AN ANALYSIS OF THE HOUSE GOP TAX PLAN

Leonard E. Burman, James R. Nunns, Benjamin R. Page,

Jeffrey Rohaly, and Joseph Rosenberg*

Abstract

This paper analyzes the House GOP tax reform blueprint, which would significantly reduce marginal tax rates, increase standard deduction amounts, repeal personal exemptions and most itemized deductions, and convert business taxation into a destination-based cash flow consumption tax. Taxes would drop at all income levels in 2017, but the highest-income households would gain the most. Federal revenues would fall by $3.1 trillion over the first decade (static) and $3.0 trillion after accounting for macroeconomic feedback effects. Including added interest costs, the federal debt would rise by at least $3.6 trillion over the first decade and by as much as $9.2 trillion by the end of the second ten years.

*We are grateful to Lily Batchelder, Howard Gleckman, Robert Greenstein, Eric Toder, and Roberton Williams for helpful comments on earlier drafts. Yifan Zhang prepared the draft for publication and Devlan O'Connor edited it. The authors are solely responsible for any errors. The views expressed do not reflect the views of the House GOP or those who kindly reviewed drafts. This is an expanded and updated version of a paper posted on the Tax Policy Center website on September 16, 2016. The findings and conclusions contained within are those of the authors and do not necessarily reflect positions or policies of the Tax Policy Center or its funders.

I. INTRODUCTION

House Speaker Paul Ryan announced on June 24, 2016 the House GOP blueprint for broad income tax reform. The proposal would reduce tax rates, simplify many provisions, and convert the taxation of business income into a destination-based cash-flow consumption tax.[1] Many important details are not specified in the blueprint. We needed to make assumptions about these unspecified details for our analysis (see Appendix A). In addition, Speaker Ryan's staff says the plan will be adjusted if necessary to offset any net revenue loss attributable to the tax provisions including macroeconomic feedback effects and excluding the effect of repealing the taxes enacted as part of the Affordable Care Act.[2]

The Tax Policy Center (TPC) has estimated the revenue cost and the distributional effects of a plan consistent with the House GOP blueprint. We estimate that a plan such as this would reduce federal revenue by $3.1 trillion over the first decade of implementation and by an additional $2.2 trillion in the second decade, before accounting for added interest costs or considering macroeconomic feedback effects.[3] Most of the revenue loss arises from business tax cuts.

TPC, in collaboration with the Penn-Wharton Budget Model (PWBM), also prepared two sets of estimates of the House GOP plan

---

[1] Paul Ryan, *A Better Way: Our Vision for a Confident America*, GOP TAX REFORM TASK FORCE (June 24, 2016), http://abetterway.speaker.gov/_assets/pdf/ABetterWay-Tax-PolicyPaper.pdf [perma.cc/G6B3-YMT3].

[2] That is, the net revenue loss estimated by dynamic scoring could be as great as $0.8 trillion over the first decade and $1.4 trillion over the second. Ryan argues that the revenue loss from the ACA taxes should be offset "by repealing the massive new entitlement program created by Obamacare." *supra* note 1 at 16. It is unclear what the replacement for ACA would be and we did not consider changes in health care outlays—including the refundable premium tax credit—in our analysis.

[3] These estimates account for many microeconomic behavioral responses, such as reduced use of tax preferences and increased capital gains realizations when marginal tax rates on income and capital gains decline. The methodology we follow in preparing these estimates follows the conventional approach used by the Joint Committee on Taxation and the U.S. Department of the Treasury to estimate revenue effects before considering the macroeconomic effects. As noted in the text, we do not model certain potentially large tax avoidance responses because of uncertainty about exactly how the proposal would be implemented.

that take into account macroeconomic feedback effects.[4] Both sets of estimates indicate that the plan would boost GDP in the short run, reducing the revenue cost of the plan. However, longer-run estimates indicate that over time the effect on output would become negative, increasing the revenue cost of the plan. Including macroeconomic feedbacks, the revenue loss falls to $3.0 trillion over the first decade, but rises to $3.4 trillion over the second decade. Including interest costs, the federal debt would increase by $3.6 trillion by 2026 and by $9.2 trillion by 2036. Eventually, rising debt pushes up interest rates, which crowds out private investment and slows growth. By 2036, the PWBM estimates that GDP would be 2.6 percent lower than if the tax cuts had not been enacted. These estimates are sensitive to parameter assumptions and the effects on GDP could be larger or smaller in both the short- and the long-run.

The plan would cut taxes at every income level in 2017, but high-income taxpayers would receive the biggest cuts, both in dollar terms and as a percentage of income. Overall, the plan would cut the average tax bill in 2017 by $1,810, increasing after-tax income by 2.5 percent. Three-quarters of the tax cuts would benefit the top 1 percent of households. The average tax cut for the highest-income 0.1 percent (incomes over $3.7 million in 2015 dollars) would be about $1.3 million, 16.9 percent of after-tax income. Households in the middle fifth of the income distribution would receive an average tax cut of almost $260, or 0.5 percent of after-tax income, while the poorest fifth of households would see their taxes go down an average of about $50, or 0.4 percent of their after-tax income. By 2025, households in some upper-middle income groups would have tax increases (although staff report that the plan will be adjusted so that no income group would experience an overall tax increase). The average tax cut at other income levels would be smaller in 2025, relative to after-tax income, than in 2017.

The plan would reduce the top individual income tax rate to 33 percent from the current 39.6 percent, reduce the corporate rate from 35 to 20 percent, and cap at 25 percent the tax rate on profits of pass-through businesses (such as sole proprietorships and partnerships), which are taxed under the individual income tax. Individuals could

[4] *See* Benjamin R. Page & Kent Smetters, *Dynamic Scoring of Tax Plans,* TAX POLICY CTR., URBAN INST. & BROOKINGS INST. (Sept. 16, 2016), http://www.taxpolicycenter.org/sites/default/files/alfresco/publication-pdfs/2000921-Dynamic-Scoring-of-Tax-Plans.pdf [perma.cc/3ZG2-PLXT] for a description of the macroeconomic models used in TPC's analysis.

deduct half of their capital gains, dividends, and interest, reducing the top effective rate on such income to 16.5 percent.

The plan would increase the standard deduction and child tax credit. It would repeal personal exemptions and all itemized deductions except those for charitable contributions and home mortgage interest. The plan would also eliminate the alternative minimum tax (AMT), estate and gift taxes, and all taxes associated with the Affordable Care Act (ACA).

The corporate income tax would be replaced by a cash-flow consumption tax that would apply to all businesses: investments would be immediately deducted (i.e., expensed) and interest would no longer be deductible. The cash flow tax would be border adjustable, meaning receipts from exports would be excluded and purchases of imports would not be deductible. The plan would move the U.S. tax system to a destination-based system in which all sales to U.S. consumers would be taxable, regardless of their source, and all sales to foreign consumers would be exempt from U.S. tax.

The marginal tax rate cuts would boost incentives to work, save, and invest if interest rates do not change. The plan would reduce the marginal effective tax rate on most new investments, which would increase the incentive for investment in the U.S. and reduce tax distortions in the allocation of capital. In the short run, increased investment would raise labor productivity and U.S. wages by increasing capital per worker. However, increased government borrowing would push up interest rates and crowd out private investment, eventually offsetting the plan's positive effects on private investment unless federal spending was sharply reduced to offset the effect of the tax cuts on the deficit. If the plan is modified to reduce the overall revenue loss, the adverse effects of rising interest rates could moderate or be eliminated. Those unspecified modifications could also, of course, modify economic incentives.

II. MAJOR ELEMENTS OF THE PROPOSAL

A. Individual Income Tax

The House GOP tax plan would consolidate the regular standard deduction, additional standard deductions for age or blindness, and the personal exemption for tax filers into new standard deduction amounts of $12,000 for single filers, $18,000 for head of household filers, and $24,000 for joint filers.

The plan would reduce the number of individual income tax brackets from the current seven brackets to three—12, 25, and 33

percent—cutting the top 39.6 percent rate by 6.6 percentage points (Table 1).

The plan would replace the special rates on capital gains and dividends with a 50 percent deduction, which would also apply to interest income. The top rate on capital gains and dividends would be reduced from 23.8 percent (including the 3.8 percent surtax on net investment income) to 16.5 percent, a decrease of over 30 percent. The top rate on interest income would be reduced from 43.4 percent to 16.5 percent, a decrease of over 60 percent.

TABLE 1

Tax Rates under Current Law and the House GOP Tax Plan

Among tax filers claiming the standard deduction, 2016[a]

Single filers				Childless married couples filing jointly			
Adjusted gross income ($)		Current marginal rate (%)	House GOP plan marginal rate (%)	Adjusted gross income ($)		Current marginal rate (%)	House GOP plan marginal rate (%)
Over	But not over			Over	But not over		
0	10,350[b]	0	0	0	20,700[b]	0	0
10,350	12,000	10	0	20,700	24,000	10	0
12,000	19,625	10	12	24,000	39,250	10	12
19,625	21,275	15	12	39,250	42,550	15	12
21,275	48,000	15	12	42,550	96,000	15	12
48,000	49,650	25	12	96,000	99,300	25	12
49,650	101,500	25	25	99,300	172,600	25	25
101,500	103,150	28	25	172,600	175,900	28	25
103,150	200,500	28	25	175,900	252,150	28	25
200,500	202,150	33	25	252,150	255,450	33	25
202,150	423,700	33	33	255,450	433,750	33	33
423,700	425,350	35	33	433,750	437,050	35	33
425,350	425,400	35	33	437,050	487,650	35	33
425,400	427,050	39.6	33	487,650	490,950	39.6	33
427,050	and over	39.6	33	490,950	and over	39.6	33

Source: Urban-Brookings Tax Policy Center based on the House GOP tax plan and IRS tax brackets.
(a) Tax filers who itemize deductions would not benefit from the House GOP tax plan's increase in the standard deduction and would thus face tax brackets different from those shown in this table.
(b) The lowest tax bracket under current law covers the standard deduction plus personal exemptions: $6,300 + $4,050 for single filers and $12,600 + $8,100 for childless married couples filing jointly. It does not include the additional standard deduction for elderly or blind people (which is consolidated, along with taxpayer pesonal exemptions, into the higher standard deduction of $12,000 for single filers and $24,000 for married couples filing jointly under the House GOP tax plan).

