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Senate Tax Bill Has Same Basic Flaws as House Bill

Increases Deficits, Tilts Heavily Toward the Wealthy, and Would lead to Deep Program Cuts in the Future

By Sharon Parrott

The Senate Finance Committee tax bill, like the Republican tax framework released in September and the House Ways and Means Committee tax bill, would drive up deficits by $1.5 trillion over the next decade and give very large tax cuts to the wealthiest households and profitable corporations but only token help to millions of low-income working families.

The core of the bill is a large corporate tax cut that would overwhelmingly benefit wealthy households, along with a tax cut for "pass-through" businesses that's also heavily tilted to high-income households and an estate tax cut providing a reduction in the tax worth $4.4 million per estate (for the estates of married couples) for the nation's largest estates. These tax cuts are so costly that they require offsets like removing the tax deduction for state and local taxes to comply with the limitation that the tax cuts *only* increase deficits by $1.5 trillion over the decade. They leave little room for meaningful help to low- and moderate-income families.

Even a provision touted as targeting working families — an expansion of the Child Tax Credit — would do far more for high-income families than low- and moderate-income families. Some 10 million children in low-income working families would get $75 or less, while families with incomes between $150,000 and $1 million would become newly eligible for the credit. A married couple with two children earning $1 million would newly receive a full $3,300 Child Tax Credit, on top of large additional tax cuts from other provisions.

Moreover, when attention turns to addressing deficits — which the bill would drive significantly higher — low- and middle-income families would likely bear much of the burden. Indeed, when the tax cuts are ultimately paid for, these families would likely lose more in health care, education, job training, and other services than they gain in tax cuts, while high-income households would likely remain large net winners.

Bill Likely to Continue Adding to Deficits Beyond Initial Decade

The nation faces major long-term fiscal challenges stemming from the imbalance between the tax revenues projected under current law and the projected level of federal expenditures, which will rise in coming decades as the aging of the baby-boom generation raises federal health and retirement costs. The Senate bill, like the House bill, would compound these fiscal challenges.

The Senate bill would increase deficits by $1.5 trillion over the coming decade. When fully in effect, it would increase deficits by *more than* $150 billion per year, in part because it phases in certain costly provisions, including the cut in the corporate rate, to reduce its cost over the first decade. In 2027, for example, the bill would cost $217 billion.

Under the rules governing the legislative process the tax bill is using — called "reconciliation" — the bill cannot increase deficits *on paper* in the decades after 2027. However, the materials released by the Finance Committee do not show how the bill will comply with this requirement, and ultimately the Senate will likely use a familiar gimmick to mask the bill's true cost after 2027: schedule some or all of the tax cuts to expire so they appear to have no cost after 2027. History shows, however, that despite such sunsets, policymakers are unlikely to allow most tax breaks to expire, which means the tax bill will likely lead to substantial deficit increases in the decades to come.

Policymakers used this same "sunsetting" gimmick to make the 2001 Bush tax cuts appear not to increase deficits after the initial decade. When the tax cuts neared expiration, policymakers made 82 percent of them permanent, and higher deficits resulted. The cost of the Bush tax cuts from 2001-2018 (as amended by later legislation) accounts for about one-third of the debt held by the public in 2018.[1]

Large Tax Cuts Likely to Lead to Large Budget Cuts

If these tax cuts become law, many of the same policymakers and interests that pushed for them will likely decry the resulting higher deficits and debt, declare federal programs to be the culprit, and seek deep budget cuts — presumably the same kinds of cuts they have outlined in their budget plan — while not offering any proposals to raise revenues. This could happen as soon as next year; indeed, some members of Congress have signaled their intent to push for deep budget cuts next year in another reconciliation process.[2]

The budget resolution that Congress adopted this month calls for *$5.8 trillion* in program cuts over the coming decade. These include $1.8 trillion in cuts in Medicaid, Medicare, and other health care entitlement programs and $800 billion in cuts *below* the already austere sequestration levels in "non-defense discretionary" programs, the budget area that includes education and training, transportation, scientific and medical research, protection of the food and water supply, child care, low-income housing assistance, services for frail elderly people, and much more.

Such cuts would necessarily fall most heavily on families and individuals with low or modest incomes — the same families that would gain little from the Senate tax bill.

