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## AN ANALYSIS OF DONALD TRUMP'S REVISED TAX PLAN

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### ABSTRACT

This paper analyzes presidential candidate Donald Trump's revised tax proposal, which would significantly reduce marginal tax rates, increase standard deduction amounts, repeal personal exemptions, cap itemized deductions, and allow businesses to elect to expense new investment and not deduct interest expense. His proposal would cut taxes at all income levels, although the largest benefits, in dollar and percentage terms, would go to the highest-income households. Federal revenues would fall by \$6.2 trillion over the first decade before accounting for added interest costs and macroeconomic effects. Including those factors, the federal debt would rise by at least \$7.0 trillion over the first decade and by at least \$20.7 trillion by 2036.

An earlier version of this publication was released on October 11, 2016. This revised version includes macroeconomic estimates of Donald Trump's revised tax plan, modeled in partnership with the Penn Wharton Budget Model. We provide dynamic scoring estimates of Trump's tax proposals using two new models: TPC's short-term Keynesian Model and the Penn Wharton Budget Model's Overlapping Generations Model.

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*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.*

In speeches on August 8, September 13, and September 15, 2016, Republican presidential candidate Donald Trump described his new framework for a revised tax plan. The proposal would reduce tax rates, simplify many provisions, and reform business taxation.<sup>1</sup> The revised framework, as set out in those speeches and campaign publications and statements, leaves many important details unspecified. We needed to make many assumptions about these unspecified details to analyze the plan (appendix A).

The Urban-Brookings Tax Policy Center (TPC) estimates that a plan consistent with the revised Trump tax plan would reduce federal revenue by \$6.2 trillion over the first decade of implementation and by an additional \$8.9 trillion in the second decade.<sup>2</sup> Three-fourths of the revenue loss would come from reductions in business taxes. These revenue estimates do not consider interest costs or macroeconomic feedback effects.

TPC, in collaboration with the Penn Wharton Budget Model (PWBM), also prepared two sets of estimates of the revised Trump plan that take into account macroeconomic feedback effects.<sup>3</sup> Both sets of estimates indicate that the plan would boost gross domestic product (GDP) in the short run, reducing the revenue cost of the plan. However, including interest costs, the federal debt would increase by at least \$7.0 trillion over ten years, even with these positive macroeconomic feedback effects on revenues. By 2024, the PWBM indicates that GDP would be smaller than it would be otherwise because growing budget deficits would push up interest rates and crowd out investment, and the federal debt would increase by \$22.1 trillion by 2036. These estimates are sensitive to assumptions about how savings, investment, and labor supply would respond to policy changes such as the Trump plan, so the effects on GDP could be larger or smaller in both the short- and the long-run. Trump, however, promises unspecified spending cuts and also argues that other elements of his economic plan would boost tax revenues, which could negate some or all of the negative effects of rising deficits.

The plan would cut taxes at every income level, 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 \$2,940, increasing after-tax income by 4.1 percent. However, the highest-income taxpayers (0.1 percent of the population, or those with incomes over \$3.7 million in 2016 dollars) would experience an average tax cut of nearly \$1.1 million, over 14 percent of after-tax income. Households in the middle fifth of the income distribution would receive an average tax cut of \$1,010, or 1.8 percent of after-tax income, while the poorest fifth of households would see their taxes go down an average of \$110, or 0.8 percent of their after-tax income.

The revised Trump plan would reduce the top individual income tax rate to 33 percent, reduce the corporate rate to 15 percent, and allow owners of pass-through businesses (such as sole proprietorships, partnerships, and S corporations) to elect to be taxed at a flat rate of 15 percent rather than under the regular individual income tax rates. Capital gains and dividends would be taxed under the current preferential rate structure. Distributions from “large” pass-through businesses received by owners who elected the 15 percent flat rate would be taxed as dividends.

The plan would increase the standard deduction and add a new deduction and other tax benefits for child and dependent care. It would repeal personal exemptions and the head of household filing status, and cap itemized deductions. The plan would also eliminate the alternative minimum tax (AMT) and the net investment income tax enacted as part of the Affordable Care Act (ACA). The plan would eliminate the estate and gift taxes, but would tax capital gains (above a large exemption amount) at death.

Both corporate and pass-through businesses could elect to immediately deduct (i.e., expense) investment, but would then not be allowed to deduct interest expenses. The plan would also repeal certain business tax expenditures.

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 US and reduce tax distortions in the allocation of capital. Increased investment could raise labor productivity and US wages by increasing capital per worker. However, increased government borrowing could push up interest rates and crowd out private investment, thereby offsetting some or all of 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.

## **MAJOR ELEMENTS OF THE PROPOSAL**

### ***Individual Income Tax***

The revised Trump plan would consolidate the regular standard deduction, additional standard deductions for age or blindness, and the personal exemptions for tax filers and dependents into new standard deduction amounts of \$15,000 for single filers and \$30,000 for joint filers. The head of household filing status would be repealed.

The plan would reduce the number of individual income tax brackets from the current seven to three: 12, 25, and 33 percent, cutting the top 39.6 percent rate by 6.6 percentage points (table 1). The special rate structure for capital gains and dividends would be retained, but the 3.8 percent net investment income tax rate that currently applies to capital gains and dividends would be repealed (see below).

The plan would also add a new deduction for child and dependent care expenses, and increase the earned income tax credit (EITC) for working parents who would not benefit from the deduction. Further, the plan would provide a new form of tax-favored savings account related to child and dependent care expenses, and expand the credit for employer-provided child care.

**TABLE 1**

**Tax Rates under Current Law and under Revised Trump Plan**  
Among tax filers claiming the standard deduction, 2016<sup>a</sup>



Single filers				Childless married couples filing jointly			
Adjusted gross income (\$)		Current marginal rate (%)	Trump marginal rate (%)	Adjusted gross income (\$)		Current marginal rate (%)	Trump marginal rate (%)
Over	But not over			Over	But not over		
0	10,350 <sup>b</sup>	0	0	0	20,700 <sup>b</sup>	0	0
10,350	15,000	10	0	20,700	30,000	10	0
15,000	19,625	10	12	30,000	39,250	10	12
19,625	48,000	15	12	39,250	96,000	15	12
48,000	52,500	25	12	96,000	105,000	25	12
52,500	101,500	25	25	105,000	172,600	25	25
101,500	127,500	28	25	172,600	252,150	28	25
127,500	200,500	28	33	252,150	255,000	33	25
200,500	423,700	33	33	255,000	433,750	33	33
423,700	425,400	35	33	433,750	487,650	35	33
425,400	and over	39.6	33	487,650	and over	39.6	33

**Source:** Urban-Brookings Tax Policy Center based on the revised Trump plan and IRS tax brackets.

<sup>a</sup> Tax filers who itemize deductions would not benefit from the revised Trump plan's increase in the standard deduction and would thus face tax brackets different from those shown in this table.

<sup>b</sup> 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 personal exemptions, into the higher standard deduction of \$15,000 for single filers and \$30,000 for married couples filing jointly under the revised Trump plan).

The plan would cap the total amount of itemized deductions that could be claimed at \$100,000 for single filers and \$200,000 for joint filers. The plan would also repeal the individual AMT and amend the taxation of "carried interest," the income of certain investment managers that is currently treated as preferentially taxed capital gains. Under

the proposal, carried interest would be treated as labor income subject to ordinary income tax and payroll tax. However, hedge funds and private equity partnerships, which earn a substantial portion of income in the form of carried interest, would qualify for the special 15-percent business tax rate and thus would retain a substantial tax advantage on their income compared with wage earners.

Increasing the standard deduction would significantly reduce the number of filers who itemize. We estimate that 27 million (60 percent) of the 45 million filers who would otherwise itemize in 2017 would opt for the standard deduction. Repealing personal exemptions and the head of household filing status, however, would cause many large families and single parents to face tax increases.

### ***Estate and Gift Taxes***

The revised Trump plan would eliminate the federal estate, gift and generation-skipping transfer taxes. The plan would also tax capital gains held until death, with an exemption of \$5 million (\$10 million for married couples).<sup>4</sup>

Eliminating the estate tax would remove several economic distortions (such as the incentive it creates to spend down asset balances below the threshold for taxation). However, eliminating the estate tax would also remove the incentive it provides for the wealthy to make charitable contributions.<sup>5</sup> Taxing the capital gains of wealthy decedents at death would reduce the incentive for wealthy individuals to hold on to appreciated assets until death to escape capital gains tax.

### ***Business Taxes***

The revised Trump plan would cut the top corporate tax rate from 35 percent to 15 percent. Owners of pass-through entities (sole proprietorships, partnerships, and S corporations) could elect to be taxed at a flat rate of 15 percent on their pass-through income rather than under regular individual income tax rates (the top rate would be 33 percent under the plan, compared with 39.6 percent under current law). However, distributions from “large” pass-through businesses received by owners who elected the 15 percent flat rate would be taxed as dividends.<sup>6</sup>

The 18 percentage point differential between the top rate on pass-through business income and wages would 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 compensation in the form of wages. The revised Trump plan does not specify any rules or enforcement mechanisms that might limit the number of employees who would

redefine themselves as sole proprietors or other pass-through businesses in order to benefit from the 15 percent business tax rate.<sup>7</sup> Current-law rules are difficult to enforce, leading to significant avoidance of payroll taxes; with the much larger rate differential under the revised Trump plan, avoidance would be much more prevalent.<sup>8</sup> For purposes of our analysis, we have assumed that eventually half (50 percent) of high-wage workers would become pass-through entities.<sup>9</sup>

Both corporations and pass-through businesses could elect to expense investment in equipment, structures, and inventories, rather than depreciating these purchases over time as current law requires. Businesses that elect expensing would not be allowed to deduct interest expenses. The revised Trump plan does not provide any details on how the disallowance of interest expense for businesses that elect expensing would be implemented. For purposes of our analysis, we have assumed that half of the interest on new business loans would not be deductible.

The plan would impose a tax on the existing unrepatriated earnings of US firms' foreign subsidiaries. Earnings held in cash would be taxed at 10 percent and other earnings at 4 percent, with the liability for this one-time tax payable over 10 years.

The large reduction in the corporate rate would reduce the incentive for firms to recharacterize their domestic income as foreign-source to avoid US tax. The lower corporate tax rate would also decrease the incentive for a US corporation to move its tax residence overseas (a so-called corporate inversion).

The plan would repeal the corporate AMT and certain business tax expenditures.<sup>10</sup>

### ***ACA Taxes***

Mr. Trump has proposed repealing the entire ACA, including all of the ACA taxes. However, his tax plan would specifically repeal only the 3.8 percent tax on net investment income, and we have included only the repeal of that tax in our analysis.<sup>11</sup>

## **IMPACT ON REVENUE, DISTRIBUTION, AND COMPLEXITY**

### ***Impact on Revenue***

We estimate that the Trump plan would reduce federal receipts by \$6.2 trillion between 2016 and 2026 (table 2) before accounting for macroeconomic feedback effects.<sup>12</sup> About three-fourths of the revenue loss would come from business tax provisions. Corporations

would pay less tax than they do now because their top rate would be reduced to 15 percent and the corporate AMT would be repealed. Pass-through businesses taxed under the individual income tax would pay less because they could elect a flat 15 percent rate. All businesses could elect to expense investment, a benefit which would partially be offset by the loss of interest deductions (for businesses that elected expensing), repeal of some tax expenditures, and, for multinational corporations, the tax on unrepatriated foreign income.

The remainder of the revenue loss would result primarily from net cuts in non-business individual income taxes. Reductions in income tax rates, repeal of the net investment income tax, and repeal of the individual AMT would all lose revenue. The increase in standard deduction amounts and the new child and dependent care provisions would also lose revenue, but these losses would be more than offset by the repeal of personal exemptions and head of household filing status, and the cap on itemized deductions.

Repealing the estate and gift taxes and taxing capital gains (above a \$5 million per person exemption) at death would result in a net revenue loss of \$174 billion over the budget period.

We estimate that the tax changes would reduce revenues by \$8.9 trillion in the second decade (2027–2036). While the revenue loss would be much larger in nominal terms than in the first 10 years, it represents the same share of cumulative GDP, 2.6 percent.

The revenue losses understate the effect on the national debt because they exclude the additional interest that would accrue because of increased debt. Including interest, the proposal would add \$7.2 trillion to the national debt by 2026 and \$20.9 trillion by 2036 (table 3). If the tax cuts were not offset by spending cuts, we estimate the national debt would rise by over 26 percent of GDP by 2026 and over 50 percent of GDP by 2036.

TABLE 2

## Estimated Effect of Revised Trump Plan on Tax Receipts

\$ billions, FY 2016–36



Provision	Fiscal Year							
	2016	2017	2018	2019	2020	2021	2016–26	2027–36
<b>Individual income and payroll taxes</b>								
Repeal net investment income tax	-5.6	0.9	-2.5	-12.3	-15.4	-16.1	-144.5	-279.4
Repeal alternative minimum tax	0.0	-24.1	-33.5	-36.0	-38.7	-41.4	-412.8	-699.3
Repeal head of household filing status	0.0	8.1	11.3	11.8	12.3	12.8	130.5	209.8
Repeal personal exemptions	0.0	132.9	180.5	186.1	192.4	200.4	1,999.7	2,870.6
Individual income tax rates of 12, 25, and 33 percent	0.0	-90.0	-125.4	-131.4	-138.2	-144.5	-1,490.4	-2,512.5
Increase standard deduction to \$15,000 (\$30,000 married), indexed for inflation after 2016	0.0	-118.9	-160.4	-163.3	-165.2	-168.8	-1,688.4	-2,263.9
Cap itemized deductions at \$100,000 (\$200,000 married), indexed for inflation after 2016	0.0	29.7	42.8	46.4	49.9	53.5	558.6	1,020.8
Childcare provisions	0.0	-8.3	-11.4	-11.9	-12.5	-13.0	-131.5	-204.8
Elective flat rate of 15 percent on pass-through income; distributions from large pass-throughs taxed as dividends	0.0	-54.2	-74.5	-78.1	-83.7	-87.9	-894.6	-1,423.3
Shifting of wages and salaries to business income	0.0	-6.3	-16.1	-27.8	-40.2	-53.2	-648.9	-1,915.5
Allow expensing of all investment (except land) and disallow interest deduction for pass-throughs that expense	0.0	-71.6	-89.9	-83.5	-79.1	-77.1	-689.2	-276.5
Tax carried interests as ordinary business income	0.0	0.1	0.9	1.0	1.1	1.2	10.3	12.3
Repeal certain pass-through business tax expenditures	0.0	3.3	5.2	5.7	5.8	6.1	58.0	76.4
<b>Total for individual income and payroll taxes</b>	<b>-5.6</b>	<b>-198.3</b>	<b>-273.1</b>	<b>-293.3</b>	<b>-311.4</b>	<b>-327.9</b>	<b>-3,343.3</b>	<b>-5,385.1</b>
<b>Corporate income tax</b>								
Reduce corporate rate to 15% and repeal the corporate AMT	0.0	-102.4	-207.6	-233.4	-248.0	-246.5	-2,354.8	-3,513.8
Allow expensing of all investment (except land) and disallow interest deduction for corporations that expense	0.0	-55.3	-98.6	-91.8	-84.5	-75.1	-592.8	-98.9
Deemed repatriation over 10 years of accumulated untaxed pre-2017 earnings of CFCs, with reduced rates	0.0	7.1	14.2	15.8	15.8	15.8	147.8	10.3
Repeal certain corporate tax expenditures	0.0	4.8	10.2	12.6	14.2	15.9	167.0	371.1
<b>Total for corporate income tax revenues</b>	<b>0.0</b>	<b>-145.9</b>	<b>-281.7</b>	<b>-296.7</b>	<b>-302.4</b>	<b>-289.8</b>	<b>-2,632.8</b>	<b>-3,231.4</b>
<b>Estate and gift taxes</b>								
Repeal the estate, gift and GST taxes; tax capital gains at death with \$5 million exemption	0.0	3.1	-9.9	-17.2	-18.9	-19.5	-174.2	-324.5
<b>Total for estate and gift tax revenues</b>	<b>0.0</b>	<b>3.1</b>	<b>-9.9</b>	<b>-17.2</b>	<b>-18.9</b>	<b>-19.5</b>	<b>-174.2</b>	<b>-324.5</b>
<b>Total revenue effect of all provisions</b>								
<b>Total revenue change before macro feedback (sum of amounts above)</b>	<b>-5.6</b>	<b>-341.0</b>	<b>-564.7</b>	<b>-607.2</b>	<b>-632.7</b>	<b>-637.3</b>	<b>-6,150.4</b>	<b>-8,941.0</b>
<b>Total revenue change after macro feedback (dynamic score)</b>								
<b>TPC Keynesian model estimates</b>	<b>-5.6</b>	<b>-288.0</b>	<b>-529.8</b>	<b>-589.7</b>	<b>-622.0</b>	<b>-635.0</b>	<b>-6,031.9</b>	<b>-8,941.0</b>
<b>PWBM overlapping generations model estimates</b>	<b>-5.6</b>	<b>-298.5</b>	<b>-520.5</b>	<b>-572.4</b>	<b>-603.3</b>	<b>-613.7</b>	<b>-5,972.1</b>	<b>-10,312.2</b>
<b>Exhibit: Difference in total revenue change due to macro feedback</b>								
TPC Keynesian model estimates	0.0	53.1	34.9	17.5	10.7	2.3	118.4	0.0
PWBM overlapping generations model estimates	0.0	42.5	44.2	34.8	29.5	23.6	178.3	-1,371.2

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.

Notes: AMT = alternative minimum tax; CFC = controlled foreign corporation; GST = generation-skipping transfer.



TABLE 3

Effect of Revised Trump Plan on Federal Revenues, Deficits, and the Debt  
FY 2016–36

	Fiscal Year												
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2016–26	2027–36
<b>Estimates before macro feedback</b>													
Revenue loss <sup>a</sup> (\$ billions)	5.6	341.0	564.7	607.2	632.7	637.3	634.2	645.4	666.3	691.8	724.2	6,150.4	8,941.0
As a percentage of GDP (%)	0.0	1.8	2.8	2.9	2.9	2.8	2.7	2.6	2.6	2.6	2.6	2.6	2.6
Additional interest (\$ billions)	0.0	3.9	15.0	39.5	63.5	89.6	116.0	144.0	173.4	204.7	237.8	1,087.4	4,751.4
Increase in deficit (\$ billions)	5.6	345.0	579.7	646.7	696.2	726.9	750.2	789.4	839.7	896.4	962.0	7,237.8	13,692.4
Increase in debt <sup>b</sup> (\$ billions)	5.6	350.6	930.3	1,577.1	2,273.2	3,000.1	3,750.3	4,539.6	5,379.3	6,275.8	7,237.8	7,237.8	20,930.2
<b>Cumulative increase in debt relative to GDP (%)</b>	<b>0.0</b>	<b>1.8</b>	<b>4.6</b>	<b>7.5</b>	<b>10.5</b>	<b>13.3</b>	<b>15.9</b>	<b>18.5</b>	<b>21.1</b>	<b>23.6</b>	<b>26.2</b>	<b>26.2</b>	<b>50.4</b>
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
<b>Estimates after macro feedback from TPC Keynesian model</b>													
Revenue loss <sup>a</sup> (\$ billions)	5.6	288.0	529.8	589.7	622.0	635.0	634.2	645.4	666.3	691.8	724.2	6,031.9	8,941.0
As a percentage of GDP (%)	0.0	1.5	2.6	2.8	2.9	2.8	2.7	2.6	2.6	2.6	2.6	2.6	2.6
Additional interest (\$ billions)	5.6	292.5	546.6	631.2	686.2	721.7	745.7	784.7	834.8	891.3	956.7	7,097.1	13,632.6
Increase in deficit (\$ billions)	5.6	292.5	546.6	631.2	686.2	721.7	745.7	784.7	834.8	891.3	956.7	7,097.1	13,632.6
Increase in debt <sup>b</sup> (\$ billions)	5.6	298.2	844.7	1,475.9	2,162.2	2,883.9	3,629.6	4,414.3	5,249.1	6,140.5	7,097.1	7,097.1	20,729.8
<b>Cumulative increase in debt relative to GDP (%)</b>	<b>0.0</b>	<b>1.5</b>	<b>4.2</b>	<b>7.0</b>	<b>9.9</b>	<b>12.8</b>	<b>15.4</b>	<b>18.0</b>	<b>20.6</b>	<b>23.1</b>	<b>25.7</b>	<b>25.7</b>	<b>49.9</b>
Addendum: GDP (end of period; \$ billions)	18,493.8	19,620.0	20,338.8	21,011.7	21,774.7	22,607.0	23,527.5	24,497.2	25,505.6	26,559.2	27,660.0	27,660.0	41,511.7
<b>Estimates after macro feedback from PWBM overlapping generations model</b>													
Revenue loss <sup>a</sup> (\$ billions)	5.6	298.5	520.5	572.4	603.3	613.7	617.1	635.1	664.1	698.5	743.2	5,972.1	10,312.2
As a percentage of GDP (%)	0.0	1.5	2.6	2.7	2.8	2.7	2.6	2.6	2.6	2.6	2.7	2.6	3.0
Additional interest (\$ billions)	0.0	3.4	13.5	36.2	58.8	83.7	109.1	136.3	165.2	196.2	229.5	1,031.9	4,826.1
Increase in deficit (\$ billions)	5.6	302.0	534.0	608.6	662.1	697.4	726.2	771.4	829.3	894.7	972.7	7,004.0	15,138.4
Increase in debt <sup>b</sup> (\$ billions)	5.6	307.6	841.6	1,450.2	2,112.2	2,809.7	3,535.9	4,307.3	5,136.6	6,031.3	7,004.0	7,004.0	22,142.4
<b>Cumulative increase in debt relative to GDP (%)</b>	<b>0.0</b>	<b>1.6</b>	<b>4.1</b>	<b>6.9</b>	<b>9.7</b>	<b>12.4</b>	<b>15.0</b>	<b>17.6</b>	<b>20.1</b>	<b>22.8</b>	<b>25.4</b>	<b>25.4</b>	<b>55.5</b>
Addendum: GDP (end of period; \$ billions)	18,493.8	19,484.7	20,350.3	21,097.8	21,870.1	22,715.6	23,609.1	24,534.3	25,495.1	26,491.0	27,527.5	27,527.5	39,868.4

Sources: Urban-Brookings Tax Policy Center (TPC) Microsimulation Model (version 0516-1); Congressional Budget Office (2016a, 2016b); TPC Keynesian model; Penn Wharton Budget Model (PWBM) overlapping generations model.

<sup>a</sup> Revenue loss is expressed as the effect on the deficit.

<sup>b</sup> Increase in debt equals the cumulative increase in deficit plus additional interest on the debt.

Taking macroeconomic feedback effects into account, the ratio of additional debt to GDP would be somewhat smaller, but still rise to 25.4 percent by 2026 and by 49.9 percent by 2036 (table 3). The long-run PWBM model estimates that after 2023, revenues and GDP fall below the levels estimated without macro feedback, so the ratio of debt to GDP would climb more rapidly in later years. Unspecified spending cuts, which we did not model, could offset some of the effects of rising debt on GDP growth.

Mr. Trump and his campaign believe that his proposals on trade, regulatory, and energy policy reform would raise economic output and sufficient revenues to offset most of the remaining revenue losses from his revised tax plan (Trump 2016c, Navarro and

Ross 2016). Some independent analysts, however, believe his economic policies would reduce economic output (Zandi and coauthors 2016; Noland and coauthors, 2016).

### ***Impact on Distribution***

The proposal would reduce average taxes throughout the income distribution, though as noted above, some filers would face tax increases.<sup>13</sup> Overall, taxes would decrease by an average of \$2,940, or 4.1 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 fifth of the distribution—would receive an average tax cut of \$16,660 (a 6.6 percent increase in after-tax income), the top 1 percent an average tax cut nearly 13 times larger (\$214,690, or 13.5 percent of after-tax income), and the top 0.1 percent an average tax cut approaching \$1.1 million (14.2 percent of after-tax income). In contrast, the average tax cut for the lowest-income households would be \$110, 0.8 percent of after-tax income. Middle-income households would receive an average tax cut of \$1,010, or 1.8 percent of after-tax income.

