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Testimony of Maya MacGuineas
Committee for a Responsible Federal Budget
Hearing before the House Ways and Means Subcommittee on Tax Policy:

Post Tax Reform Evaluation of Recently Expired Tax Provisions
March 14, 2018

Chairman Buchanan, Ranking Member Doggett, and Members of the Subcommittee, thank you so much for inviting me here today to discuss the tax extenders. While I am pleased to have the opportunity to discuss this topic, I'm also disappointed we continue to have these discussions. The 2015 PATH Act and the recent tax reform effort were both meant to end the practice of making tax policy one year at a time. That we continue to debate these tax extenders – which we often pass retroactively and almost always without offsets – shows how broken the policymaking process is.

I am Maya MacGuineas, president of the Committee for a Responsible Federal Budget. The Committee for a Responsible Federal Budget is a nonpartisan organization dedicated to educating the public about and working with policymakers on fiscal policy issues. Our co-chairs are Purdue University President and former OMB Director Mitch Daniels, former Secretary of Defense and former OMB Director Leon Panetta, and former Congressman Tim Penny. Our board includes past directors and chairs of the Office of Management and Budget, the Congressional Budget Office, the Federal Reserve System, the Treasury Department, and the Budget Committees. Our partner organization, Fix the Debt, is a nonpartisan coalition that supports a "grand bargain" to help deal with the debt. The group is chaired by Senator Judd Gregg and Governor Ed Rendell.

I will touch on several main points today:

1. Tax extenders are generally poor policy.
2. The 2015 PATH Act was supposed to permanently resolve the tax extenders.
3. The Tax Cuts and Jobs Act made things worse, not better.
4. With the dire fiscal situation, we can't keep debt-financing tax extenders.

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Tax Extenders are Generally Poor Policy

The tax code has well over $1 trillion annually in tax expenditures, which are oftentimes inefficient, ineffective, expensive, regressive, distorting, and pick winners and losers. It was highly disappointing that the recent tax legislation did way too little to eliminate the many tax breaks in the code – which was one of the key goals of tax reform.

Tax extenders tend to be even worse in that they are temporary, and they are particularly problematic when they are extended retroactively.

The temporary nature of tax extenders makes it hard for businesses and individuals to plan and invest. To be sure, there are sometimes legitimate reasons for temporary tax policy – to respond to a natural disaster or economic downturn, to test effectiveness, or to provide transition relief – but most of the tax extenders are temporary simply to hide their budgetary cost. That is an outright gimmick and makes no economic or budgetary sense.

Worse, when extenders are often passed retroactively, they have little or none of their intended effect. The most recent tax extenders package – which included incentives for individuals, businesses, and certain energy interests – was passed in February 2018 but extended 30+ tax breaks for 2017 only. The purpose of targeted tax breaks is often to encourage certain behavior, but incentives can't travel back in time. Retroactive tax extenders don't encourage anything; they only reward decisions already made.

For example, the recent round of tax extenders revived "empowerment zone" tax credits to businesses who invest and hire in distressed urban areas. But the break was expired for all of 2017; it did not exist while businesses were actually making those decisions. The same logic applies to many of the other breaks: extending the expensing rules for film, television, and live theatre through 2017 rewarded those businesses that *already* invested in productions, but it did nothing to encourage future investments. The energy credits work the same way. For instance, the renewable electricity production credit was provided for projects that broke ground in 2017.

Perhaps most importantly from a fiscal perspective, extenders are costly. Congress almost always extends these tax breaks without offsets. Since 2012, Congress has passed four extenders laws that added more than $1 trillion to deficits over their respective ten-year windows including interest. We simply can't afford these tax cuts that have routinely made a poor fiscal situation even worse.

The 2015 PATH Act Was Supposed to Permanently Resolve the Tax Extenders

In 2015, both parties came together to agree on a plan that would permanently deal with all tax extenders. The Protecting Americans from Tax Hikes (PATH) Act of 2015 (and the simultaneous omnibus spending bill) made many tax extenders permanent while putting the rest on a path toward expiration.

Our organization opposed the PATH Act since it ***added over $800 billion to the national debt.*** However, one silver lining was that it was supposed to provide greater certainty in the tax code and end the damaging process of making tax policy a year or two at a time.

