TAX POLICY CENTER
URBAN INSTITUTE & BROOKINGS INSTITUTION

A PRELIMINARY ANALYSIS OF THE UNIFIED FRAMEWORK

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October 27, 2017

ABSTRACT

The Tax Policy Center has produced preliminary estimates of the potential impact of proposals included in the "Unified Framework for Fixing Our Broken Tax Code." We find they would reduce federal revenue by $2.4 trillion over ten years and $3.2 trillion over the second decade (not including any dynamic feedback). Including economic feedback, revenue would fall by between $2.4 trillion and $2.5 trillion over the first ten years and by about $3.4 trillion over the second decade. In 2018, all income groups would see their average taxes fall, but some taxpayers in each group would face tax increases. Those with the very highest incomes would receive the biggest tax cuts. The tax cuts overall are smaller as a percentage of income in 2027, and taxpayers in the 80th to 95th income percentiles would, on average, experience a tax increase.

This paper was updated on October 27, 2017 to incorporate macroeconomic estimates produced by TPC and the Penn Wharton Budget Model.

The findings and conclusions contained within are those of the authors and do not necessarily reflect positions or policies of the Urban Institute, the Brookings Institution or their funders.

The Penn Wharton Budget Model (PWBM) is an integrated static microsimulation and dynamic policy analysis model available to the public. A third party—typically, a policymaker, federal agency or a think tank—is welcome to use the dynamic component of the PWBM model with the third party's own static estimates. Those dynamic estimates, however, might differ, potentially significantly, from the PWBM's own dynamic estimates based on PWBM's own static estimates.

On September 27, 2017, the White House and the congressional Republican leadership (the "Big Six") released their "Unified Framework for Fixing Our Broken Tax Code." The framