes, and do so effectively and efficiently. Others do not. Cutting tax expenditures indiscriminately is simply unwise. As with all spending programs, tax-expenditure programs should be evaluated regularly for effectiveness, and policymakers should use those performance evaluations as the basis for smart budgeting.

Potential tax expenditure cuts

Oil and gas industry tax breaks

As discussed above, the tax code doles out \$4 billion in annual subsidies to the oil and gas industry. These subsidies are wasteful and ineffective, and should be eliminated. President Obama's FY 2012 budget eliminates eight specific tax breaks for the oil and gas industry:

- The investment tax credit for enhanced oil recovery projects.
- The production tax credit for oil and gas from marginal wells.
- Expensing of intangible drilling costs.
- The deduction for qualified tertiary injectant expenses.
- The exception to the passive-loss limitation rules for working interests in oil and natural gas properties.
- Percentage depletion for oil and natural gas wells.
- The domestic manufacturing deduction for oil and natural gas companies.
- The geological and geophysical amortization period for independent producers is increased to seven years.

Eliminating all eight of these tax expenditures would mean immediate savings for taxpayers of \$22.8 billion between fiscal years 2012 and 2016. (see chart)

Eliminate oil and gas tax breaks, combined	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$3,472	\$5,360	\$4,858	\$4,601	\$4,576	\$22,867

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Tax breaks for the coal industry

The president's FY 2012 budget also eliminates four separate tax breaks for the coal industry:

- Expensing of exploration and development costs
- Percentage depletion for hard mineral fossil fuels
- Capital gains treatment for royalties
- The domestic manufacturing deduction for coal and other hard mineral fossil fuels

Eliminating these four tax breaks would save taxpayers \$136 million in FY 2012 and \$1.1 billion over the next five fiscal years.

Eliminate coal tax breaks, combined	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$136	\$222	\$236	\$249	\$265	\$1,108

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Business inventory methods

The president's budget cuts special tax provisions that allow companies to choose the most favorable methods for valuing their inventory and cost of goods sold. Specifically, the proposal would require taxpayers using the "last-in-first-out" method, or LIFO, to transition to the first-in-first-out method, or FIFO. The proposal would also eliminate the use of the lower-cost-or-market, or LCM, and subnormal goods inventory accounting methods.

Eliminating these two tax breaks would save taxpayers \$9.2 billion in FY 2012 and \$72 billion in total between FY 2012 and FY 2016.

Eliminate LIFO and LCM inventory accounting methods	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$9,200	\$16,500	\$17,300	\$17,800	\$11,200	\$72,000

CBO, Reducing the Deficit: Spending and Revenue Options (March 2011).

Eliminating international tax subsidies

The U.S. tax code subsidizes offshore investment by U.S. corporations by allowing deferrals on overseas profits. The following reforms proposed in the president's FY 2012 budget reduce the impact of this subsidy:

- Defer deduction of expense, related to deferred income
- Determine foreign tax credits on a pooling basis
- Tax currently excess returns on intangibles transfers
- Limit income shifting via intangible property transfers
- Modify the rules for dual-capacity taxpayers

Let's examine each of these reforms in turn.⁹

Defer deduction of interest expense related to deferred income

Currently, companies are permitted to deduct expenses that are properly allocable and apportioned to foreign-source income even if tax on such income is deferred until later years. This creates a mismatch between income and expenses that amounts to a subsidy (a negative tax rate) for investments that create foreign-source income.¹⁰

The president's budget eliminates this unjustifiable subsidy by requiring that if foreign-source income is deferred, expenses that are properly allocated and apportioned to that income must be deferred as well. Eliminating this tax break would save taxpayers \$3 billion in FY 2012 and \$25 billion in total between FY 2012 and FY 2016.

Defer deduction of interest expense related to deferred income	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$2,986	\$5,138	\$5,396	\$5,636	\$5,861	\$25,017

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Determine foreign tax credits on a pooling basis

A weakness in the international tax rules allows U.S. corporations to use foreign tax credits to reduce U.S. tax on income earned abroad through “cross-crediting.” Cross crediting enables companies to reduce U.S. taxes on foreign income by selectively repatriating earnings while deferring income in low-tax countries, including tax havens.

International tax experts have called cross-crediting “the equivalent of the U.S. government giving the [corporation] a grant in the amount of the U.S. residual tax

eliminated.”¹¹ The president’s FY 2012 budget proposal addresses cross-crediting by determining foreign tax credits on a pooling basis.