The plan would repeal the deduction for personal exemptions for children and other dependents, which in 2016 is $4,050 and indexed for inflation. In its place, the plan would increase the child tax credit from $1,000 to $1,500 and create a new nonrefundable credit of $500 for other dependents. The child tax credit would phase out beginning at $75,000 of adjusted gross income for single filers (as

under current law) and $150,000 for joint filers (an increase from $110,000 under current law).[5]

The plan would eliminate all itemized deductions except the deductions for mortgage interest and charitable contributions. The plan would, nonetheless, reduce or eliminate tax savings from the remaining deductions for many taxpayers for three reasons. First, eliminating most itemized deductions and increasing the standard deduction would significantly reduce the number of taxpayers who itemize.[6] We estimate that 38 million (84 percent) of the 45 million filers who would otherwise itemize in 2017 would opt for the standard deduction. Nonitemizers obviously do not benefit from itemized deductions. Second, for many who continue itemizing, the fraction of their mortgage interest or charitable contributions that exceeded the standard deduction (that is, reduces taxable income) would decline.[7] Third, many would face lower marginal tax rates, which would reduce the value of any deduction.

[5] The plan does not specify whether these credits would be indexed for inflation (the current child tax credit is not), whether the phase-out ranges for the child tax credit would be indexed for inflation (they are not indexed under current law), or whether the new $500 credit for other dependents would be subject to an income phase out (personal exemptions are phased out at higher income levels under current law). Speaker Ryan's staff did not respond to our request for clarification on these issues. For our analysis we have assumed that neither credit is indexed for inflation, that the new credit for other dependents phases out in the same manner as the child tax credit, and that the phase-out ranges are not indexed for inflation.

[6] For our analysis we have assumed that the plan repeals the limitation on itemized deductions for high-income taxpayers, although Speaker Ryan's staff did not provide clarification on this issue.

[7] The effective subsidy rate for an itemized deduction is the marginal tax rate multiplied by the fraction of the deduction in excess of the standard deduction. Thus, for example, if a taxpayer in the 25 percent tax bracket has $10,000 of mortgage interest, but total itemized deductions exceed the standard deduction by $5,000, the effective subsidy rate is 12.5 percent (5,000/10,000*25 percent). Since the plan eliminates some large itemized deductions, such as the deduction for state and local taxes, and raises the standard deduction, the fraction of itemized deductions in excess of the standard deduction will decline.

The plan would repeal the individual AMT and a number of "special interest" tax provisions, only some of which were explicitly identified and included in our estimates.[8]

B. Estate and Gift Taxes

The House GOP tax plan would eliminate the federal estate, gift and generation-skipping transfer taxes.[9]

Eliminating the estate tax would remove several economic distortions (such as the incentive it creates to spend down asset balances to below the threshold for taxation). However, eliminating the estate tax would also remove the incentive it provides the wealthy to make charitable contributions.[10]

C. Business Taxes

The House GOP tax plan would cut the top corporate tax rate from 35 percent to 20 percent. A top rate of 25 percent would apply to pass-through entities such as sole proprietorships, partnerships and S corporations, which are taxed at individual rates of up to 39.6 percent under current law.[11]

The 8 percentage point differential between the top rate on pass-through business income and wages could create a strong incentive for many wage earners to form a pass-through entity that provides labor services to their current employer instead of taking

[8] Because Speaker Ryan's staff did not respond to our request for clarification on the specific provisions that would be repealed under the plan, our revenue and distributional estimates only include repeal of the "special interest" provisions explicitly identified in the plan description. However, we do show as an addendum to our revenue estimates (Table 2) the revenue effect of repealing the other "special interest" provisions listed in Appendix A.

[9] The plan does not specify whether the basis of inter vivos gifts would continue to carry over from the transferor (carryover basis), or whether the basis of assets transferred at death would continue to be stepped up (stepped-up basis), as under current law, or whether limits would apply to the amount of stepped-up basis with carryover basis applying to the remainder, as under the law in effect in 2010 (when the estate tax was temporarily repealed). For our analysis, we have assumed that carryover basis would continue to apply to inter vivos gifts, and that the 2010 limitation on stepped-up basis would apply.

[10] Repealing the estate tax would also reduce an individual's incentive to make donations during his or her lifetime. Under current law, such donations produce an income tax deduction and reduce the size of the taxable estate, thereby saving both income and estate taxes. Overall, for wealthy individuals the plan would substantially increase the tax price of donating, which would tend to reduce charitable giving. However, the large tax cuts for high-income households discussed later would produce a partially offsetting income or wealth effect because giving tends to rise with income, all else being equal.

[11] Certain income of pass-through entities is also subject to the 3.8 percent rate on net investment income, making the top rate 43.4 percent.

compensation in the form of wages. To stem such tax avoidance, the plan would require pass-through businesses to pay "reasonable compensation" for tax purposes, so that the preferential 25 percent rate would not apply to all income of pass-through owner-operators. The plan does not specify how reasonable compensation would be defined or the rule enforced. Current-law rules are very difficult to enforce, leading to significant tax avoidance; with the much larger rate differential under the House GOP plan avoidance would be much more prevalent.[12] Nevertheless, for purposes of our analysis we have assumed that reasonable compensation would be defined in an enforceable manner and would not permit a shift from reported wages to business income. With imperfect enforcement, the plan would lose substantially more revenue than we estimate.

Both corporations and pass-through businesses would be permitted to expense (i.e., immediately deduct) all investments in equipment, structures, and inventories, rather than having to capitalize and depreciate these purchases over time as current law generally requires. In addition, businesses' net interest expense would no longer be deductible, but any unused net interest expense could be carried forward indefinitely. These rules would transform the corporate income tax and the individual income taxation of the profits of pass-through businesses into a cash-flow tax, treating business income as it would be treated under a consumption tax that allows deductibility of wages.

If all business income were taxed at the same rate, the tax would be equivalent to a subtraction method value-added tax with an offsetting credit—at the same rate—for wages. If the tax rate were set at the top individual income tax rate (33 percent in the proposal) and individual taxes on capital income were eliminated, the proposal would be equivalent to Bradford's X-tax, a progressive variant of a consumption tax.[13] The fact that there are two business tax rates, both

[12] Under current law, for high earners any income earned through a pass-through entity that is not subject to payroll tax can reduce the rate on that income by as much as 3.8 percent. Under the House GOP tax plan, any portion of current wages that could avoid payroll tax would save 2.9 percent, and if not part of "reasonable compensation" another 8 percent (the difference between the 33 percent top ordinary income tax rate and the 25 percent pass-through tax rate), for a total of 10.9 percent. Shifted earnings below the Social Security maximum ($127,200 in 2017) would also avoid the 12.4 percent OASDI tax.

[13] Robert Carroll, Alan D. Viard & Scott Ganz, *The X Tax: The Progressive Consumption Tax America Needs?* AEI (Dec. 2008), http://www.aei.org/wp-content/uploads/2011/10/20081217_No423752TPOg.pdf [perma.cc/DH32-VCHF].

below the top individual income tax rate, create numerous complications, including the incentive for income shifting already discussed.

The proposal includes a "border adjustment," which is intended to make the business income tax apply only to domestically consumed goods and services, regardless of where they are produced. Businesses would be permitted to exclude receipts from exports, and imports would not be deductible. To make the border adjustment completely neutral, taxpayers with negative taxable cash flow—which would include many or most exporters—would receive any negative tax liability as a refund. The refunds could be large. The dual business rate system also would mean that exporters would have a strong incentive to be structured as pass-throughs rather than corporations (since the refunds would be larger at a 25 percent rate than at 20 percent).[14] Importers would be more likely to incorporate than under current law, although the proposal could still penalize corporations relative to pass-throughs because dividends and capital gains would continue to be taxed at the individual level.[15]

If there is no change in the balance of trade, the border adjustment would increase revenues because U.S. imports (which would become taxable) exceed U.S. exports (which would become tax-exempt). Although it appears unlikely that such a border adjustment would be permissible under current international trade law, we have nevertheless included the revenue and distributional effects of them in

[14] Provisions would need to be made to limit the value of deductions for purchases from corporations (which are taxed at 20 percent) by pass-through entities that export their products. This could be extremely complicated. Other countries with border-adjustable tax systems use a credit-invoice VAT, which makes rebating taxes paid much simpler. Exporters simply receive a credit for taxes remitted by their suppliers, which are tracked via tax invoices.

[15] Imports direct to consumers would presumably be taxable, although it is unclear whether they would be taxed at the 20 percent corporate tax rate or the 25 percent pass-through rate.

our estimates.[16] Many analysts have noted that this short-run revenue source—$1.2 trillion over 10 years by our estimate—is effectively a form of borrowing since current trade deficits must eventually be offset by trade surpluses. Moreover, Setser argues that the trade surplus may be artificially inflated due to businesses shifting profits overseas to avoid U.S. tax and that border adjustments might raise substantially less revenue than estimated.[17]

Under the plan, the U.S. would no longer tax repatriated profits from foreign-source income generated from overseas sales. The plan would make up part of this loss of future revenue by imposing a transition tax on the existing unrepatriated earnings of U.S. firms' foreign subsidiaries. Earnings held in cash would be taxed at 8.75 percent and other earnings at 3.5 percent, with the liability for this one-time tax payable over eight years.

Adopting a destination-based tax system and eliminating deductibility of net interest expense would eliminate U.S. corporations' incentives to move their tax residences overseas (i.e., "corporate inversions") and to recharacterize domestic corporate income as foreign-source income. Border adjustability would remove these incentives, because the amount of U.S. income tax a corporation paid would not depend on where it was incorporated, where its product or service was produced, or where its shareholders resided. However,

---

[16] It appears unlikely that a business cash flow tax could be border adjusted under World Trade Organization law. *See* Wei Cui, *Destination-Based Taxation in the House Republican Blueprint*, 173 TAX NOTES TODAY 7 (2016); Wolfgang Schön, *Destination-Based Income Taxation and WTO Law: A Note* (Max Planck Inst. for Tax L. & Pub. Fin., Working Paper No. 03, 2016). Note also the conclusion of the 2005 President's Advisory Panel on Federal Tax Reform: "given the uncertainty over whether border adjustments would be allowable under current trade rules, and the possibility of challenge from our trading partners, the Panel chose not to include any revenue that would be raised through border adjustments". *Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System*, REPORT OF THE PRESIDENT'S ADVISORY PANEL ON FEDERAL TAX REFORM (Nov. 2005), http://www.treasury.gov/resource-center/tax-policy/Documents/Report-Fix-Tax-System-2005.pdf [perma.cc/V6HP-NXPW] at 172.

