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ONLY A FEW OF THE 2001 AND 2003 TAX CUT PROVISIONS BENEFIT FAMILIES WITH MODEST INCOMES

But a Superficial Treasury Analysis Obscures This Fact

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KEY FINDINGS

- A recent Treasury report, apparently intended to encourage the extension of all of the 2001 and 2003 tax cuts, incorrectly implies that many of these tax cuts benefit low- and middle-income taxpayers.
- The report calculates the benefits that four "representative taxpayer" families with modest incomes receive from the tax cuts as a whole. But it fails to explain that *all* of those benefits come from just *three* of the tax cuts: (1) improvements to the Child Tax Credit, (2) the creation of the 10-percent tax bracket, and (3) "marriage penalty" relief.
- By providing only the tax cuts' *overall* effect on these sample families, the report masks the fact that the families gain no benefit from the other costly tax cuts, such as the rate reductions for the top four tax brackets and the cuts in capital gains and dividend taxes.
- As the actual Treasury calculations indicate but the report obscures, low- and middle-income Americans have gained little from the 2001 and 2003 tax cuts other than the three provisions listed above.

A recent Treasury Department release, "Tax Relief in 2001 Through 2011," shows the reduction in taxes that four hypothetical families with modest incomes are receiving as a result of "legislation enacted during the President's term in office."[1] The implication of the release is that the 2001 and 2003 tax cuts have been highly beneficial for such families and hence should be extended.

An examination of the calculations on which the paper rests shows, however, that 100 percent of the tax benefits the Treasury computed for all four of its example families come from just three provisions of the 2001 and 2003 legislation: (1) the improvements to the Child Tax Credit; (2) the creation of the 10-percent income tax bracket; and (3) "marriage penalty" relief. By reporting only the aggregate effect of the 2001 and 2003 tax cuts on these representative families, Treasury's release masks this fact. Some readers may mistakenly conclude from the release that many of the tax cuts enacted in 2001 and 2003 are contributing to the overall tax benefits the example families are receiving, when, in fact, few of the 2001 and 2003 tax-cut provisions touch low- and middle-income people. The Treasury release consequently is likely to do more to obscure than to illuminate the choices policymakers face regarding which provisions

[1] Department of the Treasury, "Tax Relief in 2001 Through 2011", May 2008, http://www.treasury.gov/press/releases/reports/taxrelief_20012011_052708.pdf

of the 2001 and 2003 tax cuts to extend and which to allow to expire as scheduled at the end of 2010.

Treasury's Four Families Benefit Only From the Child Tax Credit Improvement, the 10 Percent Income Tax Bracket, and Marriage Penalty Relief

The Treasury's first hypothetical family is a married couple with two children in which one spouse earned $40,000 in 2007. The Treasury release reports that this family paid $2,053 less in taxes as a result of the 2001 and 2003 tax cuts, compared to what it would have paid if the tax cuts had not been enacted.[2] The Treasury document does not make clear that this relief comes entirely from three provisions of the tax legislation. The family's $2,053 tax cut consists of[3] $1,000 from the improvement in the Child Tax Credit[4], $783 from the 10 percent tax rate on the lowest income-tax bracket,[5] and $270 in "marriage penalty" relief.[6]

As Table 1 makes plain, the Child Tax Credit, 10 percent income tax bracket, and (to a much lesser extent) marriage penalty relief are responsible for *all* of the tax cuts that all four of Treasury's representative families receive.[7]

TABLE 1: Treasury's "Representative" Families Benefit Only From the Child Tax Credit Improvement, the 10 Percent Income Tax Bracket, and Marriage Penalty Relief

