

Tax Policy 2017:

Proposals and Prospects for Significant Tax Reform under the 45th President

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“July 15, 2017”

Structure of My Remarks

- Popular political support for reforming U.S. tax system.
- Structural trends in the distribution of U.S. federal tax burdens.
- Responses of presidential candidates to popular sentiment for reform.
- Tax proposals of 5 candidates: *3 Republicans* and *2 Democrats*
- Projections for November 2016 election.
- Projections about tax reform in 2017 or beyond.

"A long time ago, in a galaxy far far away..."

THE NEW YORK TIMES, FRIDAY, MAY 9, 1986

A First-Rate Tax-Reform Bill

By John H. Makin

WASHINGTON — Less than a month ago, I felt that the Senate Finance Committee had turned the effort to reform America's tax system into a national disgrace. Since then, the chairman, Bob Packwood, has led a courageous reversal by putting forward a plan that, enacted intact, could prove to be a national treasure.

Senator Packwood's proposal satisfies the basic criteria for tax reform. It reduces the top tax rate for individuals to 27 percent and the corporate tax rate to 33 percent. It achieves revenue-neutral reform by eliminating dozens of tax breaks. The effect is to allow households and corporations to keep more of each dollar they earn, irrespective of how they earn it. Compared to the other proposals already advanced, the Packwood plan represents the largest step toward real tax reform.

Those who think that the Packwood plan is a rich man's plan should think again. Under current law a couple whose taxable income is \$50,000 pays 38 cents in Federal taxes on every extra dollar they earn. Under the Packwood plan they would pay 27 cents in taxes on every extra dollar earned and if, through extra effort, they boosted their income to \$66,000,

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they would still pay to the Government 27 cents of every extra dollar earned instead of moving into the 42 percent bracket as they would under current law.

The plan does not neglect low-income taxpayers either. A combination of a \$2,000 personal exemption and a \$5,000 standard deduction removes the poor from the tax rolls. Low-income couples working hard to better their lot would pay only 15 cents on the dollar in Federal taxes until their taxable income reached \$29,300. Under current law, their tax bracket would rise steadily to reach a 25 percent tax bite at the \$28,000 level.

The proposal recognizes that a sharp drop in the top tax rate would, without some adjustment, provide disproportionate benefits to high-income individuals currently in the 50 percent bracket. It addresses this problem by denying high-income taxpayers the benefits of the \$2,000 personal exemption and the 15 percent bracket. These adjustments mean that high-income taxpayers get a tax cut about half as large, in percentage terms, as the average for all taxpayers.

The proposal treats capital gains as ordinary income and eliminates the \$2,000 I.R.A. deduction for taxpayers covered by other pension plans. With a maximum tax rate of 27 percent, the need to treat capital gains as a special category is much reduced. In the past, the main reason for a low tax rate on capital gains was to avoid taxing illu-

It could be
'a national
treasure'

sory or inflationary gains where the price of a security or a piece of property rises only as a reflection of general inflationary pressures. The Packwood proposal could further insure the attractiveness of investment by combining with its low tax rate an indexing provision that adjusts for inflation the cost of acquiring an asset.

Under current law, I.R.A. deductions represent an attempt to encourage Americans to save in the face of a tax system that otherwise encourages borrowing and discourages saving. But Mr. Packwood's lower tax rate on interest income would provide an immediate incentive for all households to add to saving. And by limiting the deduction for interest expense, the plan would further encourage saving by discouraging borrowing for current consumption. As with capital gains, the plan would be improved by indexing interest income and expense so that savers would not be taxed on the inflationary portion of interest earnings.

Corporations lose the investment tax credit under the Packwood plan,

but they gain a sharp reduction in their tax rate from 46 to 33 percent. These two provisions will go a long way toward producing an efficient mix of capital spending. Through readjustment of depreciation schedules and modified expensing provisions, the plan provides adequate investment incentives to keep the cost of capital low, thereby insuring adequate capital formation.

The plan's greatest benefit will be an end to the accelerating whirl of jockeying for tax advantages. When tax breaks are worth 27 cents on the dollar instead of 50 cents on the dollar, the payoff to lobbying Congress for special tax breaks is sharply reduced. That's why the Packwood plan has most lobbyists in a panic. And because there will be less incentive to push for tax breaks, uncertainty about the tax code will diminish. This in itself will be a great source of encouragement for the long-term investment America sorely needs.

The Packwood plan is closer to what President Reagan wanted out of tax reform than his own plan. Its top rate is well below 35 percent, it allows a \$2,000 personal exemption, it takes the poor off the tax rolls and it is revenue-neutral. The White House should work with Senate Republicans to push the plan through the Senate-House Conference Committee. Success might add the brightest jewel to the chain of the Administration's economic achievements. □

We Need Tax Reform Now!

OCTOBER 30, 2014 JOHN OLEN



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Despite on the good news we hear on television, our country has a one way ticket to destruction if we don't act now. Our best companies are being bought out by

foreign interest and those that remain are moving their headquarters

Top 20 Stocks for 2016

Tax Experts Agree: We Need Tax Reform



Forbes / Opinion

JAN 15, 2014 @ 08:00 AM 3,861 VIEWS

To Guarantee The U.S.'s Economic Future, We Need Tax Reform Now

SQUARE-OFF

What Kind of Tax Reform Do We Need?

Everyone agrees we need tax reform, but opinions on what it should look like are varied. Here are five different takes.

Tax



CENTER FOR FEDERAL TAX POLICY CENTER FOR STATE TAX POLICY CENTER FOR LEGAL REFORM

The Tax Policy Blog > Small Businesses Need Tax Reform, Too
Small Businesses Need Tax Reform, Too

Mythbusting tax reform

Tax reform is more vital than ever before

Taxes affect prosperity =
bad taxes to good taxes = gap
in economic costs between
good taxes and bad taxes

Increase the national pie

We can look after low income earners

Fairness = result of all government spending + all taxes + other incentives + payments

Spending policy also needs to be addressed

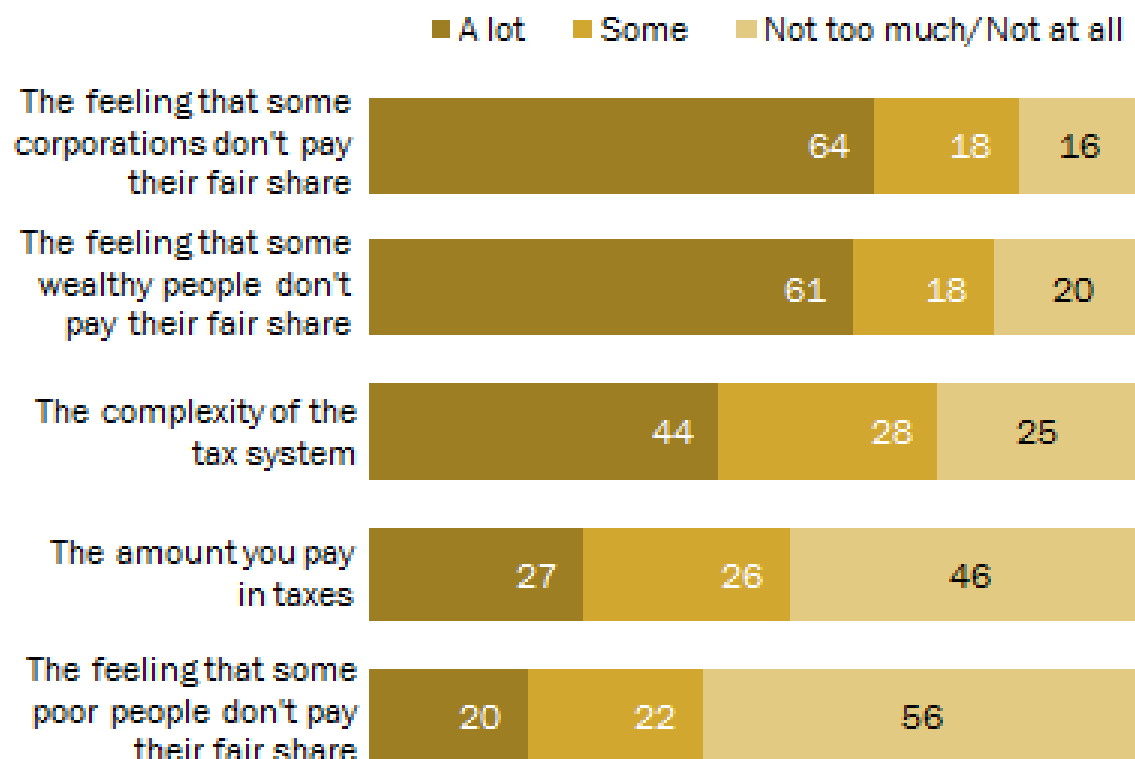
FOR RELEASE MARCH 19, 2015

Federal Tax System Seen in Need of Overhaul

*Top Complaints: Wealthy,
Corporations 'Don't Pay Fair Share'*

More Are Bothered by Corporations, Wealthy Not Paying Fair Share Than by What They Pay in Taxes

% saying each bothers them _____ about federal tax system ...



