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CBPP STATEMENT

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PENSION CONFERENCE AGREEMENT SETS UNDESIRABLE PRECEDENT FOR EXTENDING TAX CUTS PERMANENTLY WITHOUT PAYING FOR THEM

Statement by Robert Greenstein
Executive Director, Center on Budget and Policy Priorities

The pension conference agreement announced today includes the permanent extension of provisions enacted in 2001 that expand tax-preferred retirement and education savings accounts. But the conference agreement includes no offsets to pay for the cost of these tax cuts. It uses deficit financing instead.

Robert Greenstein, executive director of the Center on Budget and Policy Priorities, said: "The pension conference agreement marks the first time that tax cuts enacted in 2001 have been made permanent, and it sets an extremely undesirable precedent by failing to pay for their cost. Given the serious long-term fiscal problems the nation faces, this reliance on deficit financing is irresponsible. As the retirement of the baby-boom generation approaches, it is deeply troubling that policymakers keep passing more debt to future generations by extending costly tax cuts without paying for them."

"If this approach of making tax cuts permanent without offsetting their costs is subsequently followed for other expiring tax cuts, it would add as much as $3.3 trillion to deficits and debt over the next decade," Greenstein continued. Former Federal Reserve Chairman Alan Greenspan, among others, has counseled that expiring tax cuts should be extended only if their costs are offset. Indeed, the Administration itself has recently acknowledged that the cost of its tax cuts eventually will need to be offset if the tax cuts are made permanent.

The Joint Committee on Taxation estimates that extending the tax cuts for retirement and education savings would cost $52.6 billion between 2007 and 2016. The largest component of this cost reflects the extension of the higher contribution limits enacted in 2001 for tax-preferred retirement accounts such as 401(k)s and IRAs. The increases in these contribution limits are regressive, benefiting only six percent of U.S. households, primarily those who can afford to sock away large amounts each year.

Furthermore, the increases in the contribution limits are not slated to expire until 2010 — so there is no need to extend them now — and there is no evidence that these provisions are achieving their purported goal of increasing saving. Rather, the increases in the contribution limits primarily encourage high-income households to shift funds they already are saving from taxable investment accounts to tax-preferred retirement accounts in order to take advantage of the tax breaks, without increasing the overall amount that they save.

Conference Agreement Improves the Saver's Credit

The conference agreement also makes permanent the saver's credit, the sole provision in the 2001 law intended to boost retirement saving among low- and moderate-income households. In contrast to the provisions that increase the contribution limits for IRAs and 401(k)s, there is evidence that savings incentives which are targeted on low- and moderate-income households *are* effective. The conference agreement also indexes the income limits in the saver's credit to inflation, thereby addressing a flaw in the credit's original design. The conference agreement does not, however, index the saver's credit contribution limits for inflation, so the value of the maximum allowable contribution will erode over time. In contrast, under the conference agreement, both the income and the contribution limits for savings accounts benefiting higher-income households would be indexed for inflation.

Greenstein noted that "The saver's credit is an important mechanism for encouraging low- and moderate-income families to save for retirement. Indexing the income limits will ensure that the effects of inflation will not restrict access to the saver's credit over time. The conferees should be commended for taking this step to strengthen this savings incentive. Even here, however, offsets should have been included to pay for the cost of the improvements."

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