Portion of aggregate tax cut from:	Treasury Example 1: **Married couple filing jointly, one earner with $40,000 wage income, two children.**		Treasury Example 2: **Married couple filing jointly, one earner with $80,000 wage, two children**		Treasury Example 3: **Married couple filing jointly, one earner with $40,000 wage, one child**		Treasury Example 4: **Head of Household earning $30,000 wage, two children**	
Child Tax Credit improvement	$1,000	**49%**	$1,000	**56%**	$500	**32%**	$1,000	**64%**
10% Rate on Lowest Income Bracket	$783	**38%**	$783	**44%**	$783	**50%**	$560	**36%**
Marriage Penalty Relief	$270	**13%**	$0	**0%**	$270	**17%**	$0	**0%**
Aggregate Cut	$2,053	**100%**	$1,783	**100%**	$1,553	**100%**	$1,560	**100%**

Improvements to the Child Tax Credit, which allow each of the hypothetical families to receive the maximum credit of $1,000 per child, are responsible for more than 30 percent of each of these

2 Treasury described all of its example families as earning income from wages and salaries only and taking either an 18% itemized deduction or the standard deduction (whichever was larger).

3 Center on Budget and Policy Priority calculations, adopting Treasury's description of the family.

4 The 2001 tax-cut legislation doubled the child tax credit, increasing it from $500 to $1,000 per child. The legislation also made the child tax credit partially refundable for many more low-income working families (so households with income tax liability less than the value of the credit may receive the credit as an income tax refund).

5 The 2001 tax-cut legislation created a new 10 percent bracket, carved out of the old 15 percent tax bracket.

6 Three provisions of the 2001 tax cuts are designed to provide "marriage penalty relief" — that is, to reduce the increase in taxes a couple might otherwise face if they were to pay taxes as a married filing jointly as compared to paying taxes as two separate single filers.

7 Calculations in Table 1 are Center on Budget and Policy Priority calculations, based on Treasury's description of the example families.

families' tax reductions and account for more than half of the tax cut that two of the families get. The creation of the 10 percent tax bracket accounts for at least 36 percent of each of the families' tax cuts.

By contrast, none of Treasury's example families benefit from any of the other tax cuts enacted in 2001 and 2003, including the reductions in taxes on capital gains and dividends, the reductions in tax rates for the top four tax brackets, the curtailment of the estate tax, and various other provisions.

Only Three of the Tax Cuts Deliver Real Benefits to Low- and Moderate-Income Households

This finding is not limited to Treasury's example families. Tax Policy Center (TPC) data confirm that the only tax provisions enacted in 2001 or 2003 that deliver significant benefits to most households in the middle 20 percent of the income distribution — as well as to households in the bottom 40 percent of the distribution — are the improvements in the child credit, the 10 percent income tax bracket, and marriage penalty relief.

For example, TPC estimates that households in the middle income quintile will receive an average tax cut in 2010 of $414 from the 10 percent income tax bracket, $227 from the improvements in the Child Tax Credit, and $83 from marriage penalty relief. (See Table 2.) The total average tax cut from these three provisions for households in the middle of the income scale will be $724. In contrast, the average tax cut in 2010 for households in the middle income quintile from the reductions in the top income rates, the capital gains tax cut, and the

TABLE 2: Impact of Tax Cuts on Low-Income and Middle-Income Households

	Average tax cut in 2010 from:			
Income Class	**Child Tax Credit**	**10 Percent Bracket**	**Marriage Penalty Relief**	**Total of the three provisions**
Bottom 20 percent	$7	$18	$2	$27
Second 20 percent	$165	$189	$39	$393
Middle 20 percent	$227	$414	$83	$724

Source: Urban-Brookings Tax Policy Center
See Table 4 for income cut-offs and average incomes for income classes

TABLE 3: Impact of Tax Cuts on Low-Income and Middle-Income Households

	Average tax cut in 2010 from:			
Income Class	**25 Percent Bracket**	**28 Percent Bracket**	**Cap Gains and Dividend**	**Total of the three provisions**
Bottom 20 percent	$0	$0	$0	$0
Second 20 percent	$0	$0	$9	$9
Middle 20 percent	$8	$0	$22	$30

Source: Urban-Brookings Tax Policy Center
See Table 4 for income cut-offs and average incomes for income classes

TABLE 4: Income Ranges and Average Incomes

	2010	
	Income range:	**Average Income:**
Bottom 20 percent	Less than $16,447	$9,317
Second 20 percent	$16,447 to $31,249	$23,511
Middle 20 percent	$31,250 to $54,210	$41,886

Source: Urban-Brookings Tax Policy Center. Income is cash income.

dividend tax cut *combined* will be $30. (See Table 3.)

