

THE “MOTHER OF ALL DISTORTIONS”: ATTACKS ON RANGEL AMT PLAN NOT BASED ON REALITY

Republican congressional leaders have sharply attacked House Ways and Means Chairman Rangel’s proposal to replace the Alternative Minimum Tax with a tax surcharge for very-high-income households as a massive tax increase that would seriously damage, even “doom,” the economy. In fact, however, the Rangel plan is *not* a tax increase. Moreover, it would create a tax system that is simpler, more progressive, and likely better for the economy than either current law or the idea favored by many of the plan’s critics: eliminating the AMT without paying for it.

Fact #1: The Rangel proposal is not a tax increase; it would raise the same amount of revenue as the current AMT. Because it is revenue-neutral, it would not add to future deficits.

- In contrast, eliminating the AMT without paying for it would add up to \$2 trillion to deficits over the coming decade (2008-2017).¹ This would significantly worsen the nation’s already-grim long-term budget outlook, forcing much larger tax increases or spending cuts, or both, than would otherwise be needed to restore fiscal stability.
- Continuing the “patch” to keep the AMT from spreading into the middle and upper-middle class would be cheaper, but not by much, adding \$1.3 trillion to deficits over the next decade if the 2001 and 2003 tax cuts are extended but not paid for. If Congress allows the tax cuts to expire or pays for their extension, continuing the patch would still add \$791 billion to deficits.

Fact #2: Nearly 90 million households would pay less in taxes under Rep. Rangel’s tax bill as a whole; fewer than 4 million would pay more.

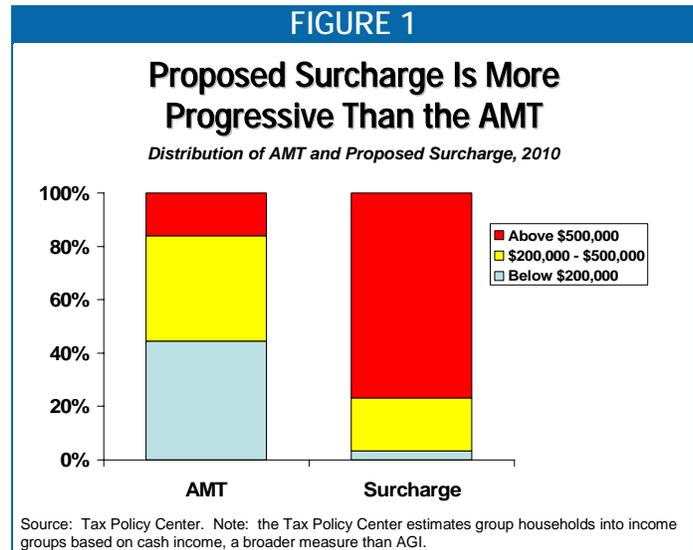
- Congress’s Joint Committee on Taxation estimates that the Rangel bill as a whole (which includes the AMT proposal plus other changes in income taxes) would cut taxes for 90 million households. Similarly, the Urban-Brookings Tax Policy Center estimates that 86 million households would get a tax cut from the legislation in 2008, while 3.7 million households would get a tax increase. The claim by some House Republicans that the bill would raise taxes for more than 100 million households is incorrect and based on severe misuse of Joint Tax Committee analysis.²

¹ Eliminating the AMT would cost \$2 trillion over the next decade if the 2001 and 2003 tax cuts are extended. Typically, proponents of eliminating the AMT without paying for it also urge that these tax cuts also be extended without offsets.

² See “Ways and Means Committee Republicans’ Use of Joint Tax Committee Data Is Deeply Deceptive,” Center on Budget and Policy Priorities, revised November 12, 2007, <http://www.cbpp.org/11-9-07tax.htm>.

Fact #3: The Rangel AMT proposal would be more progressive than the current AMT. Also, because the proposed surcharge would be indexed to inflation, it would never grow to affect middle-class households, as the AMT is set to do.

- The surcharge would not affect middle- and upper-middle-income households, because no married couple with adjusted gross income below \$200,000 would owe it, and that threshold would be indexed to inflation.
- For the typical household in the \$200,000 to \$500,000 range, the surcharge would cost only about half as much as the AMT would. The vast bulk of the revenue from the surcharge would be paid by households above \$500,000, as Figure 1 shows.



- Only the highest-income 3 percent of households would pay the surcharge. The vast majority of them benefited handsomely from the 2001 and 2003 tax breaks, and the surcharge would reduce, but not eliminate, those tax cuts. People making over \$1 million a year would still get net tax cuts averaging \$21,000 in 2008.

Fact #4: The Rangel proposal would make the tax code more efficient. In addition, because it would not increase the deficit, it would likely be better for the economy than repealing or reducing the AMT without paying for it.

- The surcharge would apply to a broader base of income than the AMT does and, therefore, taxpayers could not easily avoid it by shifting income into a different form (e.g., converting ordinary income into capital gains). Researchers have found that because taxes levied on a broader income base provide less incentive for income-shifting, they induce fewer economic distortions and are more efficient economically than taxes levied on a narrower base.
- Studies by the Joint Committee on Taxation, the Brookings Institution, and various noted economists suggest that lowering marginal tax rates will likely *harm* the economy over the long run if the tax reductions are financed by larger deficits. Thus, the Rangel proposal, which would *raise* marginal tax rates for a small percentage of households in order to *avert* an increase in deficits resulting from AMT repeal, is probably better for the economy than deficit-financed AMT repeal or reduction.

Fact #5: The Rangel proposal would be much simpler to calculate than the AMT.

- The AMT is widely regarded as complicated to compute. The surcharge, in contrast, would be extremely simple: it would just apply a tax rate to the portion of a taxpayer's adjusted gross income above a given threshold. Since filers must already report their adjusted gross income on their tax forms, the surcharge would add only seconds to the process of computing one's taxes, even for those who prepare their returns without the help of special software.