Mr. Trump's revised tax plan would provide larger nominal tax cuts in 2025—averaging \$4,020. These cuts would likewise represent a larger share (4.3 percent) of after-tax income than in 2017 (table 5 and figure 1). On average, households in the bottom two quintiles would see their after-tax income rise by less than 1.0 percent and households in the next two quintiles by less than 2.0 percent, while households in the top quintile would have tax cuts averaging 7.3 percent of after-tax income. The highest-income households (top 0.1 percent) would receive a much larger nominal average tax cut than in 2017 (about \$1.5 million), but it would represent a slightly smaller share (14.0 percent) of their after-tax income than during the first 10 years.

TABLE 4

## Distribution of Federal Tax Change

By expanded cash income percentile, 2017<sup>a</sup>



Expanded cash income percentile <sup>b,c</sup>	Percent change in after-tax income (%) <sup>d</sup>	Share of total federal tax change (%)	Average federal tax change (\$)	Average Federal Tax Rate <sup>e</sup>	
				Change (% points)	Under the proposal (%)
Lowest quintile	0.8	1.1	-110	-0.8	2.9
Second quintile	1.2	3.0	-400	-1.1	7.3
Middle quintile	1.8	6.6	-1,010	-1.5	12.1
Fourth quintile	2.2	11.3	-2,030	-1.8	15.5
Top quintile	6.6	77.7	-16,660	-4.9	21.2
All	4.1	100.0	-2,940	-3.3	16.8
<b>Addendum</b>					
80–90	2.3	7.9	-3,270	-1.9	18.3
90–95	2.8	6.2	-5,350	-2.1	20.0
95–99	6.0	16.3	-18,490	-4.5	21.0
Top 1 percent	13.5	47.3	-214,690	-9.0	24.4
Top 0.1 percent	14.2	24.2	-1,066,460	-9.3	25.1

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

Note: Number of AMT taxpayers (millions): Baseline: 4.8; Proposal: 0.

<sup>a</sup> Calendar year. Baseline is current law. Proposal includes individual, payroll, corporate, and estate provisions in the revised Trump tax plan. <http://www.taxpolicycenter.org/taxtopics/Baseline-Definitions.cfm>.

<sup>b</sup> The percentile includes both filing and nonfiling 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>.

<sup>c</sup> 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.

<sup>d</sup> 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.

<sup>e</sup> 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.

TABLE 5

## Distribution of Federal Tax Change By expanded cash income percentile, 2025<sup>a</sup>



Expanded cash income percentile <sup>b,c</sup>	Percent change in after-tax income (%) <sup>d</sup>	Share of total federal tax change (%)	Average federal tax change (\$)	Average Federal Tax Rate <sup>e</sup>	
				Change (% points)	Under the proposal (%)
Lowest quintile	0.7	0.8	-120	-0.6	3.7
Second quintile	0.9	2.2	-390	-0.8	8.0
Middle quintile	1.5	5.4	-1,090	-1.3	12.8
Fourth quintile	1.8	8.6	-2,120	-1.5	15.7
Top quintile	7.3	82.8	-24,440	-5.4	20.9
All	4.3	100.0	-4,020	-3.4	16.8
<b>Addendum</b>					
80–90	1.9	6.0	-3,380	-1.5	18.5
90–95	2.9	5.9	-7,170	-2.3	19.6
95–99	8.0	20.1	-31,610	-6.0	19.5
Top 1 percent	14.1	50.8	-317,100	-9.4	24.1
Top 0.1 percent	14.0	24.5	-1,459,720	-9.3	24.8

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

Note: Number of AMT taxpayers (millions): Baseline: 5.6; Proposal: 0.

<sup>a</sup> Calendar year. Baseline is current law. Proposal includes individual, payroll, corporate, and estate provisions in the revised Trump tax plan. <http://www.taxpolicycenter.org/taxtopics/Baseline-Definitions.cfm>.

<sup>b</sup> The percentile includes both filing and nonfiling 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>.

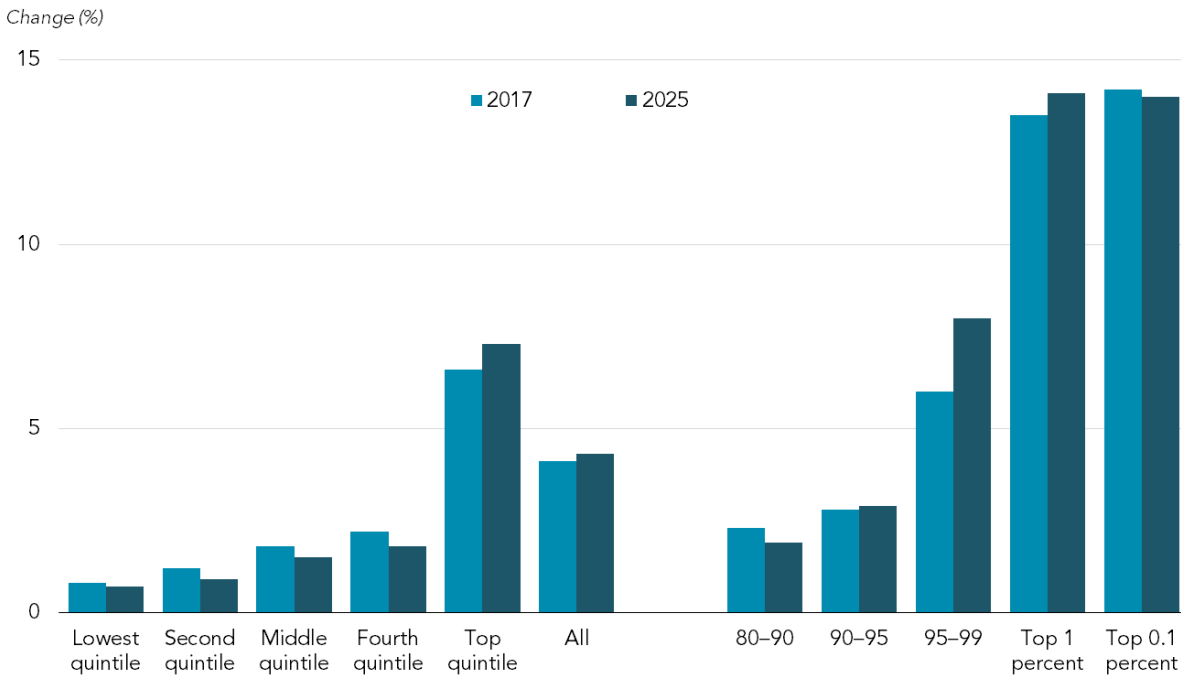
<sup>c</sup> The income percentile classes used in this table are based on the income distribution for the entire population and contain an equal number of people, not tax units. The breaks are (in 2016 dollars): 20% \$26,900; 40% \$52,300; 60% \$89,300; 80% \$149,900; 90% \$219,700; 95% \$299,500; 99% \$774,300; 99.9% \$4,760,500.

<sup>d</sup> 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.

<sup>e</sup> 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.

FIGURE 1

## Percent Change in After-Tax Income under Revised Trump Plan By expanded cash income percentile, 2017 and 2025



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

### *Impact on Complexity*

Mr. Trump's revised tax plan would simplify the tax code in several ways, but it would also create some new complexities. By significantly increasing the standard deduction and repealing personal exemptions, the plan would reduce record-keeping and reporting requirements. The number of itemizers would drop 60 percent to 27 million in 2017. Eliminating the head of household filing status, the complex AMT, and the ACA's 3.8 percent rate on net investment income would also simplify tax preparation. For some businesses, the proposal to elect expensing and the elimination of certain tax expenditures would simplify record keeping and tax preparation.

Some elements of the plan could add complexity, however. For example, new rules would be required to address high-wage earners' strong incentive to become pass-through entities. Businesses that elect expensing would lose their interest deductions, making investment decisions more complicated and encouraging complex financing arrangements that isolate investment and borrowing activities over time or in separate entities. The proposed tax benefits for child and dependent care would require parents to choose among more ways to claim tax savings by adding a new deduction and tax credit

for low-income families to the current credit and exclusion for care through a cafeteria plan.

