SCHWARTZ CENTER FOR ECONOMIC POLICY ANALYSIS
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Federal Budgeting for Retirement Security:
Tax Expenditures are Entitlements
Focus on Retirement

"From a budgetary perspective, most tax expenditures are comparable to mandatory spending for entitlement programs, in that no further action is required to provide resources for tax expenditures. Tax expenditures do not compete overtly in the annual budget process and, in effect, receive a higher funding priority than discretionary spending subject to the annual appropriations process."

Government Accountability Office, September 2005

Responsible Debt Analysis Requires Scrutiny of Tax Expenditures for Retirement

In the United States, much of our social spending happens through the back door through special provisions in the tax code. Out of the $1 trillion spent on tax expenditures in a year– around 6% of GDP – incentive programs for retirement savings are not scrutinized for effectiveness during the annual budget process.

A long-term plan for fiscal health requires every dollar of spending be effective, efficient, and fair. Tax expenditures for retirement savings are expensive, ineffective, and regressive. They need to be overhauled.

Expensive

- Federal tax expenditures support retirement savings with foregone revenues amounting to over $143 billion each year.

Total Expenditures for Retirement Security, Fiscal Year 2011

Retirement Security	
Defined Benefit Plans	44,630
Self Directed Accounts	99, 231
Total	**143,861**

Source: OMB 2010

- The top four categories in retirement expenditures (employer plans, 401(k), IRA, and Keogh plans) rank within the top 20 expenditure allocations of the budget—above child credits, education credits, and the Earned Income Tax Credit (EITC). The cumulative effect places tax expenditures for retirement second only to employer exclusions for medical care on the rankings of total outlays.

Top 5 Tax Expenditures for Fiscal Year 2011

	Provision	Projected Revenue Effect (millions of dollars)
1	Exclusion of employer contributions for medical insurance premiums and medical care	176,964
2	**Total Retirement Saving Tax Incentives**	143,861
3	Deductibility of mortgage interest on owner-occupied homes	104,540
4	Deductibility of nonbusiness state and local taxes	46,500
5	Step-up basis of capital gains at death	44,520

Source: OMB 2010

Ineffective

- Rather than increasing retirement plan coverage and savings rates, most of these subsidies go to high earners who already have adequate retirement savings and can simply shift savings to tax-favored accounts. (Ghilarducci and Arias, 2009) One study cited in the 2005 GAO report shows that no more than 9% of savings under the IRA tax expenditure are new savings engendered by the program. (GAO, 2005)

Regressive

- Taxpayers in the highest-earning 20% claim nearly 80% of the total benefits of entitlement programs for retirement accounts. More than 40% goes to the top 6% of taxpayers alone.

Distributional Effects of Eliminating Retirement Savings Entitlements

Income Quintile	Share of Total Tax Change (%)
Lowest Quintile	0.0
Second Quintile	1.6
Middle Quintile	5.7
Fourth Quintile	13.1
Top Quintile	79.6

Source: Toder, et. All 2009

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