Eliminating this tax break would save taxpayers \$2.6 billion in FY 2012 and \$22 billion in total between FY 2012 and FY 2016.

Determine the foreign tax credit on a pooling basis	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$2,655	\$4,568	\$4,798	\$5,011	\$5,211	\$22,243

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Transfer pricing

Another way our current tax code subsidizes offshore investment is through weak rules governing “transfer pricing.” Multiple studies, including reports by the U.S. Treasury Department and the nonpartisan congressional Joint Committee on Taxation, find significant evidence that multinational corporations use transactions with related entities to shift income, for tax purposes, out of the United States into low-tax countries. A U.S. corporation, for example, might shift income abroad by selling or licensing a valuable intangible asset such as a patent or formula to an overseas affiliate at an artificially low price. The corporation then enjoys the benefit of deferred taxes on the profits earned by the affiliate.

A proposal in the president’s FY 2012 budget would restrict the use of such methods by ensuring that excess returns from such transactions are not tax-deferred. The president’s budget for the coming fiscal year also plugs gaps in the current rules on transfers of intangible property by applying them to valuable business assets such as workforce in place, goodwill, and going concern value.

Eliminating these tax breaks would save taxpayers \$1.2 billion in FY 2012 and \$10.3 billion in total between FY 2012 and FY 2016.

	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
Tax currently excess returns on intangibles transfers	\$1,204	\$2,038	\$2,114	\$2,212	\$2,280	\$9,848
Limit income shifting via intangible property transfers	\$29	\$63	\$90	\$118	\$148	\$448

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Modify the rules for dual-capacity taxpayers

Current tax rules provide a special benefit to multinational corporations in extractive industries such as oil and gas, and mining. These companies are allowed to claim credits against the taxes they have paid to foreign governments even in some instances where they have received a specific economic benefit in exchange for their tax payments, such as the right to extract the country's oil resources.

These types of corporate expenses should not be creditable. To allow a tax credit is simply to provide a special subsidy. The president's FY 2012 budget would ensure that such taxpayers (known as "dual-capacity taxpayers") do not receive larger foreign tax credits than other businesses.

Eliminating this tax break would save taxpayers \$532 million in FY 2012 and \$4.5 billion in total between FY 2012 and FY 2016.

Modify the tax rules for dual-capacity taxpayers	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$532	\$918	\$974	\$1,031	\$1,085	\$4,540

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Limit itemized deductions for top-bracket taxpayers

Some of the largest tax expenditures are "itemized deductions" intended to subsidize certain activities. One of the effects of providing subsidies through tax deductions is that they provide much bigger tax benefits to those in the highest tax brackets. For a wealthy taxpayer in the highest 35-percent tax bracket, a \$100 itemized deduction is worth \$35, but for a taxpayer in the lowest 10-percent bracket that same deduction is worth \$10 (if the taxpayer itemizes deductions).

This tax-code spending is not only inequitable, but also inefficient because it targets expensive federal subsidies at those who need them the least. President Obama's FY 2012 budget would limit the value of itemized deductions for those in the highest brackets to the same tax benefit that a family in the 28-percent bracket would receive. This reduces wasteful tax-code spending while better targeting incentives.

Eliminating this tax break would save taxpayers \$6 billion in FY 2012 and \$114 billion in total between FY 2012 and FY 2016.

Limit itemized deductions for top-bracket taxpayers	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$6,008	\$18,996	\$26,418	\$29,766	\$32,696	\$113,884

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

End tax subsidies for private equity and hedge fund managers

The president's FY 2012 budget would eliminate the carried-interest loophole detailed on page 8. This means these fund managers would be required to report the profits they receive as compensation for their services as ordinary income, subject to the same rates paid by all other workers.

Eliminating this tax break would save taxpayers \$2.3 billion in FY 2012 and \$10 billion in total between FY 2012 and FY 2016. (see chart)

End tax subsidies for private equity and hedge fund managers	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$2,274	\$2,123	\$2,154	\$1,927	\$1,608	\$10,086

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Remove the exception from passive-loss rules for \$25,000 in rental loss

Rental-property investors benefit from several subsidies delivered to them through the tax code. One of these subsidies comes in the form of a special dispensation from rules relating to how investment losses are treated. Investment losses are usually subject to specific rules designed to limit taxpayers' ability to use losses as a tax shelter, but there is a specific exception for rental-property investors.