## DYNAMIC EFFECTS ON THE ECONOMY

In addition to conventional estimates, which are based on fixed macroeconomic assumptions, TPC also prepared, in collaboration with PWBM, a set of estimates of the revised Trump plan that take into account macroeconomic feedback effects.<sup>14</sup> 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 the different ways tax policy can influence the economy. Estimates using the TPC Keynesian model illustrate how the impact of the plan 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.<sup>15</sup>

The Penn Wharton Budget Model is a state of the art tool to estimate the economic effects of tax policy, but like any economic model it is an imperfect representation of the economy that we expect to evolve and improve. Therefore, these estimates (like our “static” revenue estimates) are subject to revision and improvement over time.

### *Impact on Aggregate Demand*

The revised Trump 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 would increase spending proportionately less than lower-income households in response to an increase in after-tax income. Second, the provision allowing businesses to elect 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 several years, until actions by the Federal Reserve and equilibrating forces in the economy returned output to its long-run potential level.

TPC’s Keynesian model takes into account how tax and spending policies alter demand for goods and services—and therefore output—and how close the economy is to

full capacity. Using this model, we estimate that the changes in aggregate demand generated by the revised Trump tax plan would boost the level of output by about 1.7 percent in 2017, by 1.1 percent in 2018, and by smaller amounts in later years (table 6).

**TABLE 6**  
Dynamic Effects of Revised Trump Plan on GDP  
FY 2016–36



	Fiscal Year												
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2016–26 <sup>a</sup>	2027–36 <sup>a</sup>
	GDP (\$ billions)												
<b>Before macro feedback</b>	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
<b>After macro feedback</b>													
TPC Keynesian model	18,493.8	19,620.0	20,338.8	21,011.7	21,774.7	22,607.0	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	19,484.7	20,350.3	21,097.8	21,870.1	22,715.6	23,609.1	24,534.3	25,495.1	26,491.0	27,527.5	27,527.5	39,868.4
	Exhibit: Percentage change in GDP due to macro feedback (%)												
TPC Keynesian model	0.0	1.7	1.1	0.5	0.3	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
PWBM overlapping generations model	0.0	1.0	1.1	0.9	0.7	0.5	0.3	0.2	0.0	-0.3	-0.5	-0.5	-4.0

Sources: Congressional Budget Office (2016a, 2016b); Urban-Brookings Tax Policy Center (TPC) Keynesian model; Penn Wharton Budget Model (PWBM) overlapping generations model.

<sup>a</sup> End of period.

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 0.4 and 3.6 percent in 2017, 0.2 and 2.3 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 plan’s revenue losses. TPC estimates that the plan’s effects on demand would, in themselves, boost revenues by \$53.1 billion in 2017 (or between \$12.1 and \$116.0 billion billion using TPCs full range of estimates), by \$34.9 billion (or between \$8.0 and \$76.2 billion) in 2018, and by smaller amounts in later years. The revenue effect of the revised Trump plan, taking into account the dynamic revenue gains based on the TPC Keynesian model using standard parameters, are shown above in table 2.

### ***Impact on Potential Output***

In addition to short-run effects through aggregate demand, the revised Trump 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, which is a “forward-looking” model that assumes households adjust their labor supply and savings behavior and businesses adjust their investment behavior in

response to changes in tax and spending policies. The PWBM also assumes that policymakers eventually cut spending to stabilize the debt.

### Impact on Saving and Investment

The revised Trump plan would alter incentives to save and invest in the US. Large reductions in the tax rate 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 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 the tax cuts are not eventually financed in ways that reduce incentives to save and invest, these effects, in themselves, would tend to increase the amount of saving and investment in the US economy.

**TABLE 7**  
Effective Marginal Individual Income Tax Rates on Capital Income  
In percent, 2017<sup>a</sup>



Expanded cash income percentile <sup>b,c</sup>	Tax units (thousands)	Long-term capital gains			Qualified dividends			Interest income		
		Current law	Revised Trump plan	Change (percentage points)	Current law	Revised Trump plan	Change (percentage points)	Current law	Revised Trump plan	Change (percentage points)
Lowest quintile	48,335	0.7	0.7	0.0	0.3	0.3	0.0	1.7	1.3	-0.4
Second quintile	38,629	0.8	0.8	0.0	0.8	0.7	-0.1	6.5	5.3	-1.1
Middle quintile	33,885	6.9	6.0	-0.9	7.2	6.0	-1.2	17.7	15.2	-2.4
Fourth quintile	28,656	10.6	10.0	-0.6	10.7	9.9	-0.8	22.3	19.3	-3.0
Top quintile	23,960	23.2	19.5	-3.7	22.2	19.0	-3.2	34.1	29.4	-4.7
All	174,683	21.6	18.2	-3.4	19.2	16.5	-2.7	26.8	23.4	-3.4
<b>Addendum</b>										
80–90	12,387	14.3	14.5	0.2	14.6	14.9	0.3	25.0	23.4	-1.6
90–95	5,907	16.8	15.3	-1.5	16.7	16.0	-0.7	28.3	25.2	-3.1
95–99	4,534	22.9	18.5	-4.4	22.6	18.3	-4.3	35.0	27.9	-7.1
Top 1 percent	1,133	24.1	20.1	-4.0	24.0	20.1	-3.9	36.5	31.6	-4.9
Top 0.1 percent	117	24.1	20.0	-4.1	24.0	20.0	-4.0	35.4	31.5	-3.9

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

<sup>a</sup> Projections are for calendar year 2017. Effective marginal tax rates are weighted by the appropriate income source.

<sup>b</sup> Includes both filing and nonfiling 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

<sup>c</sup> 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. METR is a forward-looking measure of the effect of the tax system on the rate of return of a hypothetical marginal investment project (i.e., one that just just breaks even). We compare the METR on different investments under the revised Trump plan with the METR under current law. Because the plan would allow businesses to elect expensing of investment and would reduce average individual-level taxes on interest, capital gains, and



dividends, METRs on most new business investment would decrease significantly (table 8).

**TABLE 8**  
**Marginal Effective Tax Rates on New Investment**  
 In percent, 2017



Category	Current law	Revised Trump plan	Change (percentage points)
<b>Business investment</b>	<b>22.0</b>	<b>6.7</b>	<b>-15.3</b>
Corporate	24.0	9.5	-14.5
Equipment	19.9	10.0	-9.9
Structures	27.9	10.0	-17.9
Intellectual property products	-0.1	5.1	5.2
Inventories	38.4	10.0	-28.4
Pass-through	18.9	2.6	-16.3
Equipment	15.5	3.2	-12.3
Structures	22.3	3.2	-19.1
Intellectual property products	-3.4	-2.5	0.9
Inventories	31.6	3.2	-28.4
<b>Addendum</b>			
Corporate (equity financed)	30.8	9.3	-21.5
Corporate (debt financed)	-7.4	10.1	17.5
Variation (s.d.) across assets	12.2	1.8	
Variation (s.d.) across industries	6.1	0.9	

**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.

Investments in intellectual property could face higher METRs than under current law because business interest deductions would be disallowed for businesses that elected expensing. But intellectual property would still face the lowest METRs of any form of investment, because the plan would retain the research and experimentation credit. Business investments financed by debt could face higher effective tax rates than under current law, because firms that expensed would lose the ability to deduct interest. Overall, the plan would lower METRs, making investment more attractive, and would reduce the tax advantage for debt- over equity-financed investments, which could reduce corporate leverage.

Although the revised Trump 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.

## Impact on Labor Supply

The revised Trump 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 about 2 percentage points on average and by over 7 percentage points for the top 0.1 percent (table 9). Research suggests that taxes play a small or negligible role on labor supply decisions for most workers. When tax rates fall, some workers choose to work more because the reward for working rises, but some choose to work less because it is easier to meet consumption goals with higher take-home pay.