[17] For example, under current law, U.S. multinationals have an incentive to shift profits to low-taxed foreign subsidiaries by transferring ownership of intangible assets to them at low price, so the subsidiaries earn artificially high profits. Those transfers (which are counted as U.S. exports) would become nontaxable in the U.S. with the border adjustment, so U.S. multinationals could reduce their worldwide tax payments by increasing the value they place on the transfers. U.S. exports would increase, with a corresponding diminution of our balance of trade deficit. Brad Setser, *Dark Matter. Soon to be Revealed?*, COUNCIL ON FOREIGN RELATIONS (Feb. 2, 2017), http://blogs.cfr.org/setser/2017/02/02/dark-matter-soon-to-be-revealed [perma.cc/VXS3-2WCQ].

as noted above, border adjustments are unlikely to be legal under existing trade law. If the plan were adopted without border adjustability and with exemption of sales from foreign production, it would be a territorial tax and would retain incentives for U.S. corporations to shift their profits to low-tax foreign subsidiaries.

The plan would repeal the corporate AMT and a number of "special interest" business tax provisions, only some of which were explicitly identified and included in our estimates.[18]

D. ACA Taxes

The House GOP health plan repeals all ACA taxes, including the 3.8 percent surtax on net investment income, the 0.9 percent additional Medicare rate on high-income workers, excise taxes (for example, the excises on medical devices and high-premium health insurance), premium credits, and related fees. We include the repeal of ACA taxes in our analysis of the House GOP tax plan. Note that the House GOP health plan also proposes a new limit on the tax exclusion for employer-provided health insurance and a new credit for non-group health insurance. We assume that the limit on the tax exclusion has the same revenue and distributional effects as the current excise tax on high-premium health insurance.[19] In addition, we exclude replacement of the ACA premium credit with the proposed non-group health insurance credit because we do not include the ACA premium credit in our current-law tax baseline.[20]

III. IMPACT ON REVENUE AND DISTRIBUTION

A. Impact on Revenue

[18] *See supra* note 8 for a discussion of special interest provisions.

[19] While an exclusion cap is a more direct and potentially more progressive way to reduce the incentive for provision of overly generous health insurance, the Cadillac plan tax is so onerous that most employers would reduce their spending to below the cap and (eventually) pass on the savings to employees. As a result, Blumberg, Holahan, and Mermin (2015) conclude that "the incidence of the ACA's excise tax is identical in most circumstances to a cap on the employer exclusion that would raise the same revenue." Linda J. Blumberg, John Holahan & Gordon Mermin, *The ACA's 'Cadillac' Tax Versus a Cap on the Tax Exclusion of Employer-Based Health Benefits: Is This a Battle Worth Fighting?* URBAN INST. (Oct. 22, 2015), http://www.urban.org/sites/default/files/publication/72391/2000482-the-acas-cadillac-tax-versus-a-cap-on-the-tax-exclusion-of-employer-based-health-benefits.pdf [perma.cc/X3NS-YB8K].

[20] The ACA premium credit is advanceable and refundable, making it more like a spending program than a tax provision. It is unclear what the replacement credit would look like.

We estimate that the House GOP tax plan would reduce federal receipts by $3.1 trillion between 2016 and 2026 before accounting for macroeconomic feedback effects (Table 2).[21] Nearly two-thirds of the revenue loss would come from business tax provisions. Corporations would pay less due because their top rate would be reduced to 20 percent and the corporate AMT would be repealed. Pass-through businesses taxed under the individual income tax would pay less because they would face a 25 percent top rate. All businesses would benefit from expensing of investment, which would be partially offset by the disallowance of interest deductibility, repeal of some tax expenditures, and, for corporations, the border adjustments and transition tax on unrepatriated foreign income.[22]

The remainder of the revenue loss would result primarily from net cuts in nonbusiness individual income taxes. Reductions in income tax rates, the 50 percent exclusion for capital income, and repeal of the ACA taxes and the individual AMT would all reduce revenue. The increased standard deduction amounts, the higher child tax credit, and the new credit for other dependents would also reduce revenue, but these losses would be more than offset by the repeal of personal exemptions and itemized deductions other than those for mortgage interest and charitable contributions.

Repealing the estate and gift taxes and requiring the basis of inherited assets to be carried over (as was done in 2010, when the estate tax was temporarily repealed), would reduce revenues by $187 billion over the budget period.

We also estimate the effect of the tax changes in the second decade (2027–2036) and find the revenue loss ($2.2 trillion) is smaller in nominal terms than that in the first 10 years, and also represents a smaller share of cumulative gross domestic product (GDP)—0.6 percent versus 1.3 percent in 2017–2026.

The House GOP blueprint indicates the plan would repeal "special interest" tax provisions, but explicitly identifies only employee fringe benefits (other than for health and retirement), the domestic production activity deduction, and credits (with several

[21] Although we assume an effective date of January 1, 2017, we estimate a slight revenue loss in 2016 because taxpayers would postpone realizing capital gains in anticipation of the 2017 reduction in capital gains rates.

[22] We report all revenues from the border adjustments as corporate, although some portion would be from pass-through entities.

exceptions).[23] We included only those explicitly identified provisions. However, the Addendum to Table 2 shows our estimates of other tax provisions the plan might repeal.

Aside from the unspecified and uncertain provisions, there are a number of uncertainties associated with the revenue projection. As noted, House GOP staff argue that repealing the ACA taxes should not be considered a revenue loss attributable to tax reform since those will be dealt with in health reform legislation. Subtracting those provisions would reduce the revenue loss by $0.8 trillion in the first decade and $1.4 trillion in the second. On the other side, the border adjustments will eventually lose revenue, and our estimate of the revenue raised by the border adjustments could be too high if the current reported trade deficit is artificially inflated by tax-motivated transfer pricing strategies. Finally, conversion of wages and salaries into pass-through business income to take advantage of the lower tax rates could result in substantial revenue losses. We have not estimated the revenue loss from such shifting in the House GOP plan, but our analysis of the Trump plan, which would have taxed pass-through income at 15 percent (10 percentage points lower than the House plan), estimated that income shifting could ultimately cost more revenue than the direct effect of cutting pass-through tax rates. The direct revenue losses understate the effect on the national debt because they exclude the additional interest that would accrue if debt were to increase. Including interest, the proposal would add $3.7 trillion to the national debt by 2026 and $8.0 trillion by 2036 (Table 3). If the tax cuts were not offset by spending cuts, we estimate the national debt would rise by 13.5 percent of GDP by 2026 and 19.3 percent of GDP by 2036. Taking macroeconomic feedback effects into account, the ratio of additional debt to GDP would be lower after ten years and larger after 20 years, rising to at least 13.2 percent by 2026 and to 22.7 percent by 2036. The PWBM model estimates that after 2036, revenues and GDP fall below the levels estimated without macro feedback by increasing amounts, so the ratio of debt to GDP would climb more rapidly in later years.

[23] The credits identified (directly or by implication) in the House GOP blueprint document as retained are the child tax credit, the EITC, education credits, the savers' credit, the research and experimentation credit, and the foreign tax credit; all other credits would presumably be repealed.

TABLE 2

Estimated Effect of House GOP Tax Plan on Tax Receipts

$ billions, FY 2016–36

Provision	Fiscal Year							
	2016	2017	2018	2019	2020	2021	2016–26	2027–36
Individual income and payroll taxes								
Repeal ACA taxes	-5.6	-23.1	-57.0	-72.2	-78.5	-82.4	-803.1	-1,430.0
Repeal alternative minimum tax	0.0	-25.0	-34.7	-37.2	-40.1	-42.9	-427.3	-723.7
Individual income tax rates of 12, 25, and 33 percent	0.0	-92.6	-129.2	-135.9	-143.1	-149.8	-1,542.9	-2,620.4
Repeal itemized deductions (other than charitable and mortgage interest) and Pease	0.0	106.6	150.3	161.8	174.8	187.3	1,907.6	3,342.0
Increase standard deduction to $24,000/$18,000/$12,000	0.0	-93.5	-126.7	-128.9	-131.6	-135.9	-1,361.0	-1,911.1
50 percent inclusion rate for capital income	-5.2	-22.8	-34.4	-44.2	-48.3	-50.6	-497.8	-848.6
Top rate of 25 percent on active business income	0.0	-22.7	-32.3	-34.8	-37.5	-39.2	-412.8	-709.5
Repeal personal exemptions for taxpayer and dependents	0.0	108.8	148.3	153.2	158.6	165.3	1,653.6	2,427.9
Additional nonrefundable credit of $500 per dependent; increase CTC phaseout for MFJ	0.0	-25.3	-33.9	-33.8	-33.7	-33.6	-325.5	-312.6
Repeal child and dependent care and elderly credits	0.0	2.7	3.6	3.7	3.8	3.9	38.9	48.8
Expense all investment; disallow deduction for net interest expense on new loans	0.0	-93.6	-113.7	-99.0	-86.8	-71.9	-637.5	487.6
Repeal individual tax expenditures explicitly identified in House GOP plan	0.0	25.2	35.5	37.2	38.1	39.0	385.2	515.7
Total for individual income and payroll tax revenue	**-10.8**	**-155.3**	**-224.1**	**-230.2**	**-224.4**	**-210.7**	**-2,022.8**	**-1,733.9**
Corporate income tax								
Reduce corporate rate to 20% and repeal the corporate AMT	0.0	-80.7	-163.6	-183.4	-194.0	-192.7	-1,844.9	-2,751.5
Expense all investment; disallow deduction for net interest expense on new loans	0.0	-70.0	-120.3	-103.4	-86.1	-66.5	-447.5	636.4
Territorial system of taxing foreign-source income earned after 12-31-16	0.0	-3.6	-7.3	-8.4	-8.7	-9.0	-87.9	-139.2
Deemed repatriation of pre-2017 profits of CFCs; taxed at reduced rates; paid over 8 years	0.0	7.8	15.6	17.3	17.3	17.3	138.3	0.0
Border adjustments (export receipts excludable; purchases of imports not deductible)	0.0	49.9	101.4	115.5	118.9	122.4	1,179.6	1,689.3
Repeal corporate tax expenditures explicitly identified in House GOP plan	0.0	5.0	10.6	13.2	14.8	16.5	171.7	372.5
Total for corporate income tax revenues	**0.0**	**-91.7**	**-163.6**	**-149.1**	**-137.8**	**-112.0**	**-890.7**	**-192.5**
Estate and gift taxes								
Repeal the estate, gift and GST taxes; carryover basis for gains	0.0	0.4	-13.2	-20.1	-21.3	-21.4	-187.4	-299.2
Total for estate and gift tax revenues	**0.0**	**0.4**	**-13.2**	**-20.1**	**-21.3**	**-21.4**	**-187.4**	**-299.2**
Total revenue effect of all provisions								
Total revenue change before macro feedback (sum of amounts above)	**-10.8**	**-246.6**	**-401.0**	**-399.5**	**-383.6**	**-344.1**	**-3,100.9**	**-2,225.6**
Total revenue change after macro feedback (dynamic score)								
TPC Keynesian model estimates	**-10.8**	**-203.6**	**-372.5**	**-387.4**	**-376.6**	**-342.6**	**-3,008.8**	**-2,225.6**
PWBM overlapping generations model estimates	**-10.8**	**-197.0**	**-367.4**	**-381.4**	**-370.1**	**-336.7**	**-3,036.9**	**-3,371.7**
Exhibit: Difference in total revenue change due to macro feedback								
TPC Keynesian model estimates	0.0	43.0	28.5	12.1	7.0	1.5	92.1	0.0
PWBM overlapping generations model estimates	0.0	49.6	33.6	18.1	13.5	7.4	64.0	-1,146.1
ADDENDUM: Tax expenditures possibly included but not explicitly identified in the House GOP tax plan								
Individual income tax and payroll tax expenditures	0.0	30.1	51.9	54.5	56.9	59.7	602.8	1,053.0
Corporate income tax expenditures	0.0	8.4	17.1	19.6	20.1	20.7	198.9	286.1