The tax benefits from the reductions in the top rates and the capital gains and dividend tax cuts accrue overwhelmingly to households at higher income levels. For example, while households in the middle 20 percent of the income distribution will receive an average of only $8 in 2010 from the 25 percent and 28 percent tax brackets, households in the top 20 percent of the income distribution will receive an average of $1,535 from these tax cuts, and those in the top 1 percent of the population will receive an average gain of $3,269. (See Appendix Table 1.)

Similarly, while households in the middle 20 percent of the income distribution will receive an average tax reduction of $22 from the capital gains and dividend tax cuts in 2010, households in the top 20 percent of the income distribution will receive an average tax benefit of $842 from these provisions, and those in the top one percent will receive an average benefit of $10,885.

Indeed, 85 percent of the benefits from extending the 25 percent tax bracket, 89 percent of the benefits from extending the capital gains and dividend tax cuts, and virtually 100 percent of the benefits of extending the 28 percent bracket and the higher brackets would flow to taxpayers in the top 20 percent of the income distribution. (See Appendix Table 2.) Moreover, the top 1 percent of households would capture 58 percent of the benefits from extending the capital gains and dividend tax cuts. (See Appendix Table 3.)

Households at the top of the income scale also will receive extremely large tax cuts as a result of the reductions in rates in the two top tax brackets — what are now the 33 percent and 35 percent brackets. The Tax Policy Center data do not provide estimates of the magnitude of the average tax reduction in 2010 by income group as a result of the rate reductions in the two top brackets. The TPC data do show, however, that the *total* tax cut in 2010 as a result of *all* provisions enacted in the 2001 and 2003 legislation will equal an average of $7,452 for those in the top 20 percent of the population, $62,515 for those in the top 1 percent, and $157,573 for those with incomes over $1 million. By contrast, the total average tax cut for people in the middle 20 percent for the population will be $814; for those in the bottom 20 percent, the average tax cut will be $37.[8]

Conclusion

Policymakers must decide in the next two years which of the tax cuts enacted in 2001 and 2003 to extend and which to allow to expire at the end of 2010. One factor for policymakers to consider in making these decisions is which households benefit from each of the tax provisions.

Treasury's recent analysis does not help policymakers with this task: it masks the fact that while improvements to the Child Tax Credit, the 10 percent income tax bracket, and marriage penalty relief benefit middle and low-income families along with other families, other costly tax cuts enacted

[8] These total tax cut figures for 2010 include the effect of the child tax credit improvement, all marginal income tax rate reductions, marriage penalty relief, capital gains and dividend tax cuts, the elimination of limits on the value of itemized deductions claimed by high-income taxpayers, and the elimination of the personal exemption phase-out for high-income taxpayers. They also include the effect of other miscellaneous tax cut provisions, including elimination of the estate tax and changes in pension and IRA provisions, the child and dependent care credit, and the student loan interest deduction.

in 2001 and 2003 deliver virtually no relief to low- and middle-income Americans and concentrate their benefits on people much higher on the income spectrum.

Furthermore, extending the tax provisions that are poor at delivering relief to low- and middle-income Americans would be costly: it would cost $1.02 trillion over 2009 to 2018 to extend the cuts in the top four marginal income tax rates, the capital gains and dividend tax cuts, and provisions that eliminate the personal exemption phase-out and the phase-out of itemized deductions for high-income taxpayers.[9] Extending the elimination of the estate tax through to 2018 would cost an additional $670 billion. By contrast, it would cost $678 billion to extend through to 2018 the Child Tax Credit improvement, the 10 percent income tax bracket, and marriage penalty relief, the three tax cuts that do benefit low- and middle-income families.[10]

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[9] Permanently eliminating the personal exemption phase-out and the phase-out of itemized deductions would exclusively benefit high-income households. The itemized deduction phase-out provision of current law limits the value of itemized deductions for taxpayers with high incomes. The personal exemption phase-out provision phases out the value of that exemption for high-income taxpayers. These two provisions were enacted as part of the bipartisan 1990 deficit reduction package. The 2001 tax-cut legislation repealed these provisions, as of 2010. For more detail about these provisions, see Aviva Aron-Dine and Robert Greenstein, "Two High Income Tax Cuts Not Yet Fully In Effect Will Cost Billions Over the Next Five Years," February 1, 2007, http://www.cbpp.org/2-1-07tax.htm.