**TABLE 9**

### Effective Marginal Individual Income Tax Rates on Wages and Salaries

In percent, 2017<sup>a</sup>



Expanded cash income percentile <sup>b,c</sup>	Tax units (thousands)	Individual income tax			Individual income tax plus payroll tax		
		Current law	Revised Trump plan	Change (percentage points)	Current law	Revised Trump plan	Change (percentage points)
Lowest quintile	48,335	2.3	1.7	-0.6	16.2	15.6	-0.6
Second quintile	38,629	15.6	14.9	-0.8	29.4	28.6	-0.8
Middle quintile	33,885	19.2	17.5	-1.7	32.8	31.1	-1.7
Fourth quintile	28,656	20.1	18.5	-1.7	33.7	32.0	-1.7
Top quintile	23,960	31.1	27.9	-3.2	38.4	35.2	-3.2
All	174,683	24.7	22.4	-2.3	35.1	32.7	-2.3
<b>Addendum</b>							
80–90	12,387	25.5	24.9	-0.5	36.6	36.1	-0.5
90–95	5,907	27.8	25.4	-2.5	35.7	33.3	-2.5
95–99	4,534	33.0	29.2	-3.7	38.6	34.8	-3.7
Top 1 percent	1,133	38.8	32.3	-6.5	42.7	36.3	-6.5
Top 0.1 percent	117	39.5	32.2	-7.3	43.3	36.0	-7.3

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

<sup>a</sup> Projections are for calendar year 2017. Effective marginal tax rates are weighted by the wages and salaries.

<sup>b</sup> Includes both filing and nonfiling 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>.

<sup>c</sup> 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.

Second earners—lower-earning spouses—are sensitive to taxes, however. A person married to a high earner might face a very high marginal tax rate on the first dollar of earnings, which, when combined with the costs of working (e.g., paying for child care), can make working seem especially unappealing. By reducing marginal tax rates and providing additional tax benefits for child care, the proposal would reduce the disincentive for entering the workforce for potential second earners.

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.

### ***Long-Run Impact on Output and Revenues***

The PWBM estimates that the revised Trump plan’s effects on investment and labor supply would boost GDP by 1.0 percent in fiscal year 2017, but GDP would decline by 0.5 percent in 2026 and by 4.0 percent in 2036 (table 6). Those economic effects would in turn alter the revenue effect of the proposal, increasing them (relative to revenues before macro feedback) by \$42.5 billion in fiscal year 2017 and by \$178.3 billion between 2017 and 2026, but would reduce revenues (by an additional \$1,371.2 billion) 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 25.4 percent of GDP in 2026 and by 55.5 percent of GDP in 2036 (table 3). These ratios of debt to GDP are lower in 2026 than projected in TPC’s conventional estimates, but higher in 2036. Trump also promises to balance the budget through a combination of very large unspecified cuts in nondefense discretionary spending and revenue gains that arise indirectly from trade, energy, and regulatory policies. If these revenue offsets materialized, GDP would increase relative to baseline (assuming that the spending cuts do not come from productivity-enhancing public investments in such things as infrastructure or education).

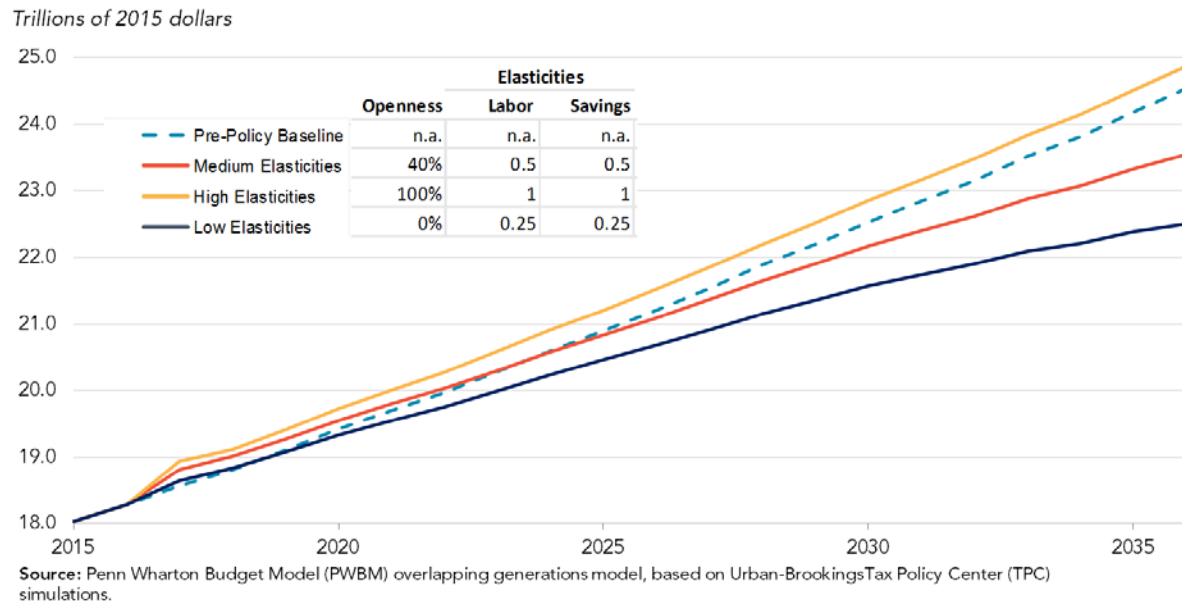
### ***Sensitivity of Macro Estimates to Assumptions***

Macroeconomic models are sensitive to assumptions about how individuals respond to incentives, the operation of world capital markets, and 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.<sup>16</sup> For example, compared with the baseline before incorporating macroeconomic response (labeled “pre-policy baseline” in figure 2), the PWBM’s baseline estimates (labeled “medium elasticities”) show GDP

initially rising, returning to the pre-policy level by 2024, and then falling below the pre-policy baseline.

The best case for a large and sustained supply-side response is one in which capital markets are open and US deficits do not affect the interest rates investors face, which are solely determined on world markets.<sup>17</sup> For the “high elasticities” scenario (figure 2), we assume 100 percent openness and that labor supply and savings are very responsive to wages and interest rates (represented by elasticities of 1.0, compared with 0.5 in the medium elasticity scenario). GDP under this set of assumptions rises very quickly to nearly 2.0 percent above the pre-policy level. The effect dampens over time, but in 2040, it is still over 1.3 percent higher.<sup>18</sup>

**FIGURE 2**  
GDP under Revised Trump Plan  
Before and after macro response



The “low elasticities” scenario makes the opposite assumptions. It assumes that capital markets are closed (no borrowing abroad), that workers and savers are relatively unresponsive to wages and interest rates. In this scenario, GDP only slightly exceeds the static level until 2019. By 2040, it falls 12.6 percent below the level in the pre-policy baseline because the government’s borrowing creates a shortage of capital and pushes up interest rates (“crowding out”).

Thus, the macro forecasts exhibit a substantial range of uncertainty.

## APPENDIX A. UNCLEAR DETAILS AND TPC'S ASSUMPTIONS ABOUT THE REVISED TRUMP PLAN

Because candidates' proposals rarely include all the details needed to model them accurately, we ask their staffs to clarify provisions or further specify details. We sent the following questions and working assumptions to Mr. Trump's campaign staff on September 26, 2016. The questions and assumptions are based on [Mr. Trump's speech in Detroit](#), [Mr. Trump's speech in Aston](#), [Mr. Trump's speech in New York](#), the position paper [on Mr. Trump's tax reform](#), the [outline of Mr. Trump's economic vision](#), the [fact sheet on Mr. Trump's economic policy](#), the [child care position paper](#) on the Trump campaign website, and the [child care fact sheet](#) on the Trump campaign website. Although we had some promising discussions with a Trump advisor, the campaign did not respond to our specific questions so we based our analysis on the assumptions listed below. If we receive clarifications in the future, we will update our analysis.

### CLARIFYING QUESTIONS AND TPC'S ASSUMPTIONS ABOUT THE PLAN

#### *Individual Income Tax Provisions*

The fact sheet on tax reform provides a number of details about individual income tax provisions, but some further specification is required for accurate scoring.

- Q1. Are the rate brackets expressed in 2016 dollars, or some other year's dollars, and are the brackets indexed for inflation from that year?
- A1. Absent clarification, TPC will assume that the brackets are expressed in 2016 dollars and will be indexed from 2016.
- Q2. Are the standard deduction amounts expressed in 2016 dollars, or some other year's dollars, and are they indexed for inflation from that year?
- A2. TPC will assume that the standard deduction amounts are expressed in 2016 dollars and will be indexed from 2016.
- Q3. Are all personal exemptions repealed, or just those for taxpayers?
- A3. TPC will assume that all personal exemptions are repealed.
- Q4. Are the limitation amounts on itemized deduction amounts expressed in 2016 dollars, or some other year's dollars, and are they indexed for inflation from that year?
- A4. TPC will assume that the limitation amounts are expressed in 2016 dollars and will be indexed from 2016.