Sources: Urban-Brookings Tax Policy Center (TPC) Microsimulation Model (version 0516-1); TPC off-model estimates; TPC Keynesian model; Penn-Wharton Budget Model (PWBM) overlapping generations model.
Note: AMT = alternative minimum tax; CFC = controlled foreign corporation; CTC = child tax credit; GDP = gross domestic product; GST = generation skipping transfer; MFJ = married filing jointly.

TABLE 3

Effect of House GOP Tax Plan on Federal Revenues, Deficits, and the Debt
FY 2016–36

TPC

	Fiscal Year												
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2016–26	2027–36
Estimates before macro feedback													
Revenue loss[a] ($ billions)	10.8	246.6	401.0	399.5	383.6	344.1	301.1	272.4	253.9	245.2	242.7	3,100.9	2,225.6
As a percentage of GDP (%)	0.1	1.3	2.0	1.9	1.8	1.5	1.3	1.1	1.0	0.9	0.9	1.3	0.6
Additional interest ($ billions)	0.0	2.9	10.9	27.8	43.1	58.5	72.5	86.0	99.0	111.9	125.0	637.6	2,040.4
Increase in deficit ($ billions)	10.9	249.5	411.9	427.3	426.7	402.6	373.6	358.3	352.9	357.1	367.7	3,738.6	4,266.0
Increase in debt[b] ($ billions)	10.9	260.4	672.3	1,099.7	1,526.3	1,929.0	2,302.5	2,660.9	3,013.8	3,370.9	3,738.6	3,738.6	8,004.5
Cumulative increase in debt relative to GDP (%)	**0.1**	**1.3**	**3.3**	**5.3**	**7.0**	**8.5**	**9.8**	**10.9**	**11.8**	**12.7**	**13.5**	**13.5**	**19.3**
Addendum: GDP (end of period: $ billions)	18,493.8	19,296.5	20,127.1	20,906.0	21,709.7	22,593.2	23,527.5	24,497.2	25,505.6	26,559.2	27,660.0	27,660.0	41,511.7
Estimates after macro feedback from TPC Keynesian model													
Revenue loss[a] ($ billions)	10.8	203.6	372.5	387.4	376.6	342.6	301.1	272.4	253.9	245.2	242.7	3,008.8	2,225.6
As a percentage of GDP (%)	0.1	1.0	1.8	1.8	1.7	1.5	1.3	1.1	1.0	0.9	0.9	1.3	0.6
Additional interest ($ billions)	0.0	3.0	11.1	27.2	41.7	55.7	69.0	82.3	95.2	107.9	120.8	614.1	1,991.2
Increase in deficit ($ billions)	10.9	206.7	383.6	414.6	418.3	398.3	370.1	354.7	349.1	353.1	363.6	3,622.9	4,216.8
Increase in debt[b] ($ billions)	10.9	217.5	601.1	1,015.7	1,434.0	1,832.3	2,202.4	2,557.1	2,906.2	3,259.4	3,622.9	3,622.9	7,839.7
Cumulative increase in debt relative to GDP (%)	**0.1**	**1.1**	**3.0**	**4.8**	**6.6**	**8.1**	**9.4**	**10.4**	**11.4**	**12.3**	**13.1**	**13.1**	**18.9**
Addendum: GDP (end of period: $ billions)	18,493.8	19,497.2	20,260.3	20,962.7	21,742.2	22,600.2	23,527.5	24,497.2	25,505.6	26,559.2	27,660.0	27,660.0	41,511.7
Estimates after macro feedback from PWBM overlapping generations model													
Revenue loss[a] ($ billions)	10.8	197.0	367.4	381.4	370.1	336.7	299.6	276.0	265.4	263.1	269.3	3,036.9	3,371.7
As a percentage of GDP (%)	0.1	1.0	1.8	1.8	1.7	1.5	1.3	1.1	1.0	1.0	1.0	1.3	1.0
Additional interest ($ billions)	0.0	2.4	9.3	24.9	39.5	54.2	67.9	81.2	94.2	107.5	121.1	602.3	2,152.0
Increase in deficit ($ billions)	10.9	199.4	376.8	406.3	409.6	390.9	367.5	357.2	359.7	370.6	390.4	3,639.2	5,523.7
Increase in debt[b] ($ billions)	10.9	210.2	587.0	993.4	1,402.9	1,793.9	2,161.4	2,518.6	2,878.3	3,248.8	3,639.2	3,639.2	9,162.9
Cumulative increase in debt relative to GDP (%)	**0.1**	**1.1**	**2.9**	**4.7**	**6.4**	**7.9**	**9.2**	**10.3**	**11.3**	**12.3**	**13.2**	**13.2**	**22.7**
Addendum: GDP (end of period: $ billions)	18,493.8	19,461.1	20,284.1	21,018.7	21,790.1	22,639.1	23,540.3	24,476.4	25,451.4	26,467.5	27,526.9	27,526.9	40,425.1

Source: Urban-Brookings Tax Policy Center (TPC) Microsimulation Model (version 0516-1); Congressional Budget Office; TPC Keynesian model; Penn-Wharton Budget Model (PWBM) overlapping generations model.

(a) Revenue loss is expressed as the effect on the deficit.

(b) Increase in debt equals the cumulative increase in deficit plus additional interest on the debt. Amounts shown for 2016-26 and 2027-36 are as of the end of those periods.

B. Impact on Distribution[24]

The House GOP tax plan would reduce taxes throughout the income distribution in 2017.[25]

[24] This distributional analysis is based on the Urban-Brookings Tax Policy Center Microsimulation Model. For a brief description of the model, *see Brief Description of the Tax Model*, TAX POLICY CTR. (Dec. 21, 2015), http://www.taxpolicycenter.org/taxtopics/Brief-Description-of-the-Model-2015.cfm. [perma.cc/4ABR-E74Q].

[25] Appendix B discusses alternative distribution measures and illustrates several alternatives for the House GOP tax plan.

Taxes would decrease by an average of $1,810, or 2.5 percent of after-tax income (Table 4). On average, households at all income levels would receive tax cuts, but the highest-income households would receive the largest cuts, both in dollars and as a percentage of income. The top quintile—or top fifth of the distribution—would receive an average tax cut of about $11,800 (4.6 percent of after-tax income). Three-quarters of total tax cuts would go to the top 1 percent, who would receive an average cut of nearly $213,000, or 13.4 percent of after-tax income. The top 0.1 percent would receive an average tax cut of about $1.3 million (16.9 percent of after-tax income). In contrast, the average tax cut for the lowest-income households would be just $50, 0.4 percent of after-tax income. Middle-income households would receive an average tax cut of $260, about the same relative to after-tax income—0.5 percent—as for the lowest-income households.

TABLE 4

Distribution of Federal Tax Change

By expanded cash income percentile, 2017[a]

Expanded cash income percentile[b,c]	Percent change in after-tax income (%) [d]	Share of total federal tax change (%)	Average federal tax change ($)	Average Federal Tax Rate[e]	
				Change (% points)	Under the proposal (%)
Lowest quintile	0.4	0.8	-50	-0.4	3.4
Second quintile	0.4	1.4	-120	-0.3	8.1
Middle quintile	0.5	2.8	-260	-0.4	13.2
Fourth quintile	0.5	3.7	-410	-0.4	17.0
Top quintile	4.6	89.0	-11,760	-3.4	22.7
All	2.5	100.0	-1,810	-2.0	18.0
Addendum					
80–90	0.2	1.2	-310	-0.2	20.0
90–95	0.2	0.7	-370	-0.2	22.0
95–99	2.5	11.0	-7,690	-1.9	23.6
Top 1 percent	13.4	76.1	-212,660	-8.9	24.5
Top 0.1 percent	16.9	46.5	-1,262,530	-11.1	23.4

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0516-1).

Notes: Number of Alternative Minimum Tax (AMT) taxpayers (millions): Baseline: 4.8; Proposal: 0.

(a) Calendar year. Baseline is current law. Proposal includes individual, payroll, corporate, excise, and estate provisions in the House GOP tax plan. http://www.taxpolicycenter.org/taxtopics/Baseline-Definitions.cfm

(b) The percentile includes both filing and non-filing units but excludes those that are dependents of other tax units. Tax units with negative adjusted gross income are excluded from their respective income class but are included in the totals. For a description of expanded cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm

(c) The income percentile classes used in this table are based on the income distribution for the entire population and contain an equal number of people, not tax units. The breaks are (in 2016 dollars): 20% $24,800; 40% $48,400; 60% $83,300; 80% $143,100; 90% $208,800; 95% $292,100; 99% $699,000; 99.9% $3,749,600.

(d) After-tax income is expanded cash income less: individual income tax net of refundable credits; corporate income tax; payroll taxes (Social Security and Medicare); estate tax; and excise taxes.

(e) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, the estate tax, and excise taxes) as a percentage of average expanded cash income.