Fig. 1: Fate of Tax Provisions in the PATH Act of 2015 & the 2016 Consolidated Appropriations Act

Extended Permanently	5-Year Extensions & Phase-downs	2 Year Extensions/Path to Expiration
Research and development tax credit	50% bonus depreciation, reducing it to 30% by 2019	Tax-free forgiveness of mortgage debt on homes
Increased small business expensing (Section 179)	Rules allowing multinationals to transfer money between overseas subsidiaries without paying tax	Deductions for mortgage insurance premiums and tuition
State and local sales tax deduction	Work Opportunity Tax Credit	Tax credits for renewable fuels, fuel cell vehicles, and two-wheeled electric vehicles
Lower refundability threshold for the Child Tax Credit	New Markets Tax Credit	Empowerment zone tax incentives for distressed urban areas
American Opportunity Tax Credit	Phased-out renewable energy credits and other energy provisions	Special expensing rules for racehorses, motorsports tracks, film/TV/theatre productions
Expanded Earned Income Tax Credit		Credits for mine safety, railroad track maintenance
Rules allowing multinational financial companies to defer tax		Provisions for depreciation on Indian reservations and Indian coal
15-year depreciation schedule for restaurant and retail buildings		Provisions for Puerto Rico, American Samoa, and the Virgin Islands
Other provisions for charity, housing, reservists, etc.		Other provisions (30 in total)
ACA Tax Extenders		
Delay Cadillac tax to 2020, pause health insurance tax for 2017, pause medical device tax for 2016 and 2017		

All parties involved in negotiating the PATH Act agreed that it was supposed to represent a permanent resolution to tax extenders.

- Ways and Means Chairman Kevin Brady described the PATH Act as "ensuring that we will no longer have to spend months each year debating temporary tax extensions."

- Senate Finance Ranking Member Ron Wyden was clear that provisions were on a path to phase out: "At the same time we are phasing out provisions like bonus depreciation which were always designed to be temporary."

- Finance Committee Member Sherrod Brown welcomed the end of repeated extensions: "What this legislation does, in terms of creating breathing room for tax reform, is it breaks the chain of just extending these tax extenders every 2 years."

- And Senate Finance Committee Chairman Orrin Hatch declared the PATH Act would put "an end to the repeated tax extenders exercise that has plagued Congress for decades . . . an almost yearly exercise in relative futility, characterized by partisan bickering as the deadlines approach with short-term extensions enacted at the last minute, leaving no one – certainly not American taxpayers – feeling any better in the end."

Despite these statements, the Bipartisan Budget Act of 2018 revived tax breaks that were intended to expire, renewing this decades-long debacle that was supposed to be resolved.

The Tax Cuts and Jobs Act Made Things Worse, not Better

Tax reform tried to have it all ways regarding tax extenders. First, lawmakers assumed all of the tax extenders that expired in the PATH Act would always continue to justify an additional $500 billion of debt-financed tax cuts as part of tax reform. Then, lawmakers wrote legislation that addressed only one of those tax extenders. Lastly, lawmakers wrote a bill that included many sunsets to make the costs look smaller, while simultaneously claiming they planned to extend the tax breaks. This was an egregious triple gimmick.

Instead of resolving the old tax extenders, the Tax Cuts and Jobs Act created new ones. Under that bill, expanded deductibility of medical costs will end in 2019, tax breaks for paid family leave and alcohol producers will end in 2020, research & experimentation costs will begin to amortize starting after 2021, full expensing of equipment will begin to phase out after 2022, and nearly all changes to the individual tax code and estate tax will end after 2025. At various points over the next decade, the legislation will also tighten rules for interest deductibility, certain international provisions, and operating losses.

If all these changes are continued, it would add up to **$1.1 trillion** more to deficits through 2028. If policymakers also continue the extenders that expired at the end of 2017, those that will expire, and the "Obamacare tax extenders," the total cost could rise to $1.6 trillion. **In other words, we may lose as much revenue from future tax extenders as we did from the tax bill itself.**

Fig. 2: Cost of Potential Tax Policy Extensions Through 2028

Extension Policy	Ten-Year Cost
Continue individual tax provisions after 2025	$550 billion
Stop amortization of research & experimentation (R&E) expenses after 2021	$125 billion
Continue full expensing after 2022	$115 billion
Prevent making foreign tax provisions more strict after 2025	$90 billion
Prevent making business interest deduction more strict after 2021	$90 billion
Continue more generous medical expense deduction after 2018	$50 billion
Continue credit for employers who offer paid leave after 2019	$35 billion
Continue craft beverage tax reforms	$10 billion
Subtotal, extensions of the 2017 tax bill	**$1.1 trillion**
Revive and extend tax provisions that expired in 2017	$90 billion
Continue other tax extenders expiring over the next decade	$70 billion
Continue delays of ACA taxes	$320 billion
Cost of extending all expiring tax policies	**$1.6 trillion**

Source: CRFB calculations based on Joint Committee on Taxation.