Eliminating this tax break would save taxpayers \$13.1 billion in FY 2012 and \$84 billion in total between FY 2012 and FY 2016.

Remove exception from passive loss rules for \$25,000 in rental loss	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$13,110	\$14,830	\$16,730	\$18,880	\$20,200	\$83,750

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table S-8

Eliminate the tax subsidy for private-purpose bonds

When an individual or corporation buys a bond and earns interest on that investment, the individual or corporation has to pay taxes on that interest. There are several exceptions to this rule, however, including certain state-and-local bond issuances for private purposes. These include bonds for certain energy facilities, water-and-sewage plants, airports, docks, hospitals, and private schools, among others.

The exclusion from taxable income of interest from these bonds amounts to a government subsidy because the bond's tax-exempt status allows the bond issuer to borrow at a lower cost than they otherwise would.

Eliminating this tax break would save taxpayers \$4.4 billion in total between FY 2012 and FY 2016, and more in later years.¹²

Eliminate the tax subsidy for private purpose bonds	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$-	\$110	\$662	\$1,433	\$2,205	\$4,410

Eliminate write-offs for corporate meals and entertainment

Eating and entertainment is a personal expense. If an individual takes his family out to dinner, he cannot deduct the cost of that meal from his taxable income. If, however, he takes someone out to lunch and claims it is for a business purpose, then he can deduct half of the cost of the meal.

This special exception acts as an unnecessary subsidy for many people who can benefit from expense accounts and their guests. Allowing deductions for business meals and entertainment also results in an unknown quantity of abuse and fraud—classifying personal expenses as “business” expenses.

This particular subsidy has been reduced twice before, and fully eliminating it will save approximately \$11 billion in FY 2012, and between FY2012 and FY 2016 would save taxpayers \$62 billion.¹³

Eliminate write-offs for corporate meals and entertainment	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$11,127	\$11,654	\$12,267	\$12,940	\$13,586	\$61,574

Replace state and local government tax-exempt bonds with Build America Bonds

The tax exclusion on state and local government bonds serves a valuable purpose, enabling many important public investments. But it is an inefficient tax-spending program. A better approach was tried and proven successful with the Build America Bonds program, launched as part of the American Recovery and Reinvestment Act of 2009 but unfortunately not renewed by Congress at the end of last year.

Build America Bonds provided a direct subsidy to state-and-local governments instead of providing an indirect subsidy through tax breaks for investors. This approach is more efficient because the subsidy goes right to the governments and is not distorted by complicated interactions with tax brackets. Replacing tax-exempt bonds with Build America Bonds and setting the subsidy rate appropriately would achieve deficit reduction.

Reforming this inefficient tax-spending program would save taxpayers \$7 billion in total between FY 2012 and FY 2016.¹⁴

Replace tax-exempt bonds with direct subsidy bonds at 25% subsidy rate	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$92	\$669	\$1,385	\$2,077	\$2,815	\$7,038

Eliminate deferral of taxes on non-dealer installment sales

A special rule allows sellers of real estate or businesses to defer paying taxes on gains from sales if they are paid in installments. Ordinarily a seller would have to recognize income and pay taxes in the year the sale occurs, or alternatively, pay interest to make up for the benefit of deferred taxes. But sellers can defer taxes on up to \$5 million from installment sales until later years.

Congress could eliminate this tax expenditure or reduce it by lowering the \$5 million limit. The savings to taxpayers in FY 2012 would be \$830 million and between FY2012 and FY 2016 would amount to \$6 billion if this tax expenditure were eliminated. A lower amount of savings could be achieved by lowering the \$5 million limit.

Limit deferral of income from installment sales	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$830	\$1,020	\$1,230	\$1,420	\$1,600	\$6,100

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table 17-1.

Eliminate tax subsidies for agribusinesses

U.S. agribusinesses enjoy preferential tax treatment for three types of business activities related to their everyday operations:

- Capital gains treatment for agricultural items
- Expensing of certain so called multiperiod planting costs
- Expensing of capital outlays for fertilizer and feed

These are special tax subsidies that other industries do not get. Certain portions of their income are taxed at a much lower rate, and they are able to immediately write off many of their costs instead of recouping those costs over a number of years as companies in most other industries must do.

Eliminating these tax subsidies would save taxpayers \$770 million in FY 2012 and \$4.9 billion in total between FY 2012 and FY 2016.