As with the revenue estimates, there are several sources of uncertainty associated with the distributional estimates. In the short-run, the burden of the net revenue raised by the border adjustments depends on how prices adjust. If exchange rates fully adjust to offset the border adjustments, then domestic prices would remain unchanged and the net revenue should be distributed similar to a cash flow tax that does not burden wage income. However, if exchange rates do not fully adjust, then domestic prices would rise, resulting in a burden more similar to that of a broad-based consumption tax.[26] An alternative approach would attribute zero burden to the border adjustments under the view that current trade deficits are temporary and will eventually be offset (with interest) by trade surpluses in the future. Additionally, the plan is unclear on many details of the business tax changes, and our methodologies differ for distributing changes in existing income taxes and consumption-based taxes. Our analysis distributes the changes in business taxes as incremental changes to the income tax according to our established methodology,[27] but this approach does not yield the same result as if the cash flow tax was distributed as a replacement for the current income tax on business income.[28]

In order to illustrate the uncertainty concerning the short-run effects of the plan across the income distribution, we report the percent change in after-tax income in 2017 under alternative assumptions about the size of the changes in tax burdens due to the business tax provisions and the border adjustments, and how those burdens are distributed (Table 5). Overall, under the alternative assumptions the

[26] Eric Toder, Jim Nunns & Joseph Rosenberg, *Methodology for Distributing a VAT*, TAX POLICY CTR. (Apr. 2011), http://www.taxpolicycenter.org/sites/default/files/alfresco/publication-pdfs/1001533-Methodology-for-Distributing-a-VAT.PDF [perma.cc/89GU-JK3D]

[27] Jim Nunns, *How TPC Distributes the Corporate Income*, TAX POLICY CTR., URBAN INST. & BROOKINGS INST. (Sept. 13, 2012), http://www.taxpolicycenter.org/publications/how-tpc-distributes-corporate-income-tax/full [perma.cc/V2XX-VD8D]

[28] Further, by convention, TPC's distributional analyses do not include short-run wealth effects. In particular, if exchange rates adjust to offset the effect of the border adjustments on international trade, the appreciation of the dollar would reduce the value of Americans' foreign asset holdings. This reduction in the value of existing (foreign) assets, which would primarily affect high-income households, is not included in the distribution tables. In addition, replacing the corporate income tax with a cash flow consumption tax could reduce the value of old capital—another transitory effect; however, we assume that transition rules (allowing existing asset holders to continue to deduct unused depreciation and interest on outstanding loans) would largely offset this wealth effect. We are reexamining our distributional assumptions and may revise our analysis in a future report.

plan would increase after-tax income in 2017 by between 1.7 and 3.4 percent. Households in the bottom four quintiles would see their after-tax income rise by as much as 1.4 percent. Households in the 80th to 95th percentiles would fare the worst. Higher-income households would receive the largest tax cuts. The top 1 percent would see after-tax incomes rise by between 8.0 and 14.1 percent, while the richest top 0.1 percent would receive tax cuts equal to between 10.0 and 17.4 percent of after-tax income.

In the longer-run, the burden of the border adjustments would not depend on which prices adjust and the distribution of tax changes would be similar to the full exchange rate adjustment scenario. Although, by 2025, the average tax cut would be smaller and households in the 80th to 95th percentiles on average would have tax increases rather than cuts. (Speaker Ryan's staff have told us that the

TABLE 5

Distribution of Federal Tax Change

By expanded cash income percentile, 2017[a]

TPC

Expanded cash income percentile[b,c]	Percent change in after-tax income (%) [d]				
	Business tax changes distributed as incremental income tax reforms			Business tax changes distributed as consumption tax replacement	
	No exchange rate adjustment	Full exchange rate adjustment	No burden from border adjustments	No exchange rate adjustment	Full exchange rate adjustment
Lowest quintile	0.4	1.0	1.2	0.2	0.9
Second quintile	0.4	1.0	1.2	0.1	0.7
Middle quintile	0.5	1.1	1.4	0.2	0.8
Fourth quintile	0.5	1.0	1.4	0.1	0.6
Top quintile	4.6	4.0	5.5	3.3	2.7
All	2.5	2.5	3.4	1.7	1.7
Addendum					
80–90	0.2	0.7	1.2	-0.3	0.2
90–95	0.2	0.5	1.1	-0.5	-0.2
95–99	2.5	2.4	3.4	1.4	1.4
Top 1 percent	13.4	10.8	14.1	10.7	8.0
Top 0.1 percent	16.9	13.1	17.4	13.8	10.0

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0516-1).

Notes: Number of Alternative Minimum Tax (AMT) taxpayers (millions): Baseline: 4.8; Proposal: 0.

(a) Calendar year. Baseline is current law. Proposal includes individual, payroll, corporate, excise, and estate provisions in the House GOP tax plan. http://www.taxpolicycenter.org/taxtopics/Baseline-Definitions.cfm

(b) The percentile includes both filing and non-filing units but excludes those that are dependents of other tax units. Tax units with negative adjusted gross income are excluded from their respective income class but are included in the totals. For a description of expanded cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm

(c) The income percentile classes used in this table are based on the income distribution for the entire population and contain an equal number of people, not tax units. The breaks are (in 2016 dollars): 20% $24,800; 40% $48,400; 60% $83,300; 80% $143,100; 90% $208,800; 95% $292,100; 99% $699,000; 99.9% $3,749,600.

(d) After-tax income is expanded cash income less: individual income tax net of refundable credits; corporate income tax; payroll taxes (Social Security and Medicare); estate tax; and excise taxes.

ultimate proposal will not raise taxes on any income group so presumably the plan will be revised to meet this objective.)

IV. DYNAMIC EFFECTS ON THE ECONOMY

In addition to conventional estimates, which are based on fixed macroeconomic assumptions, TPC also prepared, in collaboration with the Penn Wharton Budget Model (PWBM), a set of estimates of the House GOP plan that take into account macroeconomic feedback effects. Estimates of the impacts of tax changes on the economy are subject to considerable uncertainty and can vary widely depending on the models and assumptions chosen. We present "dynamic" estimates from two models to illustrate different ways that tax policy can influence the economy. Estimates using the TPC Keynesian model illustrate how the plan's impact on aggregate demand would influence the economy in the short run—that is, over the next few years. Estimates using the PWBM illustrate the longer-run impact of the plan on potential output through its effects on incentives to work, save, and invest, and on the budget deficit. TPC also plans to build a neoclassical model of potential output whose results could be integrated with those of the Keynesian model, but that work is still in process.

TABLE 6
Dynamic Effects of House GOP Tax Plan on GDP
FY 2016–36

	Fiscal Year												
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2016–26[a]	2027–36[a]
	GDP ($ billions)												
Before macro feedback	18,493.8	19,296.5	20,127.1	20,906.0	21,709.7	22,593.2	23,527.5	24,497.2	25,505.6	26,559.2	27,660.0	27,660.0	41,511.7
After macro feedback													
TPC Keynesian model	18,493.8	19,497.2	20,260.3	20,962.7	21,742.2	22,600.2	23,527.5	24,497.2	25,505.6	26,559.2	27,660.0	27,660.0	41,511.7
PWBM overlapping generations model	18,493.8	19,461.1	20,284.1	21,018.7	21,790.1	22,639.1	23,540.3	24,476.4	25,451.4	26,467.5	27,526.9	27,526.9	40,425.1
	Exhibit: Percentage change in GDP due to macro feedback (%)												
TPC Keynesian model	0.0	1.0	0.7	0.3	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
PWBM overlapping generations model	0.0	0.9	0.8	0.5	0.4	0.2	0.1	-0.1	-0.2	-0.3	-0.5	-0.5	-2.6

Source: Congressional Budget Office; TPC Keynesian model; Penn-Wharton Budget Model (PWBM) overlapping generations model.
(a) End of period.

A. Impact on Aggregate Demand

The House GOP tax plan would increase aggregate demand, and therefore output, in two main ways. First, by reducing average tax rates for most households, the plan would increase after-tax incomes. Households would spend some of that additional income, increasing demand. This effect would be attenuated to some degree because most tax reductions would accrue to high-income households, which are likely to increase spending proportionately less than would lower-income households in response to increased after-tax income. Second, the provision allowing businesses to expense investment would create

an incentive for businesses to raise investment spending, further increasing demand. These effects on aggregate demand would raise output relative to its potential level for the next few years, until actions by the Federal Reserve and equilibrating forces in the economy returned output to its long-run potential level.

Using the TPC Keynesian model, we estimate that these factors would boost output by about 1.0 percent in 2017, by 0.7 percent in 2018, and by smaller amounts in later years (Table 6). Using a range of assumptions about the response of household spending to changes in income, the response of investment to the expensing provision, and the impact of increased demand on output, TPC estimates that the impact on output could be between 0.2 and 2.3 percent in 2017, 0.1 and 1.5 percent in 2018, and smaller amounts in later years.

Those increases in output would boost incomes, which in turn would raise tax revenue, offsetting some of the revenue losses from the tax plan. TPC estimates that the plan's effects on demand would, in themselves, boost revenues by $43 billion in 2017 (or between $12 billion and $129 billion in calendar year 2017 using TPCs full range of estimates), by $29 billion (or between $4 and $42 billion) in 2018, and by smaller amounts in later years. The revenue effect of the House GOP plan, taking into account the dynamic revenue gains based on the TPC Keynesian model using standard parameters, is shown in Table 2.

B. Impact on Potential Output

In addition to short-run effects on aggregate demand, the House GOP tax plan would have a lasting effect on potential output—altering incentives to work, save, and invest—as well as on the budget deficit. Those lasting effects, described below, were estimated using the PWBM.

C. Impact on Saving and Investment

The House GOP tax plan would alter incentives to save and invest in the United States. Large reductions in the tax rates on corporate and pass-through business income, lower effective marginal tax rates on long-term capital gains and qualified dividends for most taxpayers with such income, and much lower rates on interest income throughout the income distribution would all increase the after-tax return to savers (Table 7). Assuming that interest rates do not change and that the tax cuts are not eventually financed in ways that reduce

incentives to save and invest, these effects, in themselves, would tend to increase saving and investment in the U.S. economy.

