BROOKINGS ECONOMISTS FIND MAGNITUDE OF GIMMICKS IN NEW TAX LAW REPRESENTS SHARP DEPARTURE FROM THE PAST

The tax legislation being signed into law today squeezes a large array of tax cuts into a $350 billion package by “sunsetting” most of the tax cuts (i.e., scheduling them to expire) after a few years. The 2001 tax cut, as well, made extensive use of sunsets for the same purpose.

Since sunsets are not new to the tax code, this raises a question: is the aggressive use of sunsets in this year’s legislation and in the 2001 tax act a new and dangerous development from the standpoint of fiscal integrity and responsibility, or is it a time-honored practice, even if it represents a dubious way for Congress to do business?

In a new analysis, Brookings Institution economists William Gale and Peter Orszag answer this question. They find that while sunsets have long been part of the tax code, such measures traditionally have involved only relatively minor tax provisions with small costs. The degree to which sunsets are now being used for provisions with large costs represents a sharp departure from the past.

For each year going back to 1996, Gale and Orszag use Congressional Budget Office data to estimate the cost in the tenth year that would result from extending all of the tax provisions slated to expire over the coming decade. They find:

- At no time from 1996 to January 2001 would the cost of extending all of the expiring tax provisions have amounted to more than $22 billion in the tenth year. As a percentage of the Gross Domestic Product, the highest level that the cost in the tenth year reached was 0.14 percent of GDP.

- In dramatic contrast, with enactment of the new legislation, the cost of extending all tax provisions that are now scheduled to expire over the decade ahead is $430 billion in the tenth year (i.e., in fiscal year 2013), or 2.4 percent of GDP.

- To gain a sense of the magnitude of 2.4 percent of GDP, it is triple the size of the Social Security shortfall over the next 75 years, as projected by the Social Security Trustees. The Trustees place the size of the Social Security shortfall at 0.73 percent of GDP over the 75-year period.

Gale and Orszag also find that the cost over the next ten years of extending all of the tax provisions that now have sunsets, including those in the new law, is nearly $2 trillion. They note that this “is roughly as large as the official costs of the 2001, 2002, and 2003 tax cuts combined.”

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