Eliminate tax subsidies for agribusinesses, combined (expensing of ag costs and capital outlays, cap gains)	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$770	\$860	\$940	\$1,090	\$1,250	\$4,910

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table 17-1.

Eliminate the special Blue Cross Blue Shield deduction

Most health insurance companies have to pay income tax on their profits, but certain Blue Cross and Blue Shield providers are an exception to this rule. These health insurance companies benefit from a special deduction that similar health insurance companies do not enjoy, which amounts to a federal subsidy of their operations.

Eliminating this special deduction would save \$680 million in FY 2012 and \$3.1 billion between FY 2012 and FY 2016.

Eliminate the special Blue Cross Blue Shield deduction	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$680	\$590	\$530	\$610	\$710	\$3,120

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table 17-1.

Eliminate timber tax subsidies

Timber companies benefit from a number of special subsidies that are delivered through the tax code. One of these comes in the form of a special tax rate on timber sales. Another is timber companies' ability to immediately write off the costs associated with timber production even though most other companies can only write off similar production costs over a number of years.

The combined effect of these tax breaks is that timber investments can actually be subject to a *negative* tax rate.¹⁵ In other words, the government is simply paying timber businesses.

Eliminating these tax subsidies would save taxpayers \$340 million in FY 2012 and \$1.6 billion in total between FY 2012 and FY 2016.

Eliminate timber tax subsidies, combined (expensing and cap gains)	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$340	\$90	\$370	\$410	\$400	\$1,610

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table 17-1.

Eliminate the special tax break for horse breeders

A special tax break slipped into the 2008 farm bill allows horse breeders to write off their investments (the horses) over three years. A report conducted by the Treasury Department determined that racehorses actually have a much longer useful life.¹⁶ A faster, three-year depreciation schedule represents an unwarranted subsidy for the breeders.

Estimates are not readily available on how much taxpayers would save by eliminating this special subsidy.

Eliminate the foreign earned-income exclusion

A special exclusion in the tax code shields up to \$92,900 of income earned by American citizens living abroad from U.S. taxes. Because expatriates can claim a tax credit against their U.S. tax liability for taxes paid to other countries, the foreign earned-income exclusion is not needed to protect them from “double” taxation by both the United States and the country where they live.

According to the Congressional Research Service, the exclusion is of particular value to expatriates who pay little or no foreign taxes because it can reduce or eliminate their U.S. tax liability.¹⁷ Put simply, the exclusion “subsidizes employers sending their employees overseas.”

Eliminating this tax break would save taxpayers \$5.4 billion in FY 2012 and \$31 billion in total between FY 2012 and FY 2016.

Remove foreign earned income exclusion	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$5,400	\$5,800	\$6,140	\$6,430	\$6,730	\$30,500

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table 17-1.

Eliminate health savings accounts

Health savings accounts are tax-advantaged savings accounts for individuals with high-deductible health plans. Health savings accounts are intended to help users pay for health costs, but they have largely become tax shelters for the wealthy. Individuals may claim a triple tax benefit:

- A deduction for contributions to an HSA before spending anything on health care
- Tax-free accumulation of earnings within the account
- A tax-free withdrawal to pay for health care once it’s provided

Because of their design, health savings accounts are used by “higher-income individuals with the means to pay higher deductibles and the desire to accrue tax-free savings,” according to the Government Accountability Office.¹⁸ HSAs may also draw younger and healthier individuals to high-deductible plans, raising insurance costs for everyone else.

Eliminating this tax break would save taxpayers \$2 billion in FY 2012 and \$11 billion in total between FY 2012 and FY 2016.

Eliminate MSAs/HSAs	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$1,980	\$2,070	\$2,210	\$2,350	\$2,510	\$11,120

Source: OMB, Budget of the United States Government, Fiscal Year 2012, Table 17-1.

Deny the deduction for vacation homes and yachts

As discussed earlier on pages 7–8, the tax code currently allows a tax break for interest paid on mortgages used to buy vacation homes and loans for the purchase of yachts.¹⁹ The deduction that the tax code allows for mortgage interest is intended to promote homeownership, but allowing taxpayers to claim it on both a primary residence and a vacation property or yacht does not, by definition, expand homeownership.