TABLE 7

Effective Marginal Individual Income Tax Rates on Capital Income

In percent, 2017[a]

TPC

Expanded cash income percentile[b,c]	Tax units (thousands)	Long-term capital gains			Qualified dividends			Interest income		
		Current law	House GOP Tax Plan	Change (percentage points)	Current law	House GOP Tax Plan	Change (percentage points)	Current law	House GOP Tax Plan	Change (percentage points)
Lowest quintile	48,340	0.7	2.0	1.3	0.3	1.1	0.8	1.7	0.9	-0.8
Second quintile	38,630	0.8	3.5	2.7	0.8	3.2	2.4	6.5	3.3	-3.2
Middle quintile	33,880	6.9	7.3	0.4	7.2	6.8	-0.4	17.7	7.7	-9.9
Fourth quintile	28,660	10.6	10.2	-0.4	10.7	10.5	-0.2	22.3	10.1	-12.1
Top quintile	23,960	23.2	15.7	-7.6	22.2	15.1	-7.1	34.1	14.6	-19.5
All	174,680	21.6	14.8	-6.7	19.2	13.6	-5.6	26.8	11.8	-15.0
Addendum										
80–90	12,390	14.3	11.4	-2.9	14.6	11.6	-3.0	25.0	11.8	-13.3
90–95	5,910	16.8	12.7	-4.1	16.7	12.6	-4.1	28.3	12.6	-15.7
95–99	4,530	22.9	14.5	-8.4	22.6	14.2	-8.5	35.0	14.5	-20.5
Top 1 percent	1,130	24.1	16.2	-8.0	24.0	16.1	-7.9	36.5	15.5	-21.0
Top 0.1 percent	120	24.1	16.3	-7.9	24.0	16.2	-7.8	35.4	15.4	-20.0

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0516-1).

(a) Projections are for calendar year 2017. Effective marginal tax rates are weighted by the appropriate income source.

(b) Includes both filing and non-filing units but excludes those that are dependents of other tax units. Tax units with negative adjusted gross income are excluded from their respective income class but are included in the totals. For a description of expanded cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm

(c) The income percentile classes used in this table are based on the income distribution for the entire population and contain an equal number of people, not tax units. The breaks are (in 2016 dollars): 20% $24,800; 40% $48,400; 60% $83,300; 80% $143,100; 90% $208,800; 95% $292,100; 99% $699,000; 99.9% $3,749,600.

The overall effect of taxes on incentives to save and invest can be summarized in the proposal's effect on marginal effective tax rates (METRs) on new investments.[29] METR is a forward-looking measure of the tax system's effect on the rate of return of a hypothetical marginal investment project (i.e., one that just breaks even). We compare the METR on different investments under the House GOP tax plan with the METR under current law. Because the plan would allow expensing (i.e., immediate deduction) of all investment and would reduce average individual-level taxes on interest, capital gains, and dividends, METRs for most new business investment would decrease significantly (Table 8). Investments in intellectual property would face higher METRs than under current law because business interest deductions would be disallowed, but intellectual property would still face the lowest METRs of any form of investment because the plan

[29] Joseph Rosenberg & Donald Marron, *Tax Policy and Investment by Startups and Innovative Firms*, TAX POLICY CTR. (Feb. 9, 2015), http://www.taxpolicycenter.org/UploadedPDF/2000103-tax-policy-and-investments-by-startups-and-innovative-firms.pdf [perma.cc/UMK4-9FWA].

would retain the research and experimentation credit. Business investments financed by debt would face higher effective tax rates than under current law, because the loss of interest deductibility would exceed the benefit of expensing. Overall, the plan would lower METRs, making investment more attractive, and would eliminate the tax advantage for debt- over equity-financed investments, which could reduce corporate leverage.

Although the House GOP tax plan would improve incentives to save and invest, it would also substantially increase budget deficits unless offset by spending cuts, resulting in higher interest rates that would crowd out investment. While the plan would initially increase investment, rising interest rates would eventually decrease investment below baseline levels in later years.

TABLE 8

Marginal Effective Tax Rates on New Investment

In percent, 2017

Category	Current Law	House GOP Tax Plan	Change (percentage points)
Business investment	**22.0**	**6.3**	**-15.7**
Corporate	24.0	8.8	-15.2
Equipment	19.9	9.3	-10.6
Structures	27.9	9.3	-18.6
Intellectual property products	-0.1	4.1	4.2
Inventories	38.4	9.3	-29.1
Pass-through	18.9	2.5	-16.4
Equipment	15.5	3.1	-12.4
Structures	22.3	3.1	-19.2
Intellectual property products	-3.4	-3.0	0.4
Inventories	31.6	3.1	-28.5
Addendum			
Corporate (equity financed)	30.8	8.3	-22.5
Corporate (debt financed)	-7.4	9.8	17.2
Variation (s.d.) across assets	12.2	1.4	
Variation (s.d.) across industries	6.1	0.7	

Source: Urban-Brookings Tax Policy Center calculations. See Rosenberg and Marron (2015) for discussion.
Notes: s.d. = standard deviation. Estimates for are calendar year 2017. The baseline is current law.

D. Impact on Labor Supply

The House GOP tax plan would reduce effective tax rates on labor income (i.e., wages and salaries for employees and self-employment income for others). Effective marginal tax rates on labor income would be reduced by an average of about 2 percentage points and by over 7 percentage points for the top 0.1 percent (Table 9). In combination with increased investment, which raises worker productivity and wages, these effects would initially raise labor supply. Over time, however, because the plan would eventually reduce investment and the capital stock, it would also ultimately depress pretax wages and reduce labor supply.

TABLE 9

Effective Marginal Individual Income Tax Rates on Wages, Salaries, and Self-Employment Income

In percent, 2017[a]

Expanded cash income percentile[b,c]	Tax units (thousands)	Individual income tax			Individual income tax plus payroll tax		
		Current law	House GOP Tax Plan	Change (percentage points)	Current law	House GOP Tax Plan	Change (percentage points)
Lowest quintile	48,340	2.3	2.2	-0.1	16.2	16.0	-0.1
Second quintile	38,630	15.6	14.1	-1.5	29.4	27.9	-1.5
Middle quintile	33,880	19.2	17.8	-1.4	32.8	31.4	-1.4
Fourth quintile	28,660	20.1	19.3	-0.8	33.7	32.9	-0.8
Top quintile	23,960	31.1	28.4	-2.6	38.4	35.4	-3.0
All	174,680	24.7	22.9	-1.9	35.1	33.0	-2.1
Addendum							
80–90	12,390	25.5	25.0	-0.5	36.6	36.1	-0.5
90–95	5,910	27.8	26.6	-1.3	35.7	34.4	-1.3
95–99	4,530	33.0	30.4	-2.6	38.6	35.3	-3.2
Top 1 percent	1,130	38.8	32.3	-6.5	42.7	35.3	-7.4
Top 0.1 percent	120	39.5	32.4	-7.2	43.3	35.3	-8.0

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0516-1).

(a) Projections are for calendar year 2017. Effective marginal tax rates are weighted by the wages and salaries.

(b) Includes both filing and non-filing units but excludes those that are dependents of other tax units. Tax units with negative adjusted gross income are excluded from their respective income class but are included in the totals. For a description of expanded cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm

(c) The income percentile classes used in this table are based on the income distribution for the entire population and contain an equal number of people, not tax units. The breaks are (in 2016 dollars): 20% $24,800; 40% $48,400; 60% $83,300; 80% $143,100; 90% $208,800; 95% $292,100; 99% $699,000; 99.9% $3,749,600.

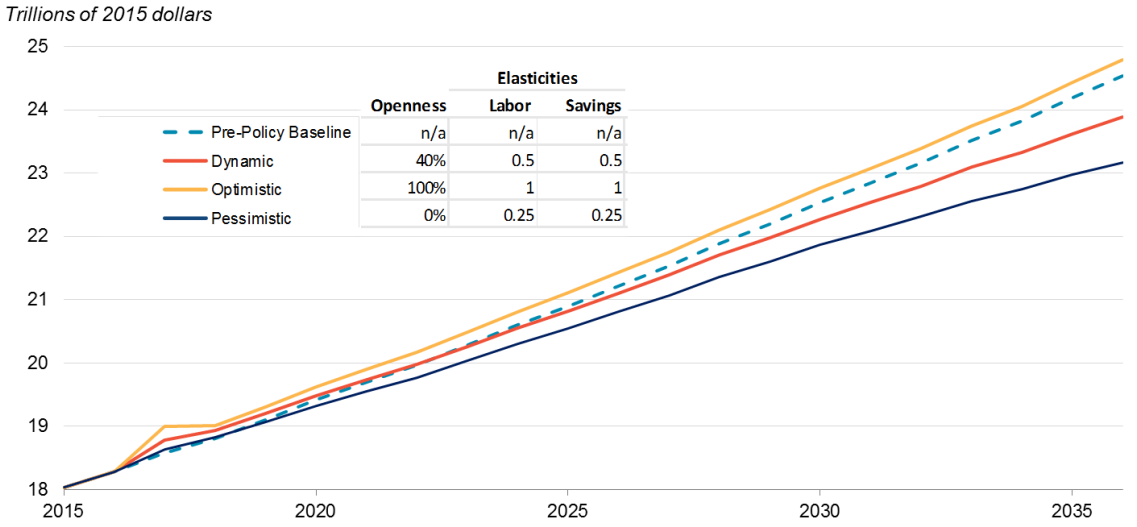
E. Long-Run Impact on Output and Revenues

The PWBM estimates that the House GOP tax plan's effects on investment and labor supply would boost GDP by 0.9 percent in 2017, but would reduce GDP by 0.5 percent in 2026 and by 2.6 percent in 2036 (Table 6). Those economic effects would in turn alter revenues, increasing them by $49.6 billion in 2017 and by $64.0 billion between 2017 and 2026, but reducing them by $1.1 trillion between 2027 and 2036 (Table 2). Taking into account the dynamic effects on GDP and revenues from the PWBM, the plan would increase debt by 13.2 percent of GDP by 2026 and by 22.7 percent of GDP by 2036 (Table 3). The impact on the ratio of debt to GDP is lower in 2026, but higher in 2036, than projected in TPC's conventional estimates.

FIGURE 1

GDP under House GOP Tax Plan

Before and after macro response



Source: Penn Wharton Budget Model (PWBM), based on Urban-BrookingsTax Policy Center (TPC) simulations.
Note: n.a. = not applicable.

F. Sensitivity of Macro Estimates to Assumptions

Macroeconomic models are sensitive to assumptions about how individuals respond to incentives, the operation of world capital markets, and other government policies. Different types of models also can produce very different estimates. The PWBM allows users to see how different assumptions change the model's estimates.[30] For example, compared with the baseline before incorporating

[30] A user interface to the PWBM is available here: http://www.budgetmodel.wharton.upenn.edu/tax-policy-2/ [perma.cc/CCN4-5M4J]. Users may alter assumptions and see effects on GDP, employment, capital stock, etc.

macroeconomic response (labeled "pre-policy baseline" in figure 1), the PWBM's baseline estimates (labeled "dynamic") show GDP rising in the short run before eventually returning to the pre-policy level and then falling below the pre-policy baseline.