[10] Center on Budget and Policy Priority calculations based on Congressional Budget Office and Tax Policy Center estimates. Figures exclude the additional interest cost on increases to debt attributable to extending these provisions.

Appendix: Distribution of the Tax Cuts by Income Percentile

APPENDIX TABLE 1: Average Tax Cut from Specified Provisions, by Cash Income Category						
	Child Tax Credit	10 Percent Bracket	Marriage Penalty Relief	25 Percent Bracket	28 Percent Bracket	Capital Gains and Dividends
Bottom 20 percent	$7	$18	$2	$0	$0	$0
Second 20 percent	$165	$189	$39	$0	$0	$9
Middle 20 percent	$227	$414	$83	$8	$0	$22
Fourth 20 percent	$252	$619	$148	$193	$0	$68
Top 20 percent	$173	$713	$1,064	$1,174	$361	$842
Top 1 percent	$5	$614	$1,050	$1,704	$1,565	$10,885
Above $1 million	$5	$627	$1,103	$627	$1,678	$33,889

Source: Urban-Brookings Tax Policy Center

APPENDIX TABLE 2: Shares of Total Tax Cut from Specified Provisions, by Cash Income Category						
	Child Tax Credit	10 Percent Bracket	Marriage Penalty Relief	25 Percent Bracket	28 Percent Bracket	Capital Gains and Dividends
Bottom 20 percent	1%	1%	0%	0%	0%	0%
Second 20 percent	20%	10%	3%	0%	0%	1%
Middle 20 percent	28%	21%	6%	1%	0%	2%
Fourth 20 percent	31%	32%	11%	14%	0%	7%
Top 20 percent	21%	37%	80%	85%	100%	89%
Top 1 percent	0%	2%	4%	6%	22%	58%
Above $1 million	0%	0%	1%	2%	6%	45%

Source: Urban-Brookings Tax Policy Center

APPENDIX TABLE 3: Percentage Change in After-Tax Income from Specified Provisions, by Cash Income Category						
	Child Tax Credit	10 Percent Bracket	Marriage Penalty Relief	25 Percent Bracket	28 Percent Bracket	Capital Gains and Dividends
Bottom 20 percent	0.1%	0.2%	0.0%	0.0%	0.0%	0.0%
Second 20 percent	0.8%	0.9%	0.2%	0.0%	0.0%	0.0%
Middle 20 percent	0.7%	1.2%	0.2%	0.0%	0.0%	0.1%
Fourth 20 percent	0.4%	1.1%	0.3%	0.3%	0.0%	0.1%
Top 20 percent	0.1%	0.4%	0.7%	0.7%	0.2%	0.5%
Top 1 percent	0.0%	0.1%	0.1%	0.2%	0.2%	1.2%
Above $1 million	0.0%	0.0%	0.1%	0.1%	0.1%	1.5%

Source: Urban-Brookings Tax Policy Center

APPENDIX TABLE 4: Income Ranges and Average Incomes for Income Groups		
	2010	
	Income range:	**Average Income:**
Bottom Quintile	Less than $16,447	$9,317
Second Quintile	$16,447 to $31,249	$23,511
Middle Quintile	$31,250 to $54,210	$41,886
Fourth Quintile	$54,211 to $96,523	$72,976
Top Quintile	More than $96,523	$1,384,540
Top 1 percent	More than $481,460	$1,384,540
Above $1 million	More than $1,000,000	$2,072,989

Source: Urban-Brookings Tax Policy Center. Income is cash income.