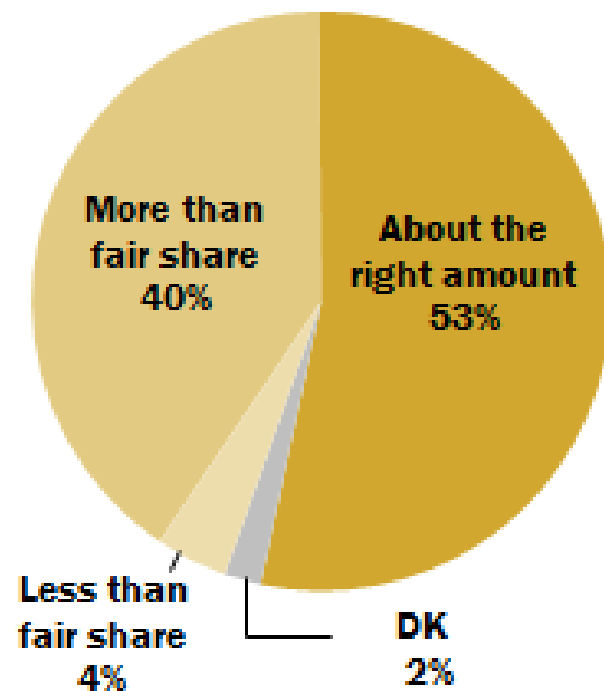
Survey conducted Feb. 18-22, 2015.

Don't know responses not shown.

PEW RESEARCH CENTER

53% Say They Pay 'About Right Amount' in Taxes

Considering what you get from fed. gov't, do you pay ____ of taxes?

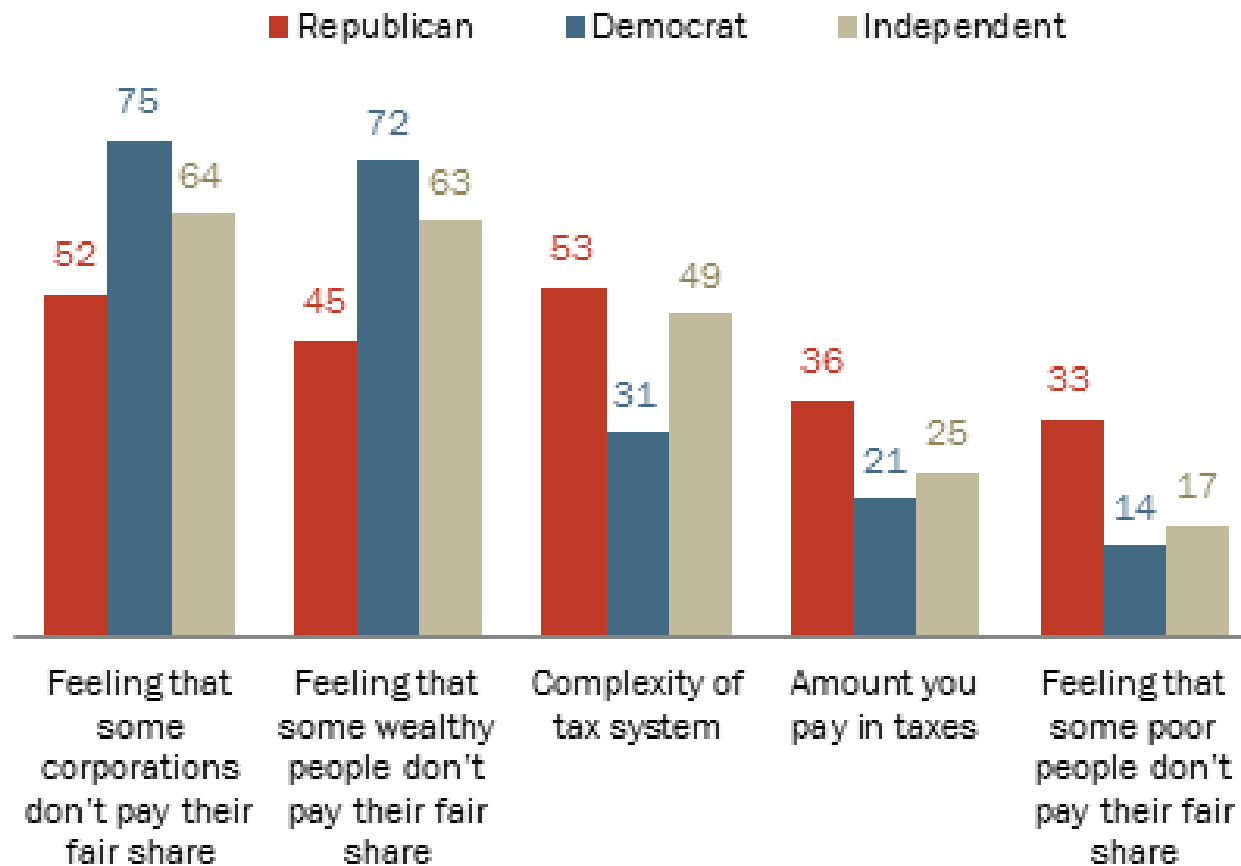


Survey conducted Feb. 18-22, 2015.
Figures may not add to 100% because of rounding.

PEW RESEARCH CENTER

Democrats, Republicans Bothered by Different Aspects of Federal Tax System

% saying each bothers them 'a lot' about federal tax system ...



Survey conducted Feb. 18-22, 2015.

PEW RESEARCH CENTER

Wider Partisan Gap on Whether Congress Should ‘Completely Change’ Federal Tax System

Which comes closest to your view of federal tax system? Should Congress ...

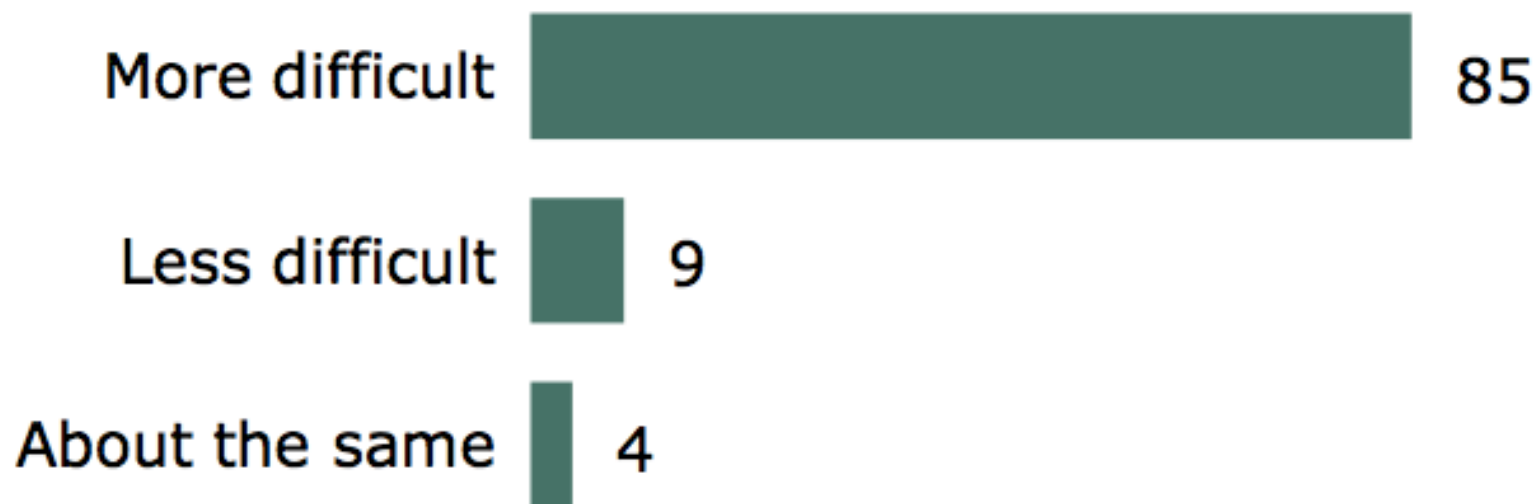
	Dec 2011		Feb 2015		
	Completely change tax system	Make only minor changes	Completely change tax system	Make only minor changes	Change in ‘completely change’
	%	%	%	%	
Total	59	34	59	38	0
Republican	60	36	66	31	+6
Conserv Rep	63	31	72	25	+9
Mod/Lib Rep	56	41	53	46	-3
Independent	63	30	63	34	0
Democrat	55	40	48	48	-7
Cons Mod Dem	53	43	46	50	-7
Liberal Dem	58	36	50	48	-6
<i>Family income</i>					
\$100,000 or more	66	31	63	36	-3
\$75,000-\$99,999	66	32	63	34	-3
\$30,000-\$74,999	60	36	64	35	+4
Less than \$30k	54	37	48	46	-6

Survey conducted Feb. 18-22, 2015. Don't know responses not shown.

