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Asset Funders Network

HOW ASSET DEVELOPMENT POLICIES ALIGN WITH TAX AND BUDGET REFORM

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Political and economic pressure is building for both tax reform and fiscal reform more broadly. Short-run tax and spending pressures from the "fiscal cliff" coupled with concerns over long-term fiscal imbalance will force policymakers to make difficult yet unavoidable choices about national budget priorities, including asset development. Concerns about the fairness of the nation's tax structure will also feature prominently.

The tax system finances more than just the activities of the government. Approximately a quarter to a third of all government subsidies or spending flows through the tax code in what are sometimes called tax expenditures. Many or most of these tax subsidy programs also need repairing, and among the largest of these tax expenditures are those used by individuals to help build their personal financial security and better known as asset development.

Numerous analyses have described the tax system's incentives for asset building as "upside down." Many of the gains from asset-building tax breaks accrue to those with higher incomes and those paying higher tax rates. Exclusions, deductions, and occasional credits generally benefit those with incomes high enough to owe taxes; leave non-itemizers ineligible for many deductions for saving and homeownership; and put homeownership further out of reach of low-income households by boosting house prices.

Upside-down incentives are also unlikely to promote new saving very well because subsidies apply mainly to those more wealthy households who can respond by simply rearranging, rather than adding to, their wealth portfolios. For example, a household with significant equity in a home can more easily take out a second mortgage while simultaneously putting money in its 401(k) account. In the case of homeownership, low-income families often face disincentives to own, as they often do not qualify for homeownership tax subsidies but do qualify for rental subsidies. Some tax subsidies to promote savings for higher education have also had limited impact on investment in education because they also exclude lower-income households.

As the gap widens between the haves and haves-not, there is growing concern about what types of policy changes might make most sense economically. There is tremendous opportunity for more constructive analysis to weigh in both over the near and far term. With enough attention to principles up front, fiscal reform can be a chance not just to balance budgets, but to retool national asset-building programs and put them within reach of those who most need help.

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