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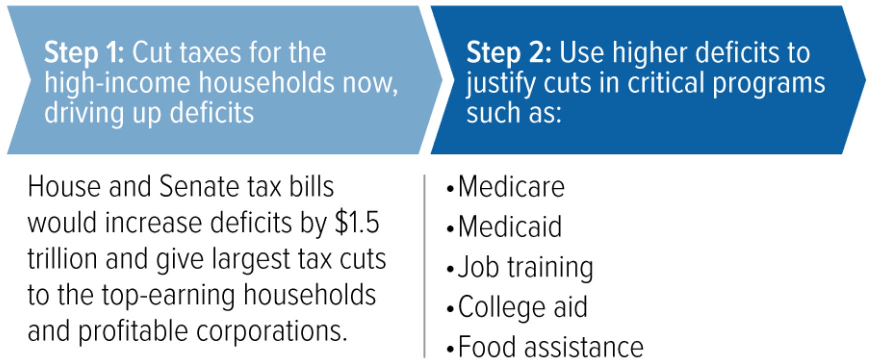
[1] Emily Horton, "The Legacy of the 2001 and 2003 "Bush" Tax Cuts," CBPP, updated October 23, 2017, https://www.cbpp.org/research/federal-tax/the-legacy-of-the-2001-and-2003-bush-tax-cuts.

[2] Lindsey McPherson, "On Debt Reduction, GOP Says Wait Till Next Year," *Roll Call*, October 26, 2017, http://www.rollcall.com/news/politics/on-debt-reduction-republicans-say-wait-till-next-year.

The Two-Step Fiscal Agenda



Tax Cuts Heavily Tilted Toward the Wealthy and Profitable Corporations

While the Senate and House tax bills are not identical, they both include costly tax cuts that disproportionately benefit high-income households and profitable corporations:

- A tax cut on "pass-through" businesses (businesses such as real estate developers whose profits are now taxed at the owners' individual income tax rates) that would provide its largest tax cuts to extremely large businesses owned by high-income households.
- A cut in the corporate tax rate to 20 percent, which would provide more than a third of its benefits to the top 1 percent of households, and an *even lower* rate on multinationals' foreign profits.
- Deep cuts in the estate tax that would only benefit the heirs of the wealthiest 0.2 percent of estates. While the Senate bill would not repeal the estate tax, it would cut taxes for the largest estates by $4.4 million, for estates held by married couples.[3]
- Cuts in individual income tax rates, including a lower top rate than the House bill. The cuts in tax rates and the changes in the tax brackets would give a couple with $10 million in taxable income a tax cut of more than $130,000 (though their overall change in tax liability would depend on all of the tax provisions affecting them).[4]
- Repeal of the Alternative Minimum Tax, which ensures that higher-income people who take a large amount of deductions and other tax breaks pay a minimum level of tax.

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[3] Chye-Ching Huang, "Doubling Estate Tax Exemption Would Give Windfall to Heirs of Wealthiest Estates," CBPP, November 9, 2017, https://www.cbpp.org/blog/doubling-estate-tax-exemption-would-give-windfall-to-heirs-of-wealthiest-estates.

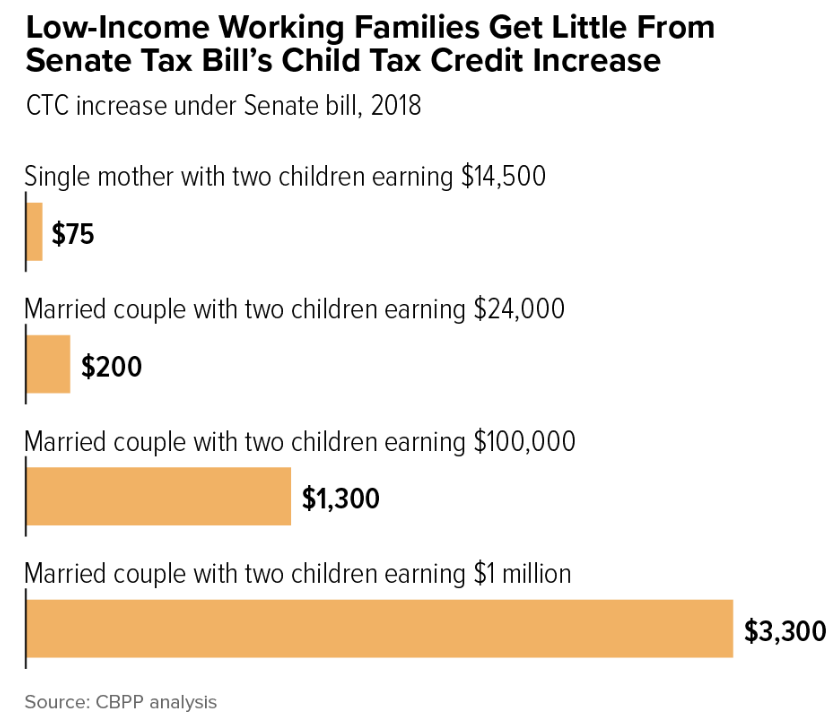
[4] A family in the top tax bracket benefits from all of the reductions in tax rates on income that falls into the lower tax brackets, as well as from the reduction in the top rate. This calculation takes into account the impact of the rate reductions – and changes in the income thresholds – in all of the brackets.

