

SUPPLEMENTARY STATEMENT OF JOSEPH W. BARR

TAX EXPENDITURES: GOVERNMENT EXPENDITURES MADE THROUGH THE INCOME TAX SYSTEM

The Annual Report of the Secretary of the Treasury for fiscal year 1968 includes an exhibit which presents Government expenditures for 1968 made through the income tax system (Exhibit 29). The availability of the budget for fiscal year 1970 enables us to present an updating of tax expenditures to cover the fiscal years 1968, 1969, and 1970 on a basis consistent with the 1970 budget data and classifications. The following statement is a condensed and revised version of the exhibit in the Secretary's 1968 Annual Report with the updated figures.

PURPOSE OF ANALYSIS

This analysis extends the budget to include Government expenditures made through the income tax system. The present Federal income tax structure contains a large number of special deductions, credits, exclusions, exemptions, and preferential rates designed to achieve various social and economic objectives. Most of these special provisions serve ends similar in nature to those served by direct Government expenditures or loan programs, and they affect the private economy in the same way. In a specific functional area the Government may have direct expenditures, direct Federal loans, Federal insurance or guarantees of private loans, and interest subsidies which represent alternative methods of accomplishing the purpose which the special tax provision seeks to achieve or encourage. This analysis, together with the fuller presentation in the Secretary's Annual Report, will permit a better understanding of the amount and allocation of resources on both the outlay and revenue side of the 1970 budget.

A tax expenditure has the same impact on the budget surplus or deficit as a direct increase in expenditures. The tax revenues which the Government does not collect because of these special tax provisions, however, are not reported in the budget as presently constituted. The absence of line items—either on the receipts or outlays side of the budget—for these revenue losses thus results in an understatement of the role of Federal Government financial influence on the behavior of individuals and businesses and on income distribution. In many areas the magnitude of tax expenditures approaches and, in some instances, approximates direct outlays having the same objective.

Tax expenditures are not disclosed in the budget and therefore are not subject to careful annual scrutiny in the budget and appropriation process. Budget outlay decisions, on the other hand, involve the departments and agencies, the Bureau of the Budget, the House and Senate program committees which are competent and experienced in their specialized fields, and the appropriation committees. Tax expenditures are not generally considered by the program departments and congressional committees concerned, and are not reviewed annually or periodically to measure the benefits they achieve against the amounts expended.

The purpose of this analysis is to present information which compares tax expenditures with direct expenditures or loan programs in various functional areas and thus to clarify and present more fully the role of the Federal Government in these areas. Such a comparison should be helpful in the allocation of public resources.

A few illustrations will indicate how tax expenditures are alternatives to direct expenditures or Government lending programs. Under the functional category of health and welfare, the budget lists large direct expenditures which benefit the aged. In addition, \$2.3 billion was expended in 1968 through the tax system to aid the elderly.

Direct expenditures for natural resources are itemized in the budget. To these should be added the \$1.6 billion assistance the tax system provides these industries by permitting the expensing of certain capital costs, the use of percentage depletion in excess of cost depletion, and special capital gains treatment for iron ore and coal royalties.

In the field of housing the Government now provides direct subsidies to lower the interest rates on mortgages paid by buyers of certain homes. Homeownership is also subsidized through the tax deductions for interest paid on home mortgages and for property taxes on homes which now cost the Government annually about \$1.9 billion and \$1.8 billion, respectively.