Q5. Is the current law limitation on itemized deductions (“Pease”) retained?

A5. TPC will assume that the limitation is retained.

### ***Childcare Provisions***

The documents on Mr. Trump’s campaign website provide a number of details about the childcare (and eldercare) provisions, but some further specification is required for accurate scoring.

Q6. The current law credit and exclusion for employment-based child and dependent care benefits (which are retained under proposal) are limited to earnings. Is the proposed above-the-line childcare/eldercare deduction likewise limited to earnings?

A6. Absent clarification, TPC will assume the deduction is limited to earnings.

Q7. The documents indicate that the childcare deduction is capped at the state average for age of child. Which data would be used to determine these averages?

A7. TPC will use the averages in the table on page 53 and 54 of the 2015 report of Child Care Aware of America, “Parents and the High Cost of Child Care” (<http://usa.childcareaware.org/wp-content/uploads/2016/05/Parents-and-the-High-Cost-of-Child-Care-2015-FINAL.pdf>).

Q8. The documents indicate that the deduction would be available to families who use stay-at-home parents as well as grandparents to provide childcare. Because no market-based expenses would be incurred, how would the deduction amount be determined?

A8. TPC will assume that the caps for children are those shown for “family child care” in the report referenced in A7, and the \$5,000 cap on eldercare expenses. (The “child care center” caps are assumed to apply to paid childcare.)

Q9. Are the income limitation levels on eligibility for the childcare/eldercare deduction a “cliff” (i.e., those with income below the relevant level get the full deduction and those with income at or above the relevant level get no deduction), the levels at which the deductions begin to phase out, or the levels at which the deduction is fully phased out? If the deduction is phased out, what is (are) the phaseout rate(s) and at what incomes do the phaseouts begin if the levels are the end of the phaseout range? Are the levels expressed in 2016 dollars, or some other year’s dollars, and are they indexed for inflation from that year?

A9. TPC will assume that the income levels represent the end of the phaseout range, that the phaseout begins at \$400,000 for joint filers and at \$150,000 for single filers, and the deduction phases out pro rata over the \$100,000 of income between the beginning and

end of the phaseout ranges (so 1% of the deduction phases out per \$1,000 of income in the phaseout range). TPC will further assume that the income limitation levels are expressed in 2016 dollars and will be indexed from 2016.

Q10. The fact sheet on tax reform indicates that a childcare rebate would be added to the earned income tax credit (EITC), with the rebate “equal to 7.65 percent of remaining eligible childcare expense, subject to a cap of half the payroll taxes paid by the taxpayer (based on the lower-earning parent in a two-earner household).” The rebate would be available to joint filers “earning \$62,400 (\$31,200 for single taxpayers) or less.” Are “remaining eligible childcare expense” the eligible expenses not taken as a deduction, or used for the current-law credit or exclusion? Is any rebate available to a one-earner married couple? Do the rebate earnings limits represent “cliffs” or the end of phaseout ranges? If they represent the end of phaseout ranges, at what income levels do the phaseouts begin and what is (are) the phaseout rate(s)?

A10. TPC will assume that no rebate is available to a one-earner married couple, and that only expenses not used for the deduction, credit, or exclusion are eligible for the rebate. TPC will also assume that the rebate earnings limits represent the end of phaseout ranges that begin at half the limit, with a phase out rate of half of 7.65 percent (i.e., 3.825 percent) of earnings in excess of the beginning of the phaseout range.

Q11. Would withdrawals from the proposed Dependent Care Savings Accounts (DCSAs) be taxable?

A11. TPC will assume that all withdrawals from DCSAs would be taxable, but if used for eligible childcare or eldercare expenses they would qualify for the proposed deductions (or credit or exclusion), and if used for eligible higher education expenses would qualify for related credits or deductions.

### ***Taxation of Pass-Through Business Income***

Mr. Trump’s speeches in Detroit and New York, the outline of his economic vision, the fact sheets on tax reform and economic policy, and subsequent statements from campaign staff do not provide clear guidance on whether regular rates or a preferential 15 percent rate would apply to the income of pass-through businesses, whether the preferential 15 percent rate (if it applies) would apply to all pass-through business income or only a portion of that income (in particular, if a 15 percent rate applies to try to prevent current high wage earners from forming a pass-through entity that provides labor services to their current employer instead of taking compensation in the form of wages), and whether some owners would be subject to further taxation on at least some earnings that weren’t retained in some pass-through.

- Q12. Is the income from pass-through businesses taxed at regular income tax rates, is the rate on such income capped at 15 percent, or can each owner elect to pay either regular income tax rates or a flat rate of 15 percent on such income?
- A12. Absent further guidance, TPC will assume that each owner can elect to pay either regular income tax rates or a flat rate of 15 percent on such income. Net losses from pass-throughs can only be used to offset positive business income, but can be carried forward as under current law.
- Q13. Can the flat 15 percent rate be elected each year? Does the election apply to all pass-through income received by an owner, or can the election be made for the income from each pass-through?
- A13. TPC will assume the election can be made each year, and applies to all pass-through income of the owner.
- Q14. Does the 15 percent flat rate, if elected, apply to all income from pass-through businesses, or only to income in excess of “reasonable compensation” (as in the House GOP plan), or only to some other portion of that income?
- A.14 TPC will assume that the 15 percent rate would apply to all business income for owners that elect the flat rate.
- Q15. Under what set of circumstances would owners of pass-through businesses be subject to tax on earnings that weren’t retained in the business (“distributions”)? Would only owners of “large” pass-throughs be taxed on distributions, and if so how is “large” defined?
- A15. TPC will assume that pass-through distributions paid out of earnings elected to be taxed at the flat 15 percent business rate would be taxed as qualified dividends. Distributions from qualifying “small businesses” would be exempt and not subject to tax as dividends. Pass-through income taxed as ordinary income would be deemed distributed in that year with no additional tax due.

### *Expensing of Investment*

In his Detroit speech, Mr. Trump said his plan would “allow businesses to immediately expense new business investment,” but in his New York speech that the plan “would allow U.S.-based manufacturers to fully expense the cost of new plants and equipment [emphasis added].” The fact sheet on tax reform also states “Firms engaged in manufacturing in the US may elect to expense capital investment [emphasis added].”

- Q16. Would expensing only be available to manufacturers, and only for plant and equipment, or could all investment (in the U.S.) be expensed by all business? Could unused depreciation



and amortization on existing assets be used after the plan goes into effect, and if so what rules would apply?

A16. TPC will assume that all businesses could expense all investment (in the U.S.), and that unused depreciation and amortization as of the effective date of the plan could be used under current law rules.

### *Interest Deductibility*

The fact sheet on tax reform indicates that firms that elect to expense investment would “lose the deductibility of corporate interest expense [emphasis added].”

Q17. Would the disallowance apply to pass-through businesses that elect to expense investment? Would the disallowance apply to interest on debt outstanding when the rules go into effect?

A17. TPC will assume that the disallowance would apply to pass-through businesses that elect to expense investment, but would not apply to interest on existing debt (so such interest would remain deductible).

### *“Special Interest” Tax Provisions*

In his Detroit speech, Mr. Trump said his plan would “eliminate the Carried Interest Deduction and other special interest loopholes” and in his New York speech that “special interest loopholes” would be closed, but no specific provisions are identified. The fact sheets on tax reform indicate that the plan “eliminates most corporate tax expenditures” except the research credit.

Q18. Which “special interest” provisions and corporate tax expenditures would be repealed? Could unused credits repealed by the plan be used once the plan goes into effect, and if so what rules would apply?

A18. TPC will assume that the corporate tax expenditures the plan would repeal are the section 199 domestic production activity deductions and all credits except the research credit, and that these same tax expenditures would be repealed for pass-through businesses taxed under the individual income tax. TPC will further assume that any unused repealed business credits as of the effective date of repeal could be used, generally under current law rules. Absent further clarification, TPC will assume that the only other “special interest” provision repealed by the plan is the carried interest provision.

### ***Repatriation of Earnings from Foreign Subsidiaries***

Q19. Is the tax rate similar to the Camp proposal, with the 10 percent rate applying only to accumulated earnings held in cash and a lower rate to the remainder? Is this one-time repatriation tax payable immediately or over some number of years?