Child Tax Credit Proposal Leaves Out Millions of Low- and Moderate-Income Children

The Senate bill's Child Tax Credit (CTC) proposal is similar to the House plan.[5] It would raise the maximum credit from $1,000 to $1,650 per child (versus $1,600 in the House plan) and extend the credit to 17-year-olds, who are now ineligible. But many low- and moderate-income children would see only a token benefit. That's because the proposal does not expand the credit meaningfully for families that receive the refundable portion of the CTC because their earnings are too low to owe federal income taxes.

One in seven children under age 17 in working families — 10 million children — whose parents work at low-wage jobs would get just $75 per family (irrespective of whether the family has more than one child), or less. About 14 million *additional* children in low-income working families would get less than the full credit increase of $650 per child (though more than $75) — in most cases, much less. Altogether, 1 in 3 children under age 17 in working families would receive a token or a partial increase because their earnings are too low to qualify for the full benefit.

FIGURE 1



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The Senate Republicans' decision to provide such small benefits to low- and moderate-income working families is especially striking because they also chose to newly extend the CTC to families with much higher incomes. Married couples with two children with incomes between $150,000 and $1,066,000 would become newly eligible for the credit.

[5] Chuck Marr *et al.,* "House Tax Bill's Child Tax Credit Increase Excludes Thousands of Children in Low-Income Working Families in Every State," CBPP, November 9, 2017, https://www.cbpp.org/research/federal-tax/house-tax-bills-child-tax-credit-increase-excludes-thousands-of-children-in-low.

Under the bill, a single mother with two children working full-time as a home health aide at the federal minimum wage and earning $14,500 would see a $75 increase in her CTC, while a married couple with two children earning $1,000,000 would be receive a *new* CTC worth $3,300. (See Figure 1.)

Bill Would Reduce States' Ability to Fund Education, Health Care, Other Services

The Senate bill would eliminate the federal deduction for state and local taxes (SALT), going beyond the already damaging House provision.[6] It would use the revenues raised by repeal to help pay for large federal tax cuts for wealthy households and corporations — a bad trade for most Americans.

That's because the SALT deduction helps state and local governments fund public services that provide widely shared benefits. Because of the deduction, higher-income filers are more willing to support state and local taxes. Repealing the deduction would almost certainly make it harder for states and localities — many of which already face serious budget strains — to raise sufficient revenues in the coming years to invest in high-quality education, infrastructure, and other priorities that are crucial to the nation's long-term economic prospects.[7] State borrowing costs could also rise as bond rating agencies react to states' reduced capacity to raise adequate revenue, making needed infrastructure projects more expensive.

States and localities could respond to this squeeze by cutting services that have broadly shared benefits. Or they could raise other taxes or fees, which would push more costs on to middle- and low-income people and make state and local tax systems even more regressive overall than they already are.[8] Either way, low- and middle-income Americans would end up bearing the burden of repealing a provision used to finance tax cuts heavily tilted towards the top.

Further, this added budget squeeze on states and localities comes as the President and congressional Republicans propose in their ten-year budget plans to shift substantial *new* costs to states, by sharply cutting Medicaid and other health funding and potentially cutting federal support for state and local services such as education, transportation, environmental protection, and low-income housing.[9]

By raising deficits, the tax bill would make enactment of these budget cuts much more likely.

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[6] Michael Leachman, "Senate Tax Plan's End to SALT Deduction a Poor Trade for Tax Cuts for Wealthy," CBPP, November 9, 2017, https://www.cbpp.org/blog/senate-tax-plans-end-to-salt-deduction-a-poor-trade-for-tax-cuts-for-wealthy.

[7] Elizabeth McNichol and Samantha Waxman, "States Faced Revenue Shortfalls in 2017 Despite Growing Economy," CBPP, updated October 4, 2017, https://www.cbpp.org/research/state-budget-and-tax/states-faced-revenue-shortfalls-in-2017-despite-growing-economy.

[8] Institute on Taxation and Economic Policy, "Who Pays Taxes in America in 2017?" April 13, 2017, https://itep.org/who-pays-taxes-in-america-in-2017/.

[9] Iris J. Lav and Michael Leachman, "The Trump Budget's Massive Cuts to State and Local Services and Programs," CBPP, June 13, 2017, https://www.cbpp.org/research/state-budget-and-tax/the-trump-budgets-massive-cuts-to-state-and-local-services-and.