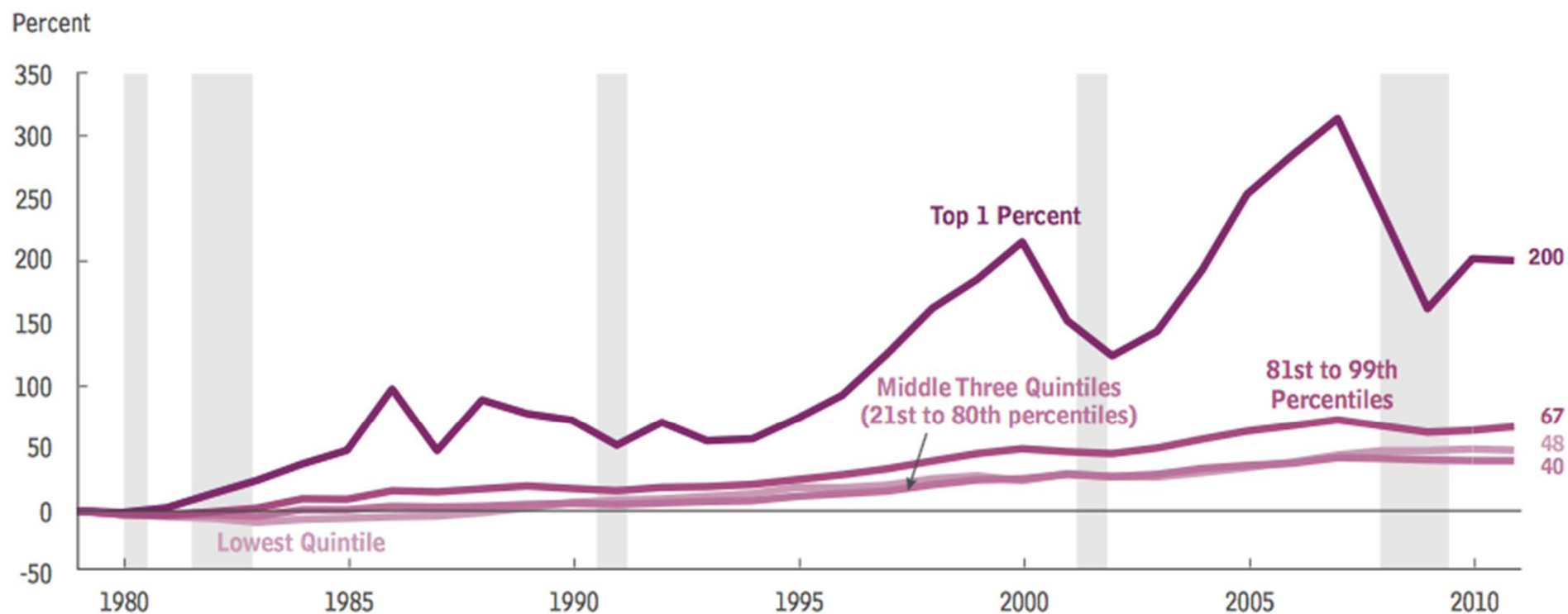
PEW RESEARCH CENTER

... and the Middle Class Says its Lifestyle is Harder to Maintain

% of middle-class adults who say it is ...for middle class to maintain standard of living today than 10 years ago



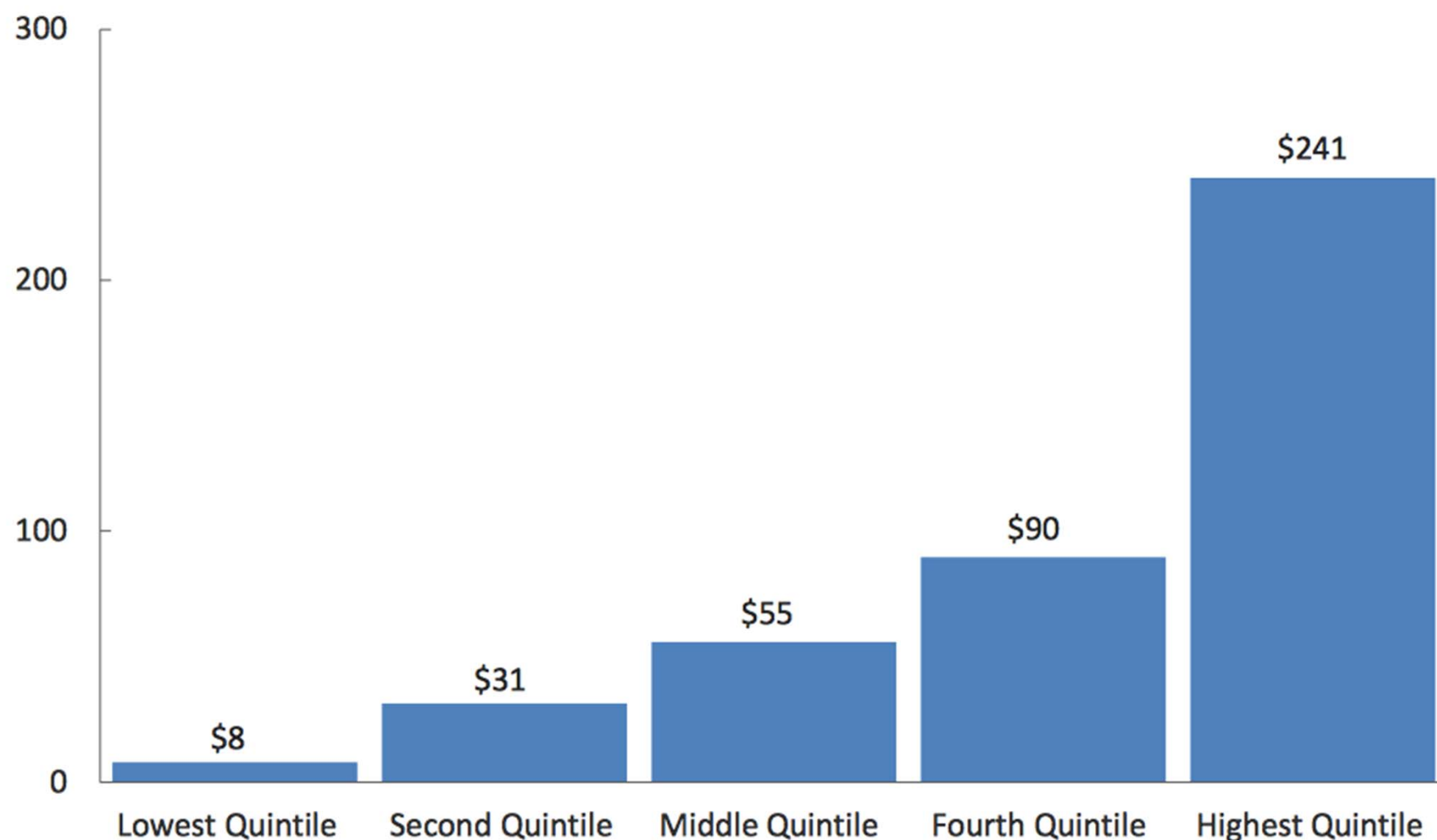
Cumulative Growth in Average Inflation-Adjusted After-Tax Income, by Before-Tax Income Group, 1979 to 2011



Source: Congressional Budget Office.