Eliminating this tax break would save taxpayers almost \$1 billion in FY 2012 and \$6.1 billion in total between FY 2012 and FY 2016.²⁰

Deny mortgage int. deduction for vacation homes and yachts	FY 12 cost (\$ millions)	FY 13 cost (\$ millions)	FY 14 cost (\$ millions)	FY 15 cost (\$ millions)	FY 16 cost (\$ millions)	Combined FY 12-16 cost (\$ millions)
	\$986	\$1,107	\$1,230	\$1,333	\$1,437	\$6,092

Source: CBO, Budget Options (2000) and authors' calculations.

Tax extenders

Spending money through the tax code, year after year

The tax expenditures identified so far in this report do not include any of the so-called “tax extenders.” These “extenders” are a group of several dozen special business tax breaks that are habitually renewed by Congress every year. The extenders include tax breaks for a wide array of industries, including ethanol, film-and-television production, restaurants, and auto racing. This assortment of special subsidies comes at a large cost to taxpayers: The most recent one-year extension increased the federal budget deficit by \$55 billion.

Many of these provisions are generous subsidies of questionable merit. Case in point: The “blenders’ credit” for domestic ethanol production will cost taxpayers nearly \$5 billion this year. Yet according to the Government Accountability Office, the investigative arm of Congress, the credit is “largely unneeded today to ensure demand for domestic ethanol production,” which is, of course, what the credit is intended to do.²¹

Federal renewable fuel standards render the tax credit unnecessary and duplicative. Moreover, with fuel standards requiring increased use of ethanol, the credit is projected to become more costly over the next several years. For these reasons, GAO recently identified the ethanol credit as an example of an inefficient redundancy in government.

Because the tax extenders are once again scheduled to expire at the end of FY 2011, their elimination will not reduce deficits in relation to the baseline estimates for the following fiscal years. For this reason—and because the effectiveness of most tax extenders has not been subject to much evaluation—this report does not discuss eliminating specific tax extender provisions in the context of deficit reduction.

Nevertheless, the tax extenders deserve much greater scrutiny before they are renewed by Congress yet again for FY 2012. There is currently no systematic process for reviewing the effectiveness of these tax breaks toward their ostensible

purposes. The provisions are typically bundled together toward the end of each legislative session, inserted into larger legislation, and renewed with little chance for analysis or debate.

Legislation authored by Rep. Lloyd Doggett (D-TX) would require the nonpartisan congressional Joint Committee on Taxation to review each of the extenders in consultation with the Government Accountability Office and then present its findings to Congress. These ongoing studies would evaluate tax extenders on the basis of ten criteria intended to provide Congress with basic information about their purpose and cost-effectiveness. The proposed study, for example, would identify the intended purpose of each tax break and review whether alternative methods of achieving the same purpose would be more cost-effective.

The Doggett provision was approved by the House of Representatives last year but did not secure passage in the Senate. As a result, Congress could be flying blind later this year when it comes time to decide which tax extenders should be renewed and which should be allowed to expire. This is an unfortunate state of affairs at a time when Congress must exercise diligence with every public dollar it spends.

Conclusion

Congress is now deep in debate about how to cut spending in the remaining seven months of FY 2011. Congress also is beginning to consider how to carry those debates into the FY 2012 budget deliberations. Tax expenditures need to be on the table for discussion for both fiscal years. The reason: policymakers simply must examine the more than \$1 trillion in spending now hidden in the tax code. That same kind of deliberative review is needed for tax extenders due to expire at the end of FY 2011.

Going forward, Congress of course must continue to focus on deficit reduction to come to grips with the nation's long-term fiscal and economic strength. Indeed, action now on deficit reduction slated to happen several years out, after our economy is stronger, is warranted. Part of that discussion must be spending cuts, but considerations of spending cuts must include all areas of spending, including an area that is rife with misspent dollars: the tax-code spending called tax expenditures.