The best case scenario for a large and sustained supply-side response is one in which capital markets are open and U.S. deficits do not affect the interest rates facing investors, which are solely determined on world markets.[31] For the "optimistic" scenario in figure 1, we assume 100 percent openness and that labor supply and savings are very responsive to wages and interest rates (represented by elasticities of 1, compared with 0.5 in the baseline). GDP under this set of assumptions rises very quickly to about 1 percent above the pre-policy level. The effect is roughly stable over time in percentage terms.

The pessimistic scenario makes the opposite assumptions. It assumes capital markets are closed—i.e., no borrowing abroad—and that workers and savers are relatively unresponsive to wages and interest rates. In this scenario, GDP falls below the static level starting in 2019. By 2040, it falls by about 9 percent compared with the level in the pre-policy baseline because the government's borrowing creates a shortage of capital and pushes up interest rates.

V. APPENDIX A. UNCLEAR DETAILS AND TPC'S ASSUMPTIONS ABOUT THE HOUSE GOP TAX PLAN

Although Speaker Ryan released a "blueprint" that describes many details about the House GOP tax plan, that document lacks some important details necessary to score the plan accurately. TPC sent the Speaker's staff two sets of clarifying questions along with TPC's working assumptions, one set on June 30, 2016, and a second on July 7, 2016. These are listed below. We based our assumptions on the Tax document released by the Speaker. The Speaker's staff was not able to provide the clarifications we requested, indicating these represented issues that Members had not yet resolved. However, they did point out that the blueprint intends that the ultimate plan be revenue neutral (after including macroeconomic feedback effects) and not raise average taxes on any income group. Some key parameters, therefore, will have to change (assuming the Joint Committee on Taxation's analysis is similar to ours), but we cannot anticipate exactly how

[31] This is typically referred to as a "small open economy" model, where a nation's capital market activity is inconsequential to world markets. It is probably not appropriate for the U.S. given how large we are relative to the world economy, but is shown as a point of comparison.

without further guidance. If we receive clarifications in the future, we will update our analysis.

A. Clarifying Questions and TPC's Working Assumptions about Broad Provisions of the Plan (Sent to the Speaker's Staff on June 30, 2016)

1. "Special-Interest" Tax Provisions

Q1.	The Tax document indicates that the plan would repeal a number of "special-interest" exemptions, deductions and credits for individuals and deductions and credits for businesses, but only identifies one of those provisions (the section 199 domestic production deduction). What, specifically, are these provisions?
A1.	TPC will assume the repealed provisions would include all of the tax expenditures listed at the end of this document.

NOTE: We included in our revenue and distributional estimates only the repeal of those tax expenditures that were clearly identified in the blueprint released by the Speaker: the section 199 domestic production deduction, employee fringe benefits (except those related to health and retirement), and all individual and business tax credits (except the child tax credit, the EITC, education credits, the saver's credit, the research and experimentation tax credit, and the foreign tax credit, all of which the blueprint identifies as retained). Revenue estimates for the other provisions listed below are included as an addendum item in Table 2.

2. Transition Rules

The document indicates that the Committee on Ways and Means will develop transition rules for the plan. Because these rules could have a significant impact on scoring of the plan, key transition rules must be specified.

Q2.	Could unused depreciation and amortization on existing assets be used after the plan goes into effect, and if so what rules would apply?
A2.	TPC will assume that unused depreciation and amortization could be used under current law rules.
Q3.	Would the plan's rules for disallowance of businesses' net interest expense, with an indefinite carryforward (with interest), apply to debt outstanding when the rules go into effect?
A3.	TPC will assume that the plan's rules would not apply, so that interest on existing debt would remain deductible without limit.
Q4.	Could unused credits repealed by the plan, including unused AMT credits, be used once the plan goes into effect, and if so what rules would apply?
A4.	TPC will assume that unused credits could be used, generally under current law rules.
Q5.	Would existing NOLs [net operating losses] be subject to the new rules under the plan?
A5.	TPC will assume that existing NOLs would be subject to the new rules.

3. Border Adjustments

The document indicates that the plan would move to a destination-basis tax system "by providing border adjustments exempting imports and taxing imports… within the context of the transformed business tax system".[32]

Q6.	How would these border adjustments be made, and would any adjustment apply to direct imports by final consumers (households and governments)?

[32] *supra* note 1 at 27.

A6.	TPC will assume that businesses would simply exclude receipts from exports and not deduct imported purchases, and that an excise tax of 20 percent (the corporate rate) would apply to direct imports by final consumers.

4. Estate and Gift Taxes

The plan would repeal the estate and generation-skipping transfer taxes. The plan does not indicate whether the gift tax would also be repealed, or how the basis of gifts and inheritances received would be determined.

Q7.	Would the plan also repeal the gift tax?
A7.	TPC will assume that the gift tax is repealed.
Q8.	Would the basis of gifts and inheritances received a) be carried over from the donor, b) stepped up to their current market value, or c) treated differently? If basis is stepped up, would there be any limits on the amount stepped up?
A8.	TPC will assume that inter vivos gifts will continue to have carryover basis and that inheritances will receive stepped-up basis, but with the limits in effect in 2010 ($1.3 million plus an additional $3 million for surviving spouses, with any additional unrealized gains carried over) but indexed for inflation from 2010.

B. TPC Assumptions (Absent Clarifications) about Other Provisions

1. Individual Income Tax

1. All current law filing statuses would be retained.
2. Individual income tax brackets would match current law (e.g., the plan's 12 percent bracket ends at the same level as the current law 15 percent bracket for each filing status).
3. The 50 percent deduction for dividends would apply only to "qualified dividends" as defined under current law.
4. Interest received from a pass-through would be reduced by interest paid by the pass-through (but not below zero) before applying the 50 percent deduction.
5. The limit on current deductibility of capital losses would be retained, but reduced from $3,000 to $1,500.
6. The limitation on itemized deductions (Pease) would be repealed.

7. The new credit for non-child dependents would phase out under the same (revised) rules used to phase out the child tax credit.

2. Business Tax Provisions

8. Adequate definitions and safeguards would be included in the plan to guide (and enforce) the "reasonable compensation" requirement for sole proprietors and pass-through businesses.
9. The 25 percent rate cap on the active business income of sole proprietors and pass-through businesses would be computed much like the current rate cap on capital gains and dividends (i.e., with active business income treated as otherwise taxable at the highest rate(s) applicable to the taxpayer).
10. The interest rate that applies to carryforwards of unused NOLs would be the 10-year Treasury rate.
11. The foreign tax credit allowed against the deemed repatriation of accumulated untaxed earnings and profits of foreign subsidiaries (as of the effective date of the plan) would be scaled down by the same ratio as the applicable rate (8.75 percent or 3.5 percent) to 35 percent.

3. Effective Date

12. All provisions would become effective January 1, 2017.

C. Provisions that TPC Will Assume are Unchanged

The Tax document identifies a number of current law provisions that the plan leaves to the Committee on Ways and Means to examine with the goal of reforming them. Because the document proposes no specific reforms of the following provisions, TPC must assume for its analysis that the current law specification of the following provisions would remain unchanged. However, we'd be happy to model the specific reforms if you can provide details.

- Earned Income Tax Credit (EITC)
- Education incentives
- Employer-provided health insurance benefits, including FSAs and HSAs [flexible spending accounts and health savings accounts]
- Employer-provided retirement benefits
- Other saving incentives (including both retirement-related and other saving incentives)
- Mortgage interest deduction
- Charitable contribution deduction

- Foreign earned income exclusion and other special rules for individuals living abroad
- Deductibility of interest paid by financial services businesses
- Research and experimentation (R&E) credit

D. Health-Related Tax Provisions

The document only partially addresses reform of health-related tax provisions. The plan would repeal all itemized deductions other than those for mortgage interest and charitable contributions, but does not specifically list the deduction for medical and dental expenses. The plan also assumes that all of the taxes enacted as part of the ACA would be repealed and not replaced with other taxes. However, repeal of these taxes is not considered part of the plan, but rather part of a separate proposal of the Health Care Task Force. The plan description includes no other health-related tax provisions. The report of the Health Care Task Force[33] indicates other health-related tax changes that would be made (e.g., a cap on the exclusion for employer-provided health benefits), but does not provide specifications that would allow scoring them.

In order to make its analysis consistent with the health-related tax changes that are specified in the plan and related plans, TPC will assume that the itemized deduction for medical and dental expenses would be repealed, along with all of the ACA taxes including the 3.8 percent net investment income tax, the 0.9 percent additional Medicare rate, excise taxes (e.g., on medical devices and high premium health insurance), and related fees. Note that the premium credit is treated as an outlay, rather than a tax, by CBO, so we do not include it among the repealed ACA taxes.

E. "Special-Interest" Tax Provisions

The following is the list of tax expenditures (including related payroll tax expenditures) that TPC assumes are repealed by the plan. Please let us know if any of these items would be retained under the proposal.

1. Corporate Income Tax

Energy credit (section 48): Solar

Energy credit (section 48): Geothermal

Coal production credit: Refined coal

Coal production credit: Indian coal

Excess of percentage over cost depletion, fuels: Oil and gas

[33] *supra* note 1.