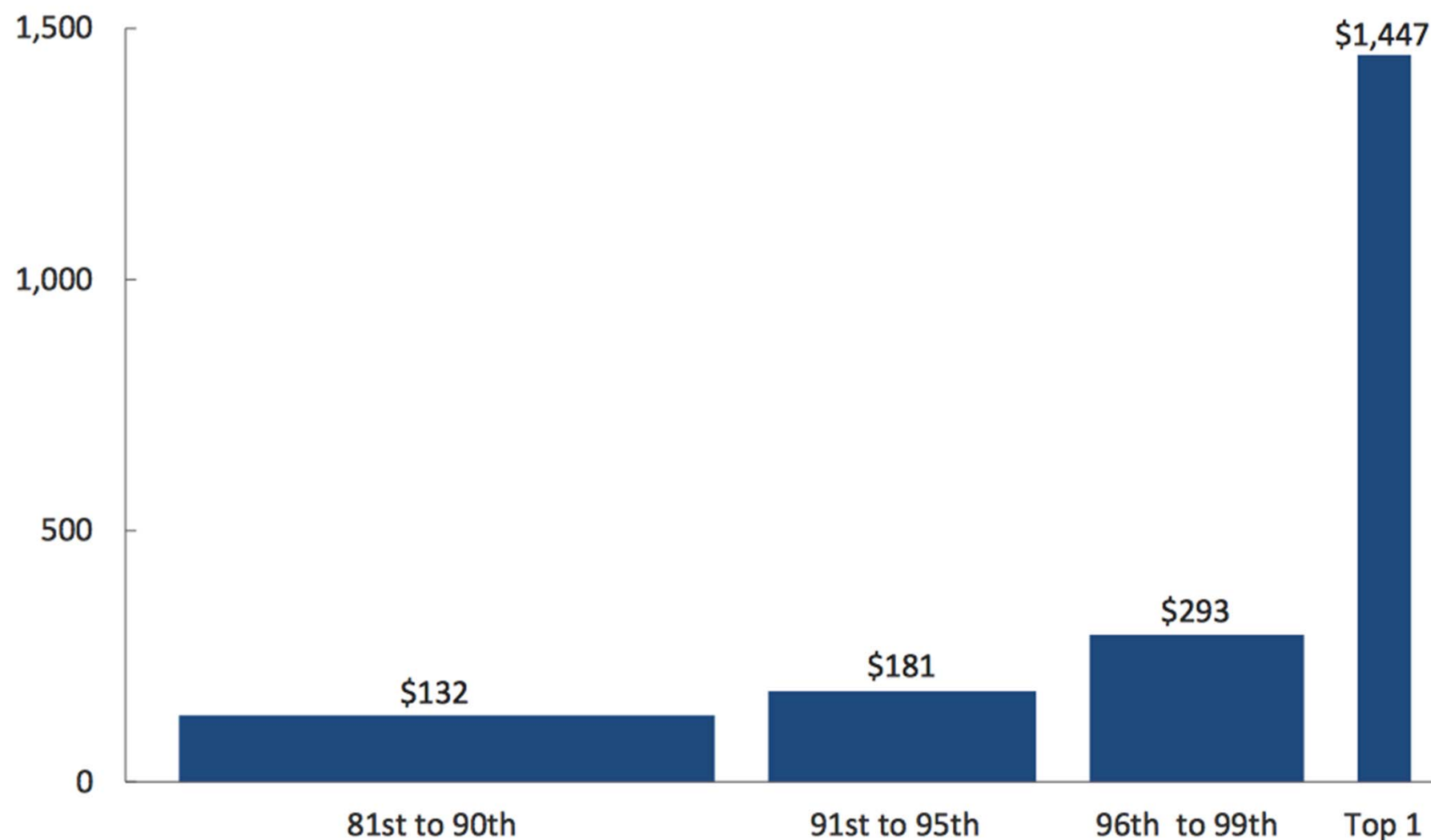
Average Market Income, by Market Income Group, 2011

Thousands of Dollars



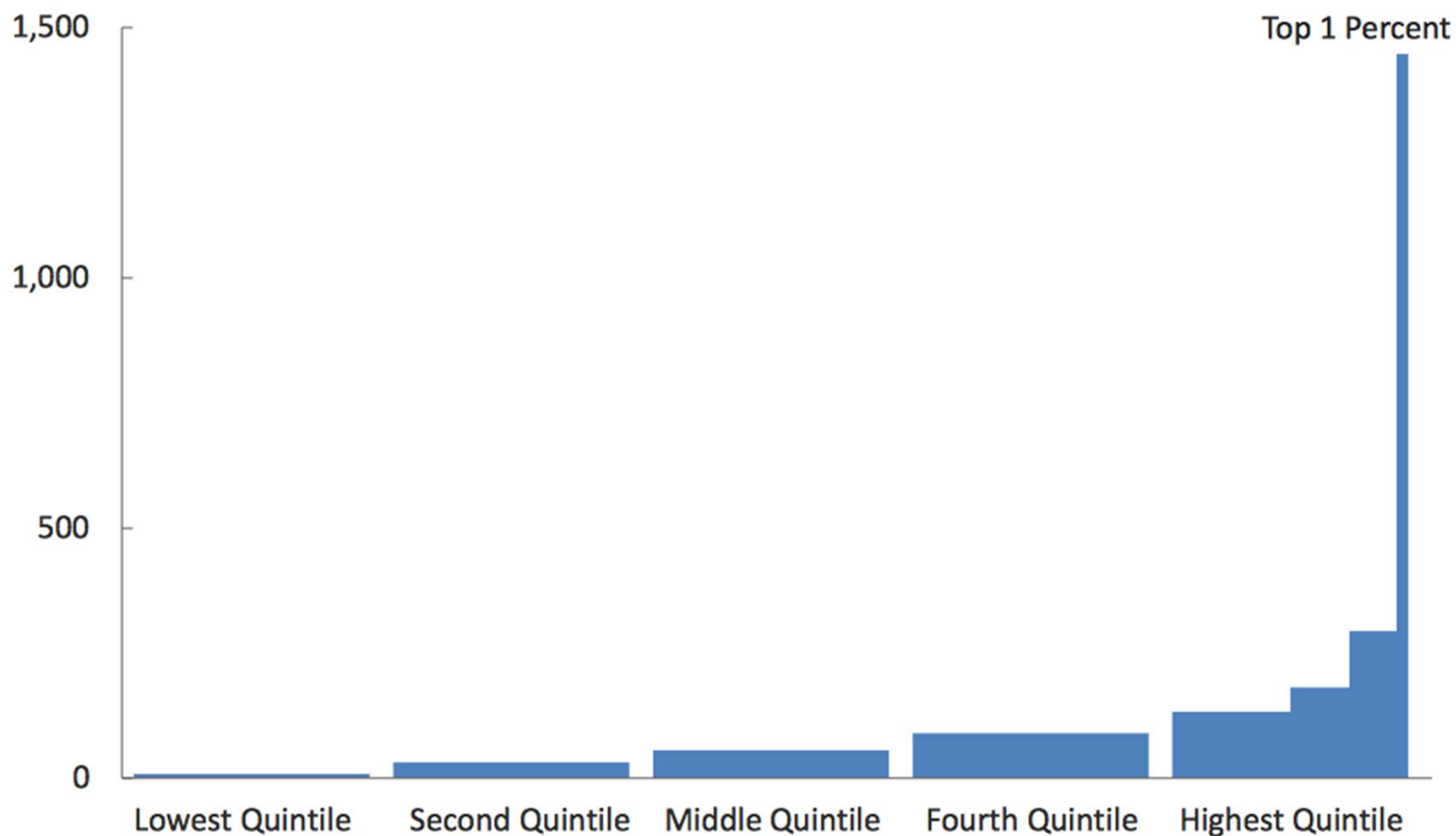
Average Market Income, Top Income Quintile, 2011