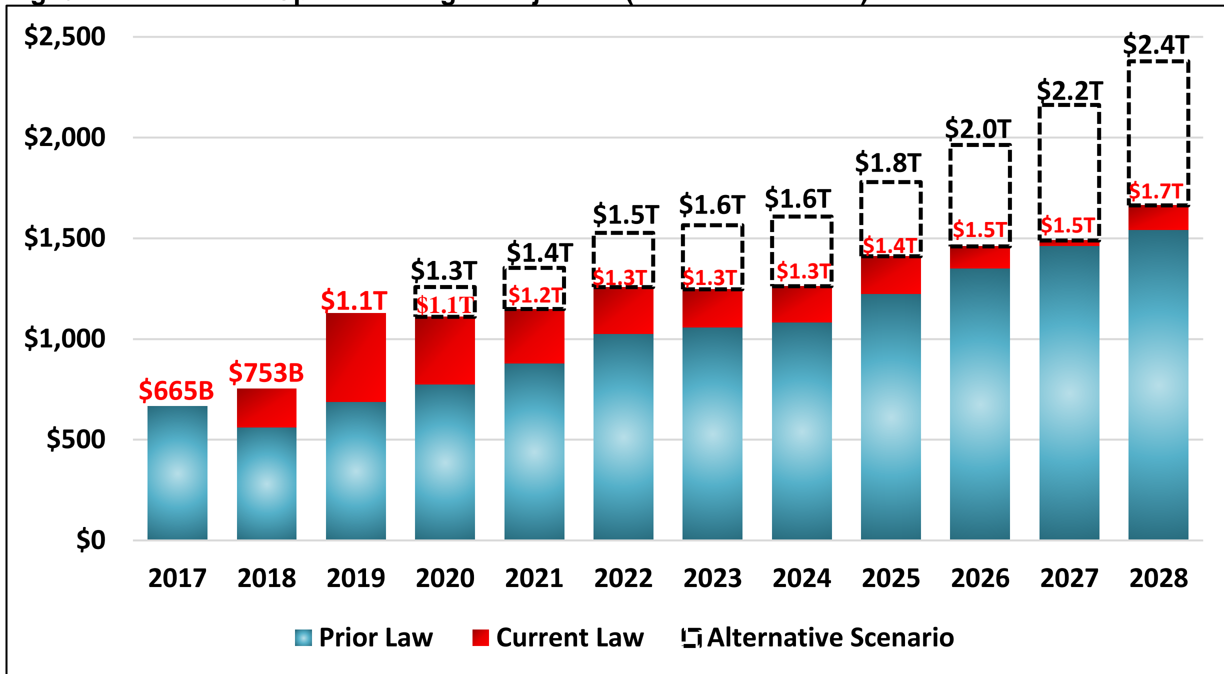
These new expirations worsen the uncertainty from the previous set of tax extenders. Indeed, analyses from across the political spectrum agree expirations in the current tax bill will reduce its growth impact. Giving businesses and individuals some certainty over future tax policy would improve investment decisions and economic outcomes. However, certainty shouldn't come at the cost of adding to the debt.

With the Dire Fiscal Situation, We Can't Keep Debt-Financing Tax Extenders

We cannot afford to keep extending revenue-losing tax policy. Many of the old and new extenders should be allowed to sunset so that they don't add to the debt, and tax policies that are continued must be fully paid for. With our debt at near-record levels, we do not have the fiscal space to keep adding them to the national credit card, and it is even more crucial to pay for policies after the major deficit-increasing legislation enacted in recent months.

Previous Congressional Budget Office (CBO) projections in June 2017 implied that debt would reach 93 percent of Gross Domestic Product (GDP) by 2028. We recently estimated that recent legislation has worsened the debt situation to the point that debt will now exceed the size of the economy within ten years. Trillion-dollar deficits are now expected to return next year rather than in 2022 as CBO last projected, and the deficit will reach a record $1.7 trillion by 2028.