A19. TPC will assume that the repatriation tax is structured in the same manner as Camp's, with the 10 percent rate applying to accumulated cash earnings and a lower 4 percent rate for non-cash earnings (resulting in the same proportional difference between the 8.75 and 3.5 percent rates in the Camp proposal). We will further assume that payments would be made over 10 years (rather than 8 in the Camp proposal).

### ***Estate and Gift Taxes***

In his Detroit speech, Mr. Trump indicated that his plan would repeal the estate tax. The fact sheet on tax reform indicates that "capital gains held until death will be subject to tax, with the first \$10 million tax free as under current law."

Q20. Would the plan repeal the generation skipping transfer (gst) and gift taxes? Is the \$10 million exemption amount per decedent, or the combined amount for a married couple? Would all of the capital gains (in excess of the exemption amount) of each spouse be taxed at death, or would gains on assets transferred to the surviving spouse be delayed (through carryover of basis) or forgiven (through step up of basis)? If carryover basis applies to spousal transfers, would the exemption of the deceased spouse carry over to the surviving spouse?

A20. TPC will assume that the gst and gift taxes are also repealed. TPC will further assume that the exemption amount is \$5 million per decedent, that carryover basis applies on appreciated assets transferred to spouses, and that the exemption of the deceased spouse also carries over.

### ***Affordable Care Act (ACA) Taxes***

In his Detroit and New York speeches Mr. Trump indicated he plans to "repeal and replace" the ACA ("Obamacare"). However, the only ACA tax explicitly listed as repealed in the fact sheet on tax reform is the 3.8 percent net investment income tax.

Q21. Does the tax plan include repeal of any other ACA taxes?

A21. TPC will assume that no other ACA taxes are repealed by the tax plan.

### *Effective Date*

No explicit effective date was specified for the tax plan in Mr. Trump's Detroit and New York speeches, or in the related documents on the campaign website.

Q22. Are all provisions intended to go into effect in 2017, or at some earlier date? Are some (such as the corporate rate reduction) assumed to be phased in, and, if so, over what time period?

A22. TPC will assume the provisions would be effective beginning in 2017, and that no provisions are phased in. We will also assume that all indexed parameters are stated at 2016 levels, so are indexed beginning in 2017.

### *Provisions in Mr. Trump's Previous Tax Plan*

Some of the provisions included in the tax reform plan announced by Mr. Trump in 2015 are not mentioned in his Detroit and New York speeches or related documents currently posted on his campaign website. For example, the proposed end of deferral of taxation of foreign subsidiaries of U.S. corporations and the tax exemption on life insurance interest for high-income earners.

Q23. Are the provisions in Mr. Trump's tax plan as announced in 2015 that are not mentioned in his recent speeches and related documents on his website included in his revised tax plan?

A23. Absent further guidance, TPC will assume that provisions not mentioned in Mr. Trump's recent speeches or related documents on his website are not included in his revised tax plan.

## 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 measures of the effects of the revised Trump 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, with the only large reduction for the top 1 percent (column 5).

**TABLE B1**

**Alternative Ways of Presenting Change in Distribution of Tax Burdens under the Revised Trump Plan**  
 By expanded cash income percentile, 2017<sup>a</sup>



Expanded cash income percentile <sup>b,c</sup>	Percent change in after-tax income <sup>d</sup> (%)	Share of total federal tax change (%)	Average federal tax change <sup>e</sup>		Share of federal taxes	
			Dollars	Percent	Change (% points)	Under the proposal (%)
Lowest quintile	0.8	1.1	-110	-20.4	-0.1	0.8
Second quintile	1.2	3.0	-400	-13.2	0.1	3.9
Middle quintile	1.8	6.6	-1,010	-11.3	0.6	10.2
Fourth quintile	2.2	11.3	-2,030	-10.5	1.2	18.8
Top quintile	6.6	77.7	-16,660	-18.6	-1.9	66.2
All	4.1	100.0	-2,940	-16.3	0.0	100.0
<b>Addendum</b>						
80–90	2.3	7.9	-3,270	-9.3	1.2	15.1
90–95	2.8	6.2	-5,350	-9.7	0.8	11.2
95–99	6.0	16.3	-18,490	-17.6	-0.2	14.9
Top 1 percent	13.5	47.3	-214,690	-26.9	-3.6	25.0
Top 0.1 percent	14.2	24.2	-1,066,460	-27.1	-1.9	12.7

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

**Note:** Number of AMT taxpayers (millions): Baseline: 4.8; Proposal: 0.

<sup>a</sup> Calendar year. Baseline is current law. Proposal includes individual, payroll, corporate, and estate provisions in the revised Trump plan. <http://www.taxpolicycenter.org/taxtopics/Baseline-Definitions.cfm>.

<sup>b</sup> The percentile includes both filing and nonfiling 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>.

<sup>c</sup> 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.

<sup>d</sup> 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.

<sup>e</sup> 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.

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<sup>1</sup> See Trump (2016a, 2016b and 2016c). See also Nunns and coauthors (2015) for TPC's analysis of Mr. Trump's original tax plan.

<sup>2</sup> 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 US Department of the Treasury to estimate revenue effects before considering the macroeconomic effects.

<sup>3</sup> See Page and Smetters (2016) for a description of the models used in TPC's macroeconomic analyses.

<sup>4</sup> In our modeling, we assume the capital gains exclusion is indexed, although the campaign documents are unclear on this point.

<sup>5</sup> Repealing the estate tax would also reduce the incentive to make donations during an individual's 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.

<sup>6</sup> The available documents describing the revised Trump tax plan do not specify how the size of pass-through businesses (or business income) would be determined. For our analysis, if the owner of one or more pass-through entities received at least \$500,000 in total pass-through business income under current law, actual distributions were assumed to be taxed in the same manner as a dividend under the plan. Actual distributions for all other pass-through businesses were assumed to be untaxed. We also assumed that payroll taxation of pass-through business income would be unchanged by the plan.

<sup>7</sup> In comparison, the House GOP plan would limit the rate cap to income in excess of "reasonable compensation" and apply a higher rate cap of 25 percent (see Ryan 2016).

<sup>8</sup> 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 revised Trump plan, any portion of current wages that could avoid payroll tax would save 3.8 percent, plus another 18 percent, for a total of up to 21.8 percent.

<sup>9</sup> Specifically, we assumed that starting in 2017, each year 5 percent of workers currently earning wages of \$100,000 or more (\$200,000 or more on a joint return) would begin to work through sole proprietorships or other pass-through businesses, until half had made that switch. Workers who switched and as a result had more than \$500,000 of total pass-through income were taxed (under the special rates that apply to dividends) on actual distributions (which we assumed would be half of their new total pass-through income).

<sup>10</sup> The available documents describing the revised Trump tax plan do not specify which business tax expenditures would be repealed, but indicate that the research and experimentation credit would be retained. We assumed the plan would repeal all business credits (other than the research and experimentation credit, which the documentation indicates would be retained, and the credit for employer-provided child and dependent care, which the documentation indicates would be expanded). We also assumed that the domestic production activities (section 199) deduction would be repealed.

<sup>11</sup> This treatment is consistent with our analysis of Mr. Trump's original tax proposal (Nunns and coauthors 2015).

<sup>12</sup> 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 reduction in capital gains rates in 2017.

<sup>13</sup> This distributional analysis is based on the Urban-Brookings Tax Policy Center Microsimulation Model. For a brief description of the model, see <http://www.taxpolicycenter.org/taxtopics/Brief-Description-of-the-Model-2015.cfm>.

<sup>14</sup> The PWBM's tax estimates are available at <http://www.budgetmodel.wharton.upenn.edu/tax-policy-2/>

<sup>15</sup> 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.

<sup>16</sup> A user interface to the PWBM is available here: <http://www.budgetmodel.wharton.upenn.edu/tax-policy-2/>. Users may alter assumptions and see effects on GDP, employment, capital stock, and other macroeconomic aggregates.



## NOTES

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<sup>17</sup> 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 US given how large we are relative to the world economy, but it is shown as a point of comparison.

<sup>18</sup> However, the more open the economy is assumed to be, the greater will be the share of income generated by new investment that will accrue to foreign investors rather than US residents.



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