Thousands of Dollars

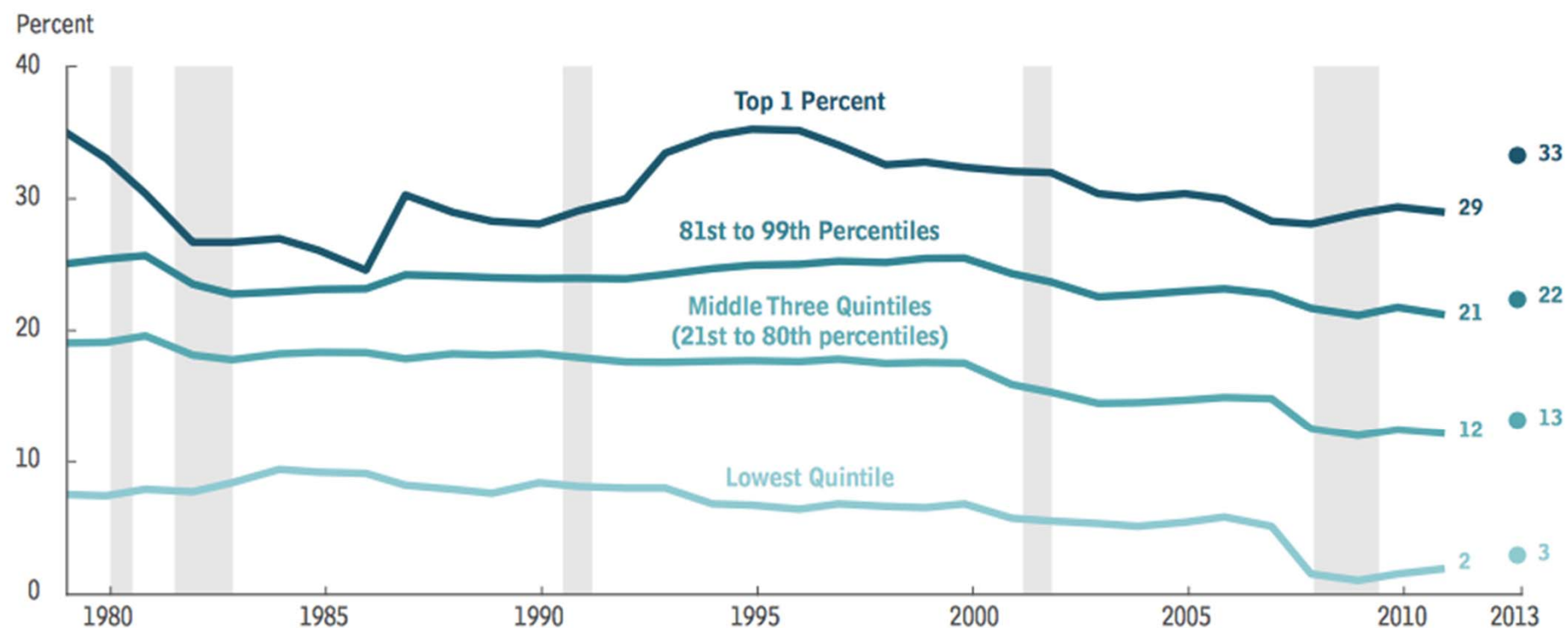


Average Market Income, by Market Income Group, 2011

Thousands of Dollars

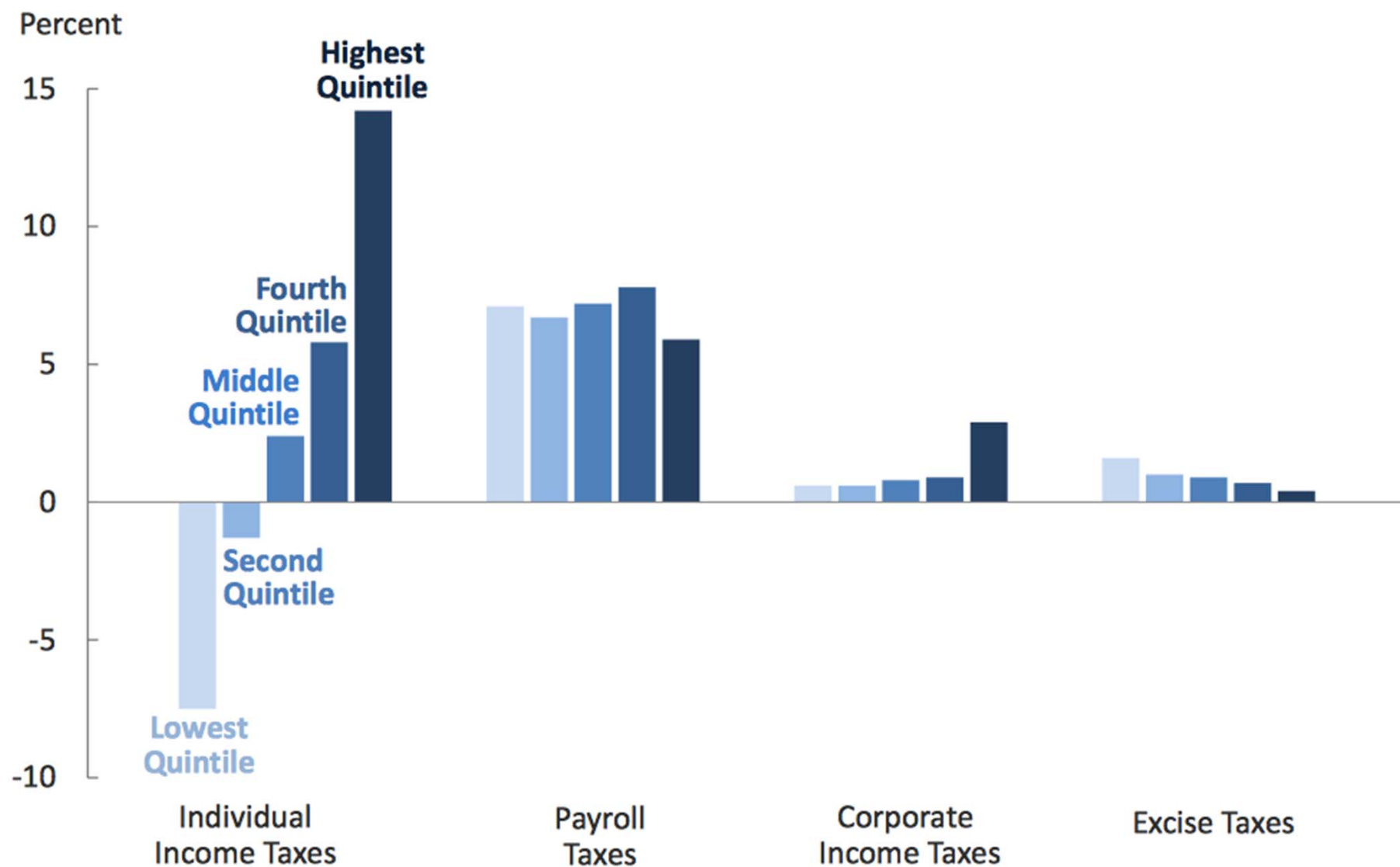


Average Federal Tax Rates, by Before-Tax Income Group, 1979 to 2011 and Projected Under 2013 Law



Source: Congressional Budget Office.

Average Federal Tax Rates, by Before-Tax Income Group and Source, 2011



TAX CUTS....

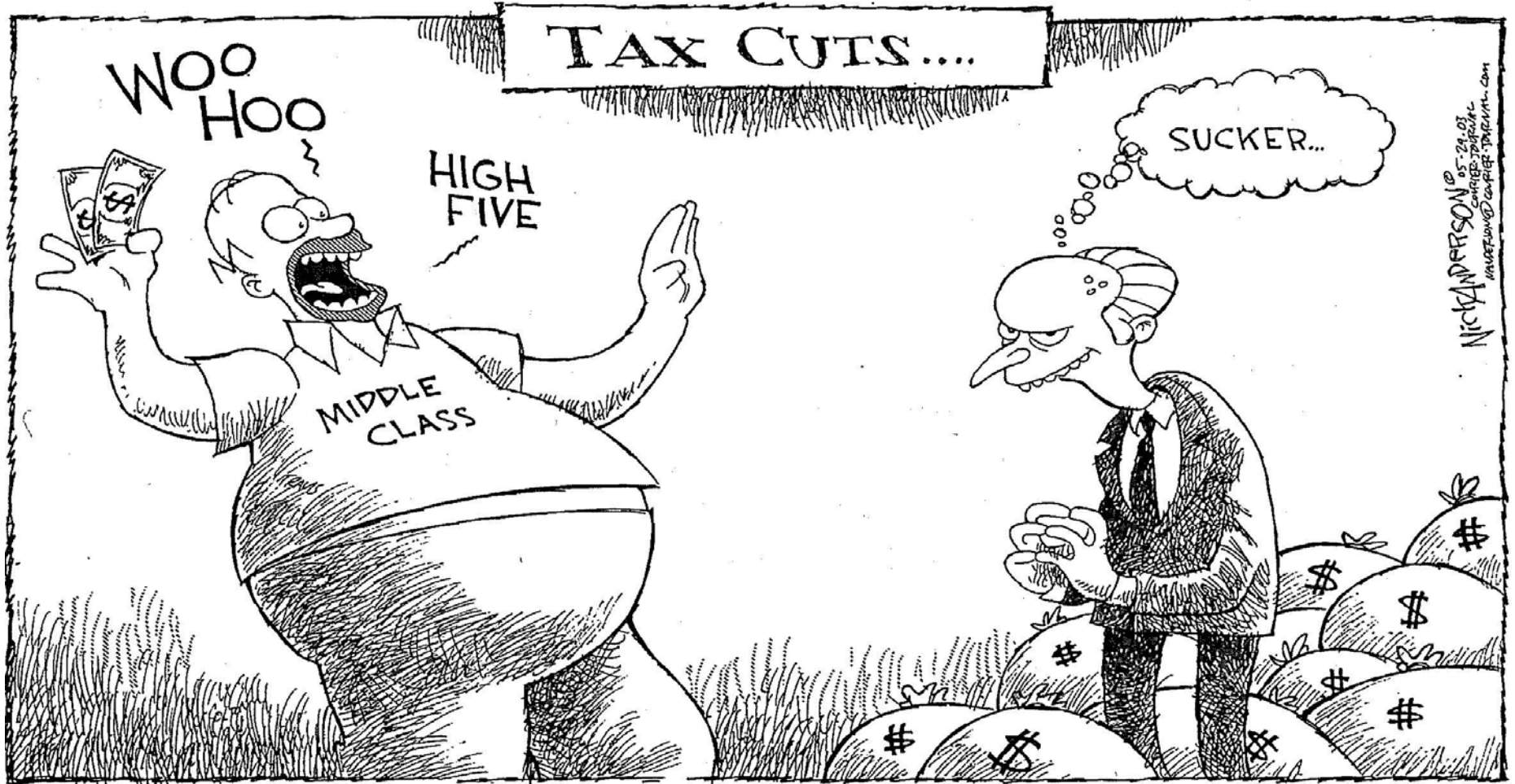
WOO
HOO

HIGH
FIVE

MIDDLE
CLASS

SUCKER...