Appendix

Potential tax expenditure cuts

Tax expenditure	Estimated savings from tax spending cuts (\$ millions)					
	FY 12	FY13	FY14	FY15	FY16	FY12-16
Business tax expenditure reforms in president's budget						
Eliminate oil & gas tax breaks, combined	\$3,472	\$5,360	\$4,858	\$4,601	\$4,576	\$22,867
Eliminate coal tax breaks, combined	\$136	\$222	\$236	\$249	\$265	\$1,108
Eliminate LIFO and LCM inventory accounting methods	\$9,200	\$16,500	\$17,300	\$17,800	\$11,200	\$72,000
Defer deduction of interest expense related to deferred income	\$2,986	\$5,138	\$5,396	\$5,636	\$5,861	\$25,017
Determine the foreign tax credit on a pooling basis	\$2,655	\$4,568	\$4,798	\$5,011	\$5,211	\$22,243
Tax currently excess returns on intangibles transfers	\$1,204	\$2,038	\$2,114	\$2,212	\$2,280	\$9,848
Limit income shifting via intangible property transfers	\$29	\$63	\$90	\$118	\$148	\$448
Modify the tax rules for dual capacity taxpayers	\$532	\$918	\$974	\$1,031	\$1,085	\$4,540
Individual tax expenditure reforms in president's budget						
Limit itemized deductions for top-bracket taxpayers	\$6,008	\$18,996	\$26,418	\$29,766	\$32,696	\$113,884
End tax subsidies for private equity and hedge fund managers	\$2,274	\$2,123	\$2,154	\$1,927	\$1,608	\$10,086
Other business/government tax expenditures						
Remove exception from passive loss rules for \$25k in rental loss	\$13,110	\$14,830	\$16,730	\$18,880	\$20,200	\$83,750
Eliminate write-offs for corporate meals and entertainment	\$11,127	\$11,654	\$12,267	\$12,940	\$13,586	\$61,574
Replace tax-exempt bonds with direct subsidy bonds at 25% subsidy rate	\$92	\$669	\$1,385	\$2,077	\$2,815	\$7,038
Limit deferral of income from installment sales	\$830	\$1,020	\$1,230	\$1,420	\$1,600	\$6,100
Eliminate tax subsidies for agribusinesses, combined (expensing of ag costs and capital outlays, cap gains)	\$770	\$860	\$940	\$1,090	\$1,250	\$4,910
Eliminate the tax subsidy for private purpose bonds	\$-	\$110	\$662	\$1,433	\$2,205	\$4,410
Eliminate the special Blue Cross Blue Shield deduction	\$680	\$590	\$530	\$610	\$710	\$3,120
Eliminate timber tax subsidies, combined (expensing and cap gains)	\$340	\$90	\$370	\$410	\$400	\$1,610
End extra accelerated depreciation for horse breeders	?	?	?	?	?	?
Other individual tax expenditures						
Remove foreign earned income exclusion	\$5,400	\$5,800	\$6,140	\$6,430	\$6,730	\$30,500
Eliminate MSAs/HSAs	\$1,980	\$2,070	\$2,210	\$2,350	\$2,510	\$11,120
Deny mortgage int. deduction for vacation homes and yachts	\$986	\$1,107	\$1,230	\$1,333	\$1,437	\$6,092
Total	\$63,811					\$502,265