Fig. 3: Deficits in the Updated Budget Projection (Billions of Dollars)

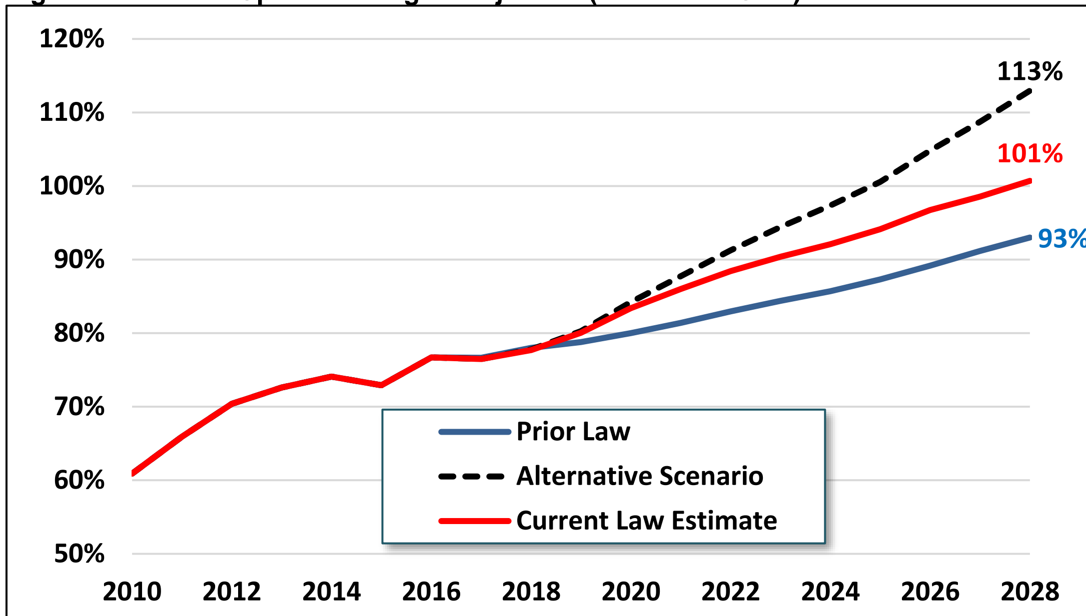


Source: CRFB calculations based on Congressional Budget Office data.

However, even these projections could be optimistic because they assume that lawmakers will allow temporary policies – including the tax extenders, other sunsets in the tax law, and the spending increases from February's budget deal – to expire as scheduled. If these policies were extended permanently without offsets, debt would exceed its all-time record of 106 percent of GDP in 2027 and reach 113 percent ($33 trillion) by 2028, while the deficit would reach $2.4 trillion that year. The 8.2 percent of GDP deficit in 2028 would be the fourth-highest since World War II; the three higher years were in the aftermath of the financial crisis.

Debt would likely continue to grow rapidly beyond 2028 and could be twice the size of the economy in about 25 years.

Fig. 4: Debt in the Updated Budget Projection (Percent of GDP)



Source: CRFB calculations based on Congressional Budget Office data.

An easy start to avoiding this fiscal course is to pay for whichever tax extenders are revived. They are now among the cheapest of the expiring provisions. If you think that reviving tax extenders is important, it should not be difficult to find ways to pay for them.

Economically, a dollar of tax preferences has the same effect as a dollar of spending. Ideally, policymakers should consider both when they have similar goals, an approach known as portfolio budgeting. For example, it would make sense to compare the energy extenders under consideration today along with energy spending programs to see which programs have the largest bang for the buck. I hope the recently appointed Joint Select Committee on Budget and Appropriations Process Reform will help reform our budget process in a way that facilitates such tradeoffs. In the meantime, if lawmakers believe in providing the incentives under consideration, maybe they should consider using some of the $290 billion discretionary spending increase they just approved under in February instead of adding complexity into the tax code.

* * *

Tax extenders were supposed to be dealt with once and for all in the 2015 legislation. We just had a massive tax cut that made an already bad fiscal situation stunningly worse. Support for extending any of these tax breaks without paying for them will cause further fiscal deterioration, and at this point, no Member of Congress should be supporting policy that would make our debt situation worse.

I thank the committee for holding this hearing today and would be delighted to work with you to identify ways to pay for the tax extenders. Thank you.