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RECONCILIATION TAX CUTS WOULD AVERAGE $43,000 FOR HOUSEHOLDS WITH INCOME OVER $1 MILLION, BUT ONLY $20 FOR MIDDLE-INCOME HOUSEHOLD

By Joel Friedman

The final agreement on the $70 billion tax-cut reconciliation package offers virtually no benefits to low- and moderate-income households, but showers high-income households with very large tax cuts.

The Urban Institute-Brookings Institution Tax Policy Center has examined the major provisions that are in the package, including a two-year extension of capital gains and dividend tax cuts, a one-year extension of relief from the Alternative Minimum Tax, and a proposal to lift the income limits that apply to converting retirement funds to Roth IRAs. Estimates by the Tax Policy Center show that: [1]

- About 87 percent of the benefits of the reconciliation conference agreement would flow to the 14 percent of households with incomes above $100,000, and 55 percent of the benefits would go to the 3 percent with incomes above $200,000. Households earning more than $1 million a year, which represent only 0.2 percent of all households, would receive 22 percent of the benefits of these tax cuts.

- In contrast, the three-quarters of households with incomes below $75,000 would receive just 5 percent of the benefits. The 60 percent of households with incomes below $50,000 would receive less than 2 percent of all benefits. In total, 68 percent of all households would receive *no* benefits whatsoever from the tax-cut package.

- Looked at in dollar terms, the differential treatment of various income groups is even more striking. The average tax cut for the 20 percent of households in the middle of the

Distribution of Major Reconciliation Tax Cuts (Assuming They Are Fully In Effect in 2006)

Income Class	Average Tax Cut
Middle 20 percent	$20
Top 1 percent	$14,100
Over $1 million	$43,000

Source: Urban-Brookings Tax Policy Center

[1] The various provisions that are expected to be in the final reconciliation bill will be in effect during different years. To estimate the distributional effects of the bill as a whole, the Tax Policy Center employed the simplifying assumption that all of the provisions would be in effect in 2006. Our distributional estimates have been updated to reflect the Tax Policy Center's most recent distributional figures.

income spectrum would be just $20. But the average tax cut for those in the top one percent of the income spectrum would be $14,100.[2] For those with incomes above $1 million, the average tax cut would be $43,000.

The reconciliation agreement provides such large tax breaks to the highest income households largely because of the capital gains and dividend tax cuts, which the Administration and Congressional leaders pushed hard to include in the bill. Nearly half (45 percent) of the benefit of extending these tax cuts would go to households with incomes of more than $1 million, according to Tax Policy Center estimates. Supporters of these tax cuts like to claim that the benefits of these tax cuts are widespread, but they typically fail to acknowledge that, for less well-off households, the tax cut only amounts to a few dollars, reflecting the modest amount of taxable assets these taxpayers hold.[3]

The benefits from lifting the income limits that apply to converting traditional IRAs to Roth IRAs are also sharply skewed to high-income households.[4] Only households with income above $100,000 are prohibited from making such conversions under current law, so lifting that limit would benefit only those households. Households with lower incomes would receive no benefit from this tax cut, as they are able to make such conversions now. Tax Policy Center estimates show that about three-quarters of the benefits of the Roth IRA proposal would flow to households with incomes above $200,000, and nearly 35 percent of the benefits would go to households with incomes of over $1 million.

The legislation's AMT relief would also flow primarily to households with incomes above $100,000. However, unlike the benefits of the investment tax cuts and the Roth IRA proposal, the majority of which go to households with incomes above $500,000, the benefits of AMT relief are concentrated on those households with incomes between $100,000 and $500,000, according to the Tax Policy Center. These households would receive about 80 percent of AMT relief. Those with higher incomes are less affected by the AMT, so receive fewer benefits from AMT relief.

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[2] The Tax Policy Center estimates of the average tax cuts for the different quintiles are as follows: bottom quintile is $0; second quintile is $7; middle quintile is $20; fourth quintile is $117; and the top quintile is $2,119. See Tax Policy Center Tables T06-0085 and T06-0086 at http://www.taxpolicycenter.org.

[3] For more detail, see Joel Friedman and Katharine Richards, "Capital Gains And Dividend Tax Cuts: Data Make Clear That High-Income Households Benefit The Most," Center on Budget and Policy Priorities, January 30, 2006.

[4] This proposal is included in the package as a way to "offset" a portion of the cost of the capital gains and dividend tax cuts after 2010. This is a gimmick of that uses timing shifts to make it appear as though one tax cut that loses revenue is offsetting the cost of another tax cut that loses revenue. For a discussion of the gimmick, see Joel Friedman and Aviva Aron-Dine, "Tax Reconciliation Agreement Distorted By Obsession With Capital Gains And Dividend Tax Cuts," Center on Budget and Policy Priorities, May 11, 2006.