NICK ANDERSON © 05-24-03
CHARGE! JOURNAL
HAND-DRIVEN CARTOONISTS.COM



GOP Candidate Tax Proposals



- Flatten individual rates (10%, 20%, 25%), increase standard deduction (\$25k/\$50k), Tax carried interest at ordinary rates (but presumably new business tax rate of 15%).
- Eliminate AMT, 3.8% NIT, Estate Tax.
- Reduce corporate rate to 15% and apply same max 15% rate to all business income including pass-through entities.



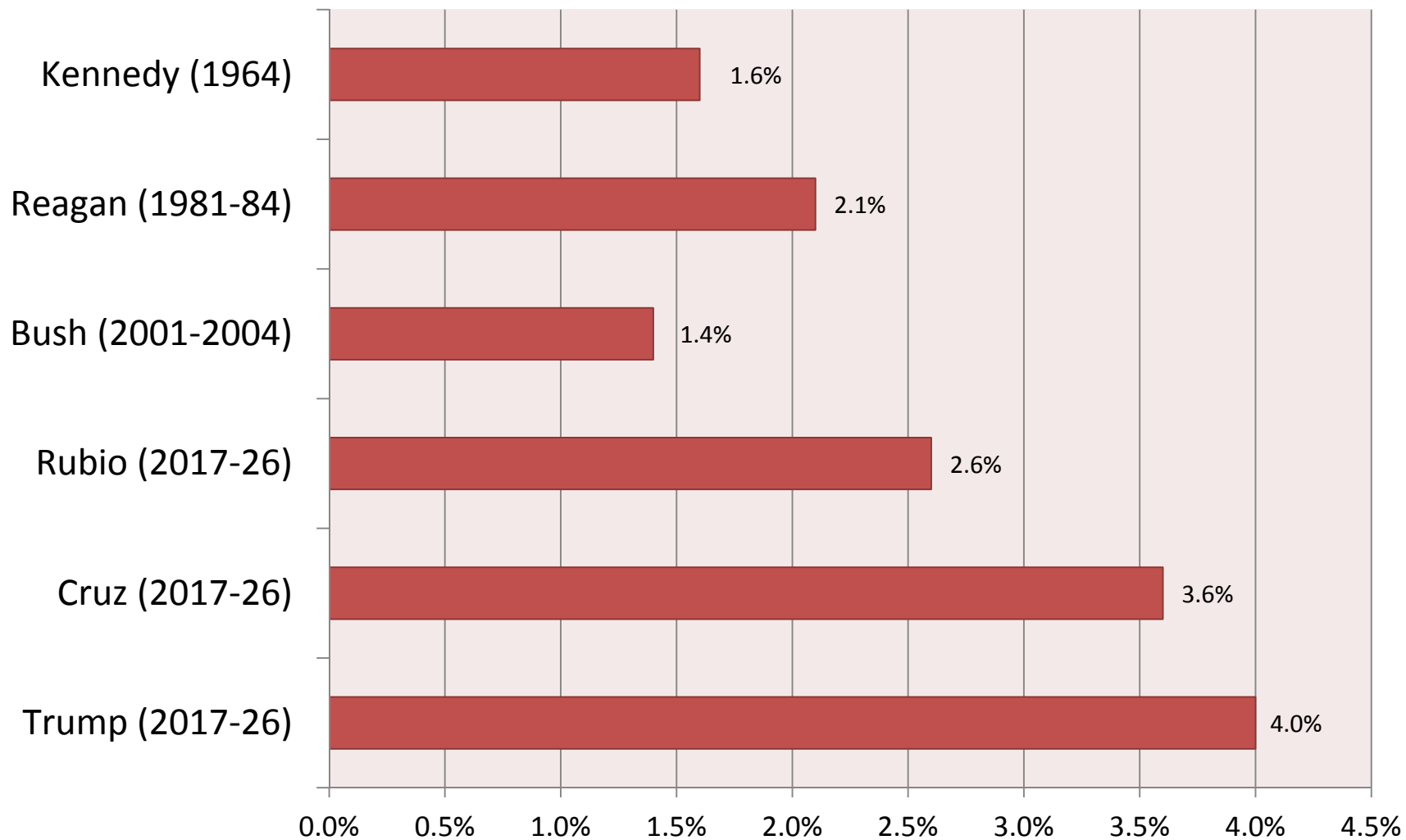
- Single rate of 10% w/ \$10k standard deduction. No deducts except charitable & home mortgage interest, expanded EITC.
- Eliminate AMT, 3.8% NIT, Estate Tax & payroll taxes.
- New “Business Flat Tax” (subtraction method VAT) of 16%. Deduction for all payments to other firms; no deduction for wages.



- Flatten rates (15%, 25%, 35%), replace standard deduction w/ refundable \$2k credit (McGovern) & new \$2.5k child credit; no deducts except charitable & home mortgage interest.
- Eliminate AMT, 3.8% NIT, Estate Tax.
- Reduce corporate rate to 25% and apply same max 25% rate to all business income including pass-through entities. All business expenses immediately deductible, as with subtraction method VAT, but wages would be deductible (and taxed at progressive rates of 15% to 35%).

Tax Cuts as a Percentage of GDP

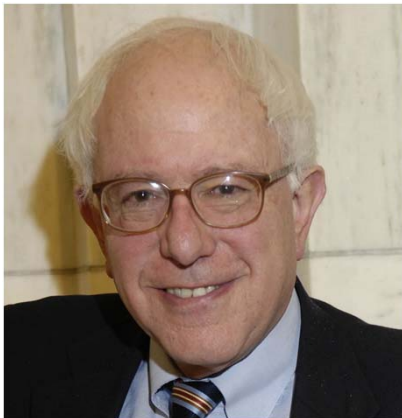
Based on Data from Len Burman, Urban-Brookings Tax Policy Center



DEM Candidate Tax Proposals



- New 4% “surcharge” on incomes greater than \$5 million (similar to French “exceptional surtax”).
- Tax carried interest as ordinary income.
- Adopt a “Buffet Rule” to ensure that those with income greater than \$1 million face effective rate of at least 30%.
- Increase top estate tax rate to 45% & reduce exemption to \$3.5 million.



- Steepens rates at high income levels with new rates of 37%, 43%, 48%, 52% (with top rate applying to income over \$10 million). All other brackets increase by 2.2%. Itemized deductions capped at 28% marginal rate.
- For those with income > \$250k, tax capital gains as ordinary income. New financial transactions tax (Tobin).
- Social security taxes extended to incomes over \$250,000. New 6.2% employer tax. New 0.2% wage tax to fund paid family leave.

JAN 17, 2016 @ 09:42 PM 407,518 VIEWS

Bernie Sanders Releases Tax Plan, Nation's Rich Recoil In Horror









Recapping the Partisan Tax Divide

- **Republican Candidate Consensus:**
 - flatten the rate structure, lower the rates
 - eliminate AMT, NIT, estate tax
 - significant reworking of business tax structure
 - significant reduction in federal revenue
- **Democratic Candidate Consensus:**
 - increase rates at the high end
 - limit deductions; limit favorable capital gains rate
 - no major departure from existing structure
 - significant increase in federal revenue






The next 8 months...

- Primaries to determine GOP nominee
- Primaries to determine DEM nominee
- November elections to determine President
- November elections to determine control of House
- November elections to determine control of Senate
- *obviously, a lot can happen between now and then*