Excess of percentage over cost depletion, fuels: Other fuels

Excess of percentage over cost depletion, nonfuel minerals

Special rules for mining reclamation reserves

Special tax rate for nuclear decommissioning reserve funds

Exclusion of contributions in aid of construction for water and sewer utilities

Exclusion of earnings of certain environmental settlement funds

Exclusion of cost-sharing payments

Credit for low-income housing

Credit for rehabilitation of historic structures

Credit for rehabilitation of structures, other than historic structures

Deferral of gain on non-dealer installment sales

Deferral of gain on like-kind exchanges

Exemptions from imputed interest rules

Completed contract rules

Credit for employer-paid FICA taxes on tips

Deduction for income attributable to domestic production activities

Credit for the cost of carrying tax-paid distilled spirits in wholesale inventories

Exclusion of gain or loss on sale or exchange of brownfield property

Income recognition rule for gain or loss from section 1256 contracts

Exemption of credit union income

Small life insurance company taxable income adjustment

Special treatment of life insurance company reserves

Special deduction for Blue Cross and Blue Shield companies

Tax-exempt status and election to be taxed only on investment income for certain small property and casualty insurance companies

Interest rate and discounting period assumptions for reserves of property and casualty insurance companies

Proration for property and casualty insurance companies

Deferral of tax on capital construction funds of shipping companies

Special tax provisions for employee stock ownership plans (ESOPs)

Deferral of taxation on spread on acquisition of stock under incentive stock option plans

Deferral of taxation on spread on employee stock purchase plans

Disallowance of deduction for excess parachute payments

Limits on deductible compensation

Credit for employer-provided dependent care

Credit for disabled access expenditures

Credit for orphan drug research

Tax credit for small businesses purchasing employer insurance

Exclusion of disaster mitigation payments

Tax Expenditures permanently extended by HR 2029:

Modification of tax treatment of certain payments under existing arrangements to controlling exempt organizations made permanent

Permanently extend and modify employer wage credit for activated military reservists

Minimum LIHTC rate for non-Federally subsidized new buildings (9%) made permanent

2. Individual Income Tax (including pass-through businesses)

Exclusion of benefits and allowances to armed forces personnel

Exclusion of military disability benefits

Deduction for overnight-travel expenses of national guard and reserve members

Exclusion of energy conservation subsidies provided by public utilities

Energy credit (section 48): Solar

Energy credit (section 48): Geothermal

Excess of percentage over cost depletion, fuels: Oil and gas

Excess of percentage over cost depletion, fuels: Other fuels

Exceptions for publicly traded partnership with qualified income derived from certain energy-related activities

Excess of percentage over cost depletion, nonfuel minerals

Special rules for mining reclamation reserves

Special tax rate for qualified timber gain (including coal and iron ore)

Treatment of income from exploration and mining of natural resources as qualifying income under the publicly-traded partnership rules

Exclusion of cost-sharing payments

Exclusion of cancellation of indebtedness income of farmers

Income averaging for farmers and fishermen

Exclusion of capital gains on sales of principal residences

Credit for low-income housing

Credit for rehabilitation of historic structures

Credit for rehabilitation of structures, other than historic structures

Deferral of gain on non-dealer installment sales

Deferral of gain on like-kind exchanges

Exemptions from imputed interest rules

Completed contract rules

Credit for employer-paid FICA taxes on tips

Deduction for income attributable to domestic production activities

Exclusion for gain from certain small business stock

Income recognition rule for gain or loss from section 1256 contracts

Exclusion of employer-paid transportation benefits (parking, van pools, and transit passes)

Exclusion of employee meals and lodging (other than military)

Exclusion of housing allowances for ministers

Exclusion of miscellaneous fringe benefits

Exclusion of employee awards

Exclusion of income earned by voluntary employees' beneficiary associations

Special tax provisions for employee stock ownership plans (ESOPs)

Deferral of taxation on spread on acquisition of stock under incentive stock option plans

Deferral of taxation on spread on employee stock purchase plans

Credit for employer-provided dependent care

Exclusion of certain foster care payments

Adoption credit and employee adoption benefits exclusion

Credit for disabled access expenditures

Credit for orphan drug research

Tax credit for small businesses purchasing employer insurance

Exclusion of workers' compensation benefits (disability and survivors payments)

Exclusion of damages on account of personal physical injuries or physical sickness

Exclusion of special benefits for disabled coal miners

Premiums on group term life insurance

Premiums on accident and disability insurance

Exclusion of survivor annuities paid to families of public safety officers killed in the line of duty

Exclusion of disaster mitigation payments

Exclusion of veterans' readjustment benefits

Deferral of interest on savings bonds

Tax Expenditures permanently extended by HR 2029:

Parity for exclusion from income for employer-provided mass transit and parking benefits made permanent

Permanently extend and modify employer wage credit for activated military reservists

Treatment of certain dividends of RICs made permanent

Exclusion of 100 percent of gain on certain small business stock made permanent

Reduction in S corporation recognition period for built-in gains tax made permanent

Minimum LIHTC rate for non-Federally subsidized new buildings (9%) made permanent

Military housing allowance exclusion for determining LIHTC eligibility made permanent

Treatment of RICs as "qualified investment entities" under section 897 (FIRPTA) made permanent

Deductibility of excise tax on high cost employer-sponsored health coverage

3. Payroll Tax

Exclusion of employer-paid transportation benefits (parking, van pools, and transit passes)

Exclusion of employee meals and lodging (other than military)

Exclusion of housing allowances for ministers

Exclusion of other employee benefits: Premiums on group term life insurance (excludes payroll taxes)

Exclusion of other employee benefits: Premiums on accident and disability insurance

Tax Expenditure permanently extended by HR 2029:

Parity for exclusion from income for employer-provided mass transit and parking benefits made permanent

F. Additional Clarifying Questions and TPC Assumptions about the Plan (Sent to the Speaker's Staff July 7, 2016)

1. "Special Interest" Tax Provisions

In addition to the list of tax expenditures listed in our prior document, we will also assume repeal of all private purpose tax exempt bonds; repeal of above-the-line deductions for expenses of educators and reservists, etc., moving expenses and alimony paid; and repeal of all personal credits (except the child tax credit, education credits, saver's credit, and the foreign tax credit; so, for example, we will assume the child and dependent care tax credit is repealed).

NOTE: We included in our revenue and distributional estimates only the repeal of those tax expenditures that were clearly identified in the blueprint released by the Speaker: the section 199 domestic production deduction, employee fringe benefits (except those related to health and retirement), and all individual and business tax credits (except the child tax credit, the EITC, education credits, the saver's credit, the research and experimentation tax credit, and the foreign tax credit, all of which the blueprint identifies as retained). Revenue estimates for the other provisions listed above are included as an addendum item in Table 2.

2. Rate Cap on Active Business Income

We will assume that income currently subject to SECA, or taxed as wages of worker/owners of subchapter S corporations, is "reasonable compensation". For the remaining income of sole proprietors and pass-through businesses, we will assume that only income that is currently not considered "passive" will qualify for the rate cap. Current active business losses will be allowed, rather than being carried forward with interest (which will shift the timing of income tax receipts somewhat, but generally not the present value of these receipts).

3. Child Tax Credit and New Credit for Other Dependents

We will assume these are not indexed for inflation.

4. Standard Deduction for Dependents

We will assume that the standard deduction for dependents (in 2016 dollars) is the *smaller* of: (i) the *greater* of (a) earned income plus $350 and (b) $1,050, and (ii) the regular standard deduction for the dependent's filing status (as modified by the proposal). We will assume all amounts are indexed for inflation.

5. Base Year for Indexing

We will assume that all indexed parameters are stated at 2016 levels, so are indexed beginning in 2017 (our assumed effective date for the plan).

VI. APPENDIX B. MEASURING DISTRIBUTIONAL EFFECTS OF TAX CHANGES

Analysts use a variety of measures to assess the distributional effects of tax changes. There is no perfect measure—often a combination of measures is more informative than any single measure.

The Tax Policy Center generally focuses on the percentage change in after-tax income because it measures the gain or loss of income available to households to buy goods and services, relative to the amount available before the tax change. A tax change that raises or lowers after-tax income by the same percentage for all households leaves the progressivity of the tax unchanged.

Other measures used to assess a tax change's effects include shares of the tax cut going to different parts of the income distribution, the size of each group's cut measured in dollars, and the percentage change in tax liability. The first two measures poorly indicate the effects of a tax change because they ignore the initial distribution of taxes and thus do not assess changes in a tax's progressivity. The percentage change in tax liability can be particularly misleading because it relies too much on the initial distribution of taxes. Cutting the tax on a person making $1,000 from $50 to $10 is an 80 percent cut, whereas reducing taxes on a person making $1 million from $250,000 to $150,000 is just a 40 percent cut. But the tax savings boosts after-tax income by only about 4 percent for the poorer person, compared with a more than 13 percent increase for the higher-income person.

Table B1 shows several different measures of the effects of the House GOP tax plan on households at different income levels in 2017. The tax cut is most significant as a share of after-tax income (column 1) for those with high incomes, as discussed above. It's also true that for this plan, high-income people get the bulk of the tax cuts (column 2), that the average tax change is highest at high income levels (column 3), and that the tax cut is a larger share of tax liability for high-income households (column 4). Finally, the share of federal tax burdens increases at most income levels, falling only for the top 1 percent (column 5).

TABLE B1

Alternative Ways of Presenting Change in Distribution of Tax Burdens under the House GOP Tax Plan

By expanded cash income percentile, 2017[a]

Expanded cash income percentile[b,c]	Percent change in after-tax income[d] (%)	Share of total federal tax change (%)	Average federal tax change[e]		Share of federal taxes	
			Dollars	Percent	Change (% points)	Under the proposal (%)
Lowest quintile	0.4	0.8	-50	-9.3	0.0	0.8
Second quintile	0.4	1.4	-120	-3.9	0.3	4.0
Middle quintile	0.5	2.8	-260	-2.9	0.8	10.4
Fourth quintile	0.5	3.7	-410	-2.1	1.6	19.2
Top quintile	4.6	89.0	-11,760	-13.1	-2.3	65.7
All	2.5	100.0	-1,810	-10.0	0.0	100.0
Addendum						
80–90	0.2	1.2	-310	-0.9	1.4	15.3
90–95	0.2	0.7	-370	-0.7	1.1	11.5
95–99	2.5	11.0	-7,690	-7.3	0.5	15.6
Top 1 percent	13.4	76.1	-212,660	-26.7	-5.3	23.4
Top 0.1 percent	16.9	46.5	-1,262,530	-32.0	-3.6	11.0

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0516-1).

Notes: Number of Alternative Minimum Tax (AMT) taxpayers (millions): Baseline: 4.8; Proposal: 0.

(a) Calendar year. Baseline is current law. Proposal includes individual, payroll, corporate, excise, and estate provisions in the House GOP tax plan. http://www.taxpolicycenter.org/taxtopics/Baseline-Definitions.cfm

(b) The percentile includes both filing and non-filing units but excludes those that are dependents of other tax units. Tax units with negative adjusted gross income are excluded from their respective income class but are included in the totals. For a description of expanded cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm

(c) The income percentile classes used in this table are based on the income distribution for the entire population and contain an equal number of people, not tax units. The breaks are (in 2016 dollars): 20% $24,800; 40% $48,400; 60% $83,300; 80% $143,100; 90% $208,800; 95% $292,100; 99% $699,000; 99.9% $3,749,600.

(d) After-tax income is expanded cash income less: individual income tax net of refundable credits; corporate income tax; payroll taxes (Social Security and Medicare); estate tax; and excise taxes.

(e) Average federal tax (includes individual and corporate income tax, payroll taxes for Social Security and Medicare, the estate tax, and excise taxes) as a percentage of average expanded cash income.