Endnotes

- 1 In fiscal year 2010, nonsecurity discretionary spending totaled \$491 billion, about 14 percent of total government outlays.
- 2 This summation of tax expenditure costs ignores interaction effects between them. However, one analysis of certain tax expenditures finds that their overall cost would appear larger if interaction effects are taken into account. Leonard Burman, Christopher Geissler, and Eric Toder, "How Big Are Total Individual Income Tax Expenditures and Who Benefits from Them?" (Washington: Urban-Brookings Tax Policy Center, 2008). The \$1.025 trillion figure is the sum total of individual and corporate income tax expenditures; it does not include tax expenditures in the payroll or gift/estate tax system, which are substantial.
- 3 The Joint Committee on Taxation prepares a similar list of tax expenditures with cost estimates.
- 4 Joint Committee on Taxation, "Background Information on Tax Expenditure Analysis and Historical Survey of Tax Expenditure Estimates" (2011).
- 5 GAO Analysis of OMB, Analytical Perspectives, Budget of the United States Government, Fiscal Years 1985-2011, adjusted for 2010 dollars.
- 6 The oil and gas industry also benefits from tax breaks that aren't specific to the industry, such as the "LIFO" accounting method and the rules for "dual capacity" taxpayers.
- 7 Richard Caperton and Sima Gandhi, "America's Hidden Power Bill" (Washington: Center for American Progress, 2010), available at <http://www.americanprogress.org/issues/2010/04/pdf/energytaxexpenditures.pdf>. Their report examined federal energy tax expenditures and includes further detail on the ineffectiveness of the percentage depletion tax break.
- 8 CBO estimates that discretionary outlays will total \$1.355 trillion under H.R.1 and \$1.360 trillion under the most recent continuing resolution—a difference of only \$5 billion.
- 9 These tax code provisions are not listed individually as tax expenditures by the Treasury Department or Joint Committee on Taxation; however they are integrally related to "deferral" of overseas profits, which is one of the largest tax expenditures.
- 10 See J. Clifton Fleming, Jr., Robert J. Peroni, and Stephen E. Shay, "Worse than Exemption," *Emory Law Journal* 80 (59) (2009): 116-18.
- 11 *Ibid.*, p. 134.
- 12 In 2009, CBO estimated that eliminating the tax exemption for new private activity bonds would lower deficits by \$0 in FY 2010, \$0.1 billion in 2011, \$0.6 billion in 2012, \$1.3 billion in 2013, and \$2 billion in 2014. We applied these estimates to the FY 2012-16 period with a 5 percent increase to reflect increases in the estimated revenue loss for this tax expenditure over the two time periods (FY 2010-14 and FY 2012-16). See Office of Management and Budget, "Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2012," table 17-1..
- 13 The deduction for business meals and entertainment is not included in official estimates of tax expenditures, and as a result there are relatively few recent analyses of the cost of this deduction. In 1996, Citizens for Tax Justice estimated its fiscal year 1996 cost to be \$5.5 billion. A Joint Committee on Taxation estimate from 2000 of a proposed change in the deduction is also consistent with this. The estimates here extrapolate the Citizens for Tax Justice estimate based on GDP growth from 1996 through 2016 (actual growth and estimated growth per CBO, "Budget and Economic Outlook" (January 2011)).
- 14 CBO estimates that replacing new tax-exempt bond issuances with direct subsidy bonds at a 15 percent subsidy rate would lower the deficit by \$0.4 billion in FY 2012, \$2.9 billion in 2013, \$6.0 billion in 2014, \$9.0 billion in 2015, and \$12.2 billion in 2016. See CBO, "Reducing the Deficit: Spending and Revenue Options" (2011). Our estimate is based on the proportional budget savings with a subsidy rate of 25 percent, assuming that a 28 percent rate is approximately revenue neutral. See Department of the Treasury, "General Explanations of the Administration's Fiscal Year 2012 Revenue Proposals" (2011), p. 21.
- 15 Calvin H. Johnson, "Timber!, Tax Notes" (Austin: University of Texas, 2009), available at http://www.utexas.edu/law/faculty/calvinjohnson/timber_11-16-09-tax-notes.pdf.
- 16 Department of the Treasury, "Report to Congress on the Depreciation of Horses" (1990), available at http://www.treasury.gov/resource-center/tax-policy/Documents/depreci8study_horses.pdf.
- 17 Committee on the Budget, United States Senate, "Tax Expenditures: Compendium of Background Material on Individual Provisions" (2010), pp. 33-35.
- 18 Government Accountability Office, "Consumer-Directed Health Plans, Early Enrollee Experiences with Health Savings Accounts and Eligible Health Plans" (2006), p. 30. See also Government Accountability Office, "Health Savings Accounts: Participation Increased and Was More Common among Individuals with Higher Incomes" (2008); Edwin Park, "GAO Study Again Confirms Health Savings Accounts Primarily Benefit High-Income Individuals" (Washington: Center on Budget and Policy Priorities, 2008), available at <http://www.cbpp.org/cms/index.cfm?fa=view&id=291>.
- 19 Internal Revenue Service, "IRS Publication 936: Home Mortgage Interest Deduction" (2010), p. 2.
- 20 The tax expenditure cost for the mortgage interest deduction for second homes was estimated based on Congressional Budget Office estimates in CBO, "Budget Options" (2000). CBO estimated that limiting the mortgage interest deduction for second homes would result in \$800 million in additional revenues in fiscal year 2005. The total mortgage interest deduction was estimated to cost \$62.2 billion in fiscal year 2005. See Office of Management and Budget, "Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2007" (2006). Therefore, based on best estimates, the second home deduction represented approximately 1.3 percent of the total mortgage interest tax expenditure. We conservatively estimated that the second home deduction will constitute 1 percent of the tax expenditure in future years. The estimates for FY 2012-2016, therefore, are 1 percent of OMB's tax expenditure estimate for the mortgage interest deduction for those years.
- 21 Government Accountability Office, "Opportunities to Reduce Potential Duplication in Government, Save Tax Dollars, and Enhance Revenue" (2011), pp. 59-61.

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