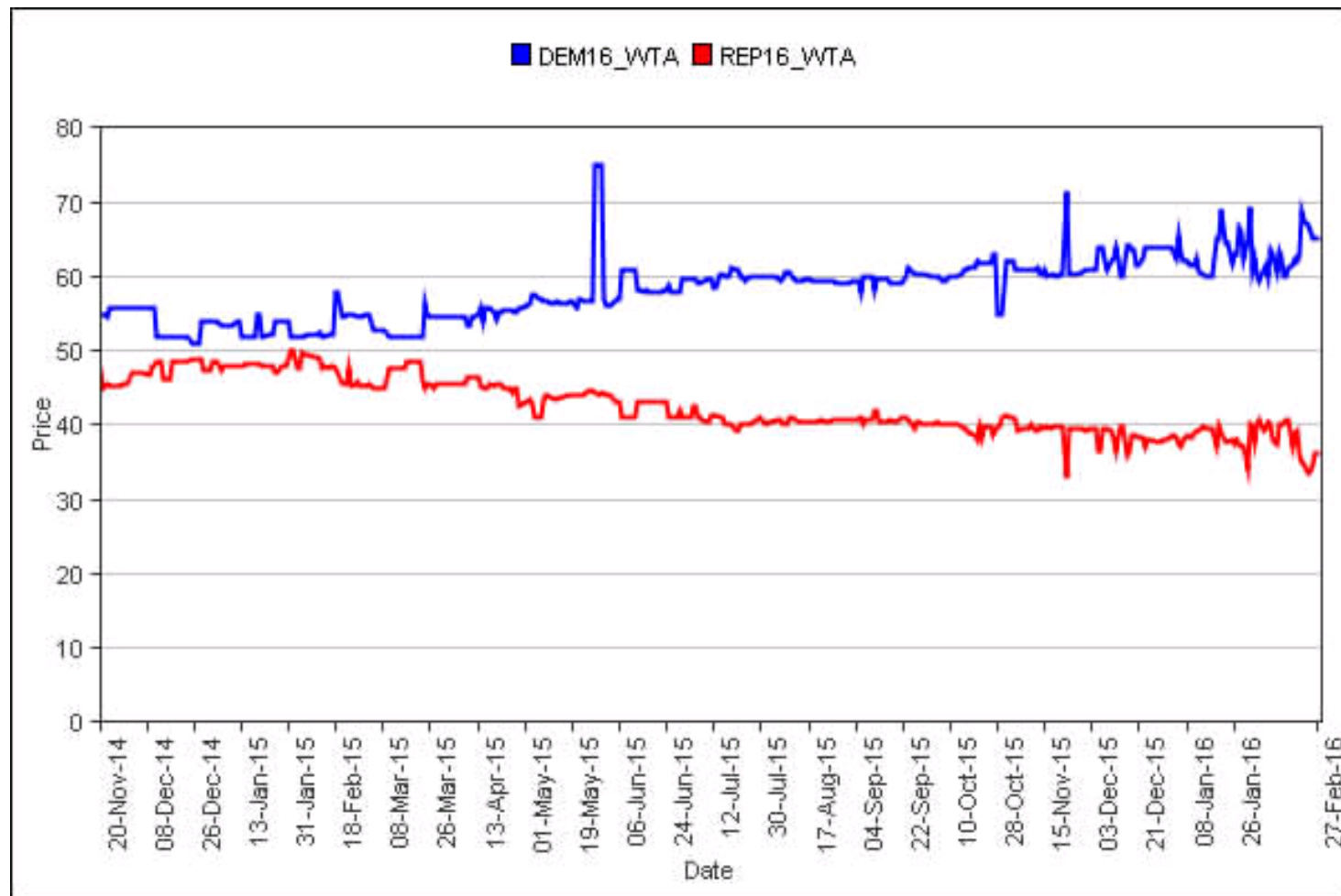
Who will win the 2016 Republican presidential nomination? (predictit.org)

RNOM16		Latest	Buy Yes	Sell Yes	Buy No	Sell No
	Donald Trump TRUMP.RNOM16	80¢ ↑ 3¢	80¢	78¢	22¢	20¢
	Marco Rubio RUBIO.RNOM16	18¢ ↓ 1¢	18¢	15¢	85¢	82¢
	Ted Cruz CRUZ.RNOM16	6¢ NC	6¢	5¢	95¢	94¢
	Mitt Romney ROMNEY.RNOM16	3¢ ↓ 1¢	4¢	3¢	97¢	96¢
	John Kasich KASICH.RNOM16	3¢ NC	5¢	3¢	97¢	95¢
	Paul Ryan RYAN.RNOM16	2¢ NC	3¢	2¢	98¢	97¢










Who will win the 2016 Democratic presidential nomination? (predictit.org)

DNOM16		Latest	Buy Yes	Sell Yes	Buy No	Sell No
	Hillary Clinton CLINTON.DNOM16	91¢ NC	91¢	90¢	10¢	9¢
	Bernie Sanders SANDERS.DNOM16	11¢ ↑ 1¢	11¢	10¢	90¢	89¢
	Joe Biden BIDEN.DNOM16	3¢ ↓ 1¢	4¢	3¢	97¢	96¢
	Elizabeth Warren WARREN.DNOM16	1¢ NC	2¢	None	None	98¢
	Martin O'Malley O'MALLEY.DNOM16	1¢ NC	1¢	None	None	99¢

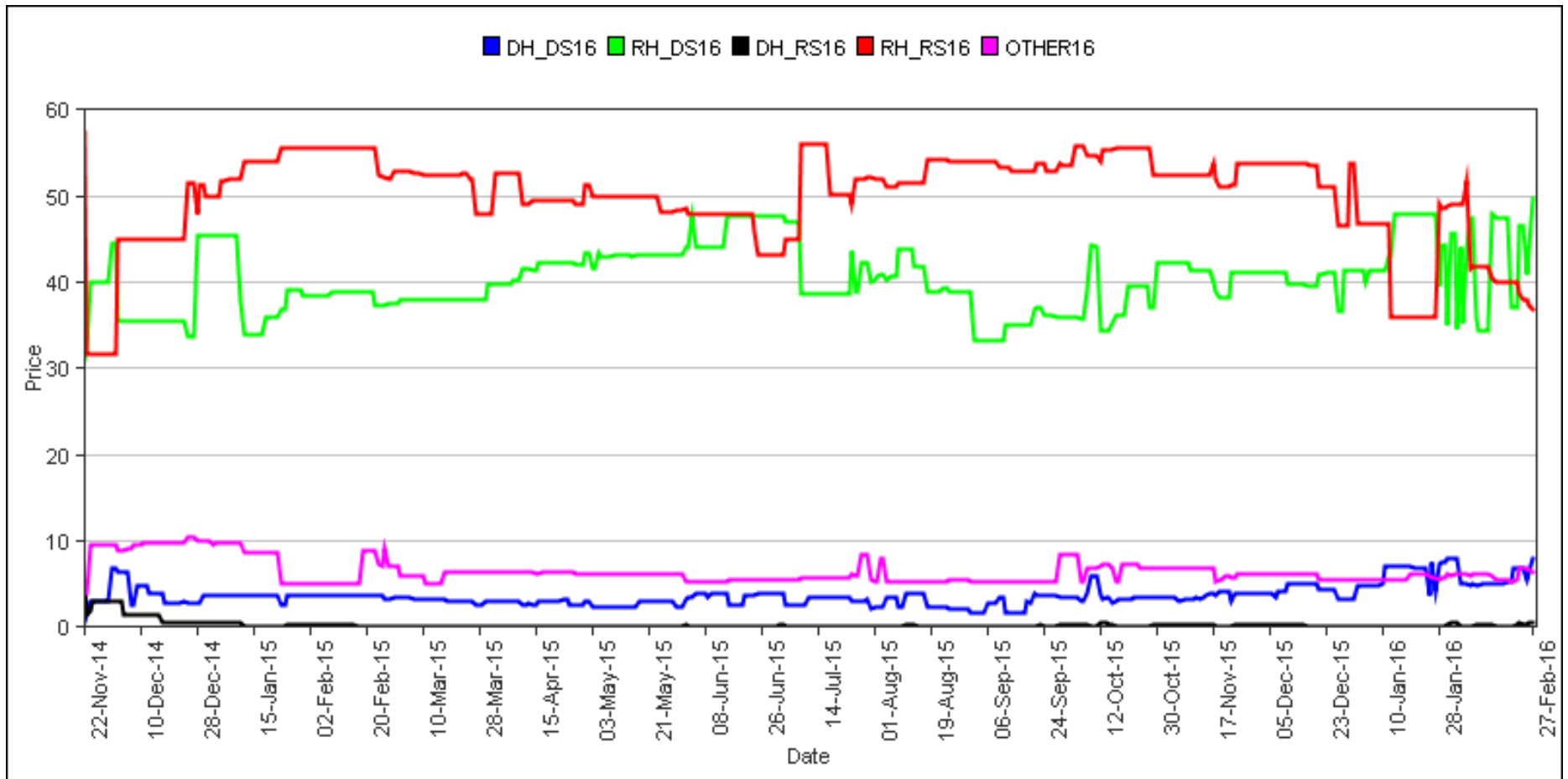
IEM Prediction Markets: Presidential Race



Who will win the 2016 presidential election? (predictit.org)

USPREZ16		Latest	Buy Yes	Sell Yes	Buy No	Sell No
	Hillary Clinton CLINTON.USPREZ16	60¢ ↑ 2¢	60¢	59¢	41¢	40¢
	Donald Trump TRUMP.USPREZ16	38¢ ↑ 2¢	38¢	37¢	63¢	62¢
	Marco Rubio RUBIO.USPREZ16	8¢ ↓ 2¢	9¢	8¢	92¢	91¢
	Bernie Sanders SANDERS.USPREZ16	8¢ ↑ 2¢	8¢	7¢	93¢	92¢
	Mitt Romney ROMNEY.USPREZ16	3¢ ↑ 2¢	3¢	1¢	99¢	97¢
	Joe Biden BIDEN.USPREZ16	2¢ NC	3¢	2¢	98¢	97¢
	Michael Bloomberg BLOOMBERG.USPREZ16	2¢ ↓ 1¢	4¢	3¢	97¢	96¢
	Ted Cruz CRUZ.USPREZ16	2¢ NC	3¢	2¢	98¢	97¢
	John Kasich KASICH.USPREZ16	1¢ NC	2¢	1¢	99¢	98¢

IEM Prediction Markets: Control of Congress



Possible Executive-Legislative Outcomes, (Very Loosely) Ranked by Likelihood

1. DEM President, DEM Senate, GOP House
2. DEM President, GOP Senate, GOP House
3. GOP President, DEM Senate, GOP House
4. GOP President, GOP Senate, GOP House

Notes

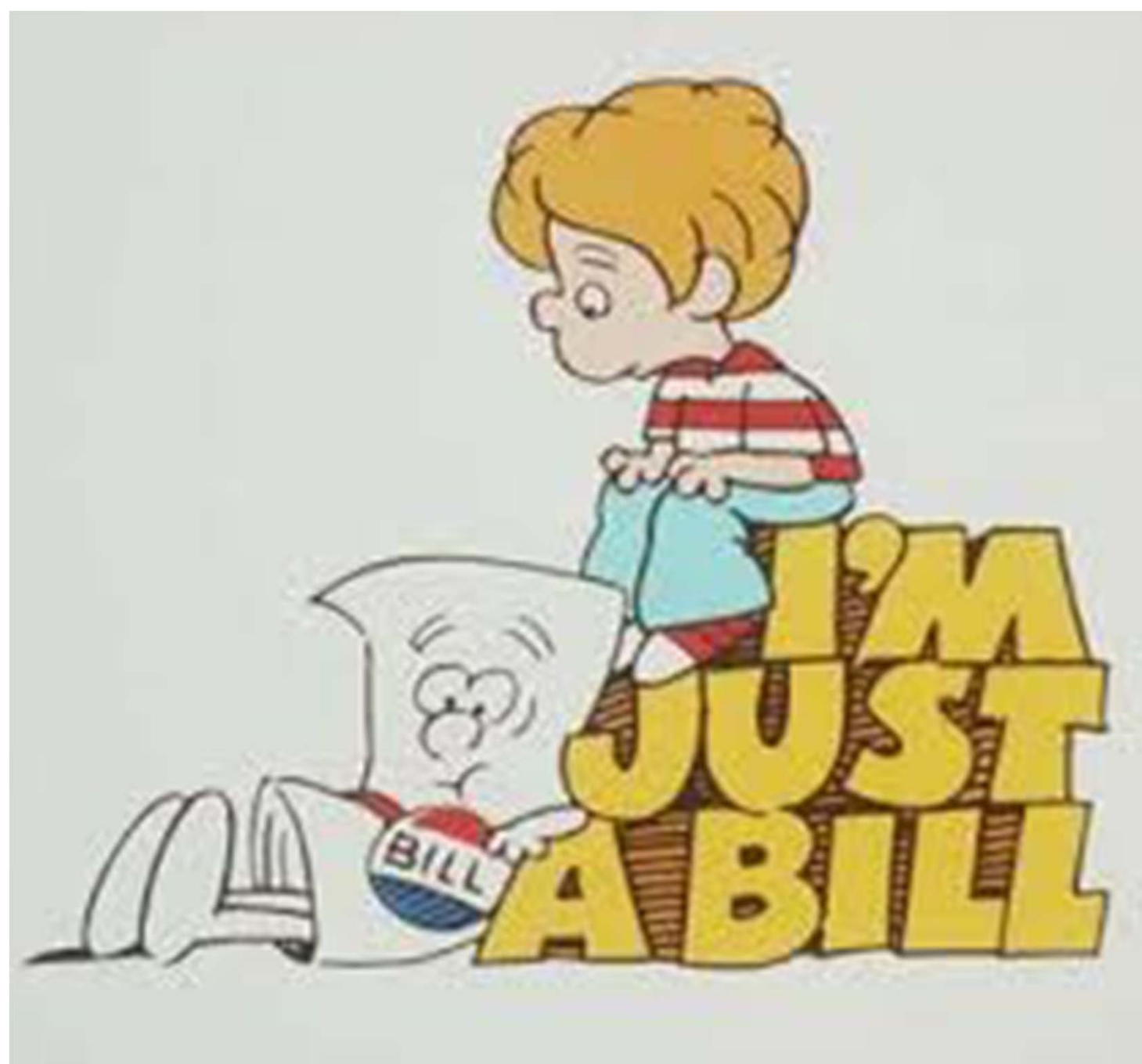
- the most likely outcomes feature divided government
- filibuster-proof Senate control very unlikely for either party
- close 2016 margins will likely accelerate the political salience of future elections (2018, 2020, etc...)

Possible Executive-Legislative Outcomes, (Very Loosely) Ranked by Likelihood

1. DEM President, DEM Senate, GOP House
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- 4. GOP President, GOP Senate, GOP House**

Notes

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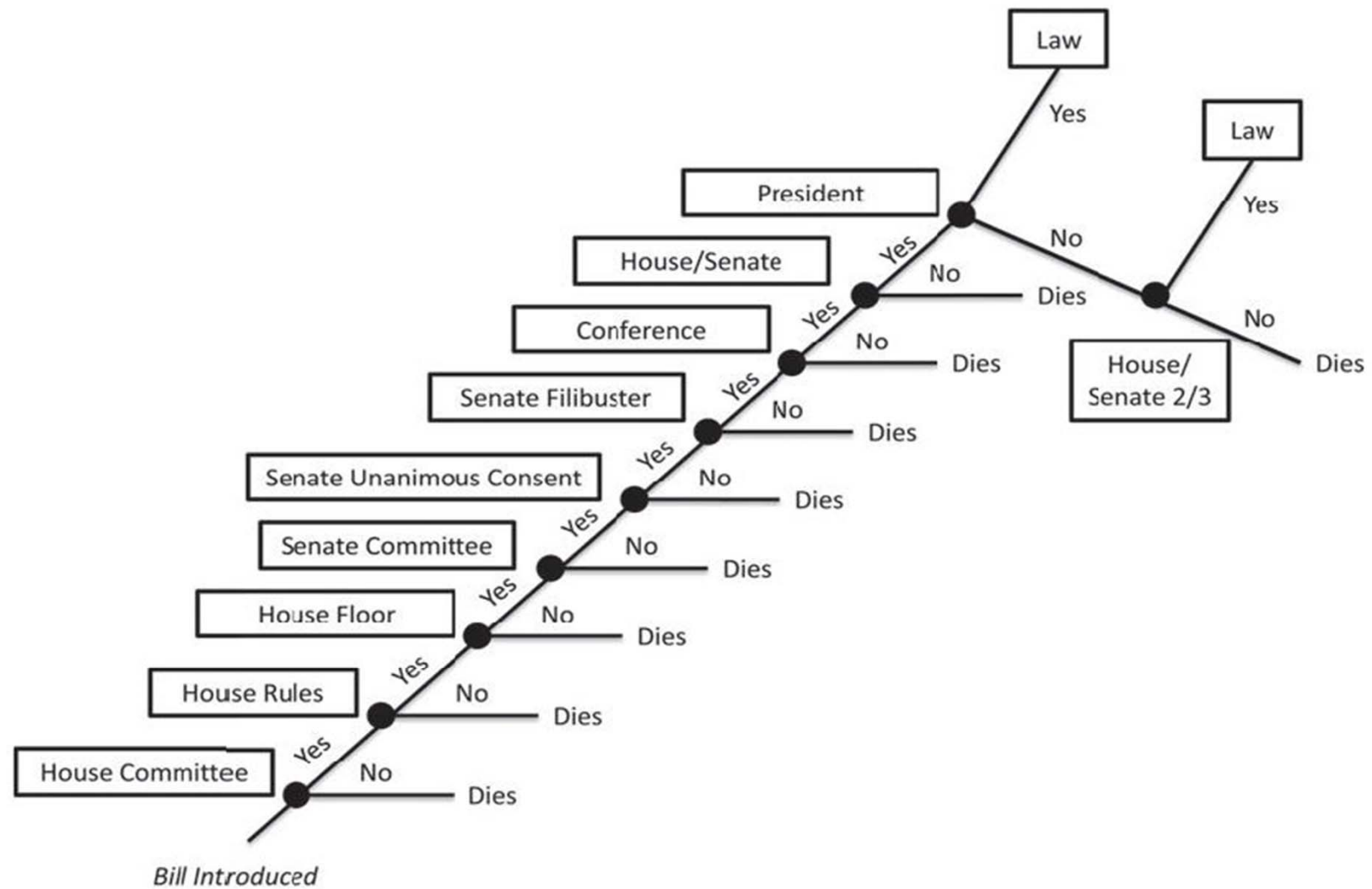


Figure 1. Veto Gates Model for Federal Legislation.

Source: Eskridge, Vetogates and American Public Law, J. Law & Econ Org. (2012)

Tax Reform Act of 2017?

- uncertainty re: influence of exogenous factors
 - significant changes in economic conditions
 - terrorist attacks
 - October surprises
- uncertainty re: logrolling, political compromise
- Safest predictions: incremental “reform”
 - *maybe* some movement on carried interest
 - *maybe* some new limitations on itemized deductions
 - *maybe* some reform of international tax rules
 - *maybe* some reduction in corporate tax rates
- Biggest unknown: what happens with GOP control of White House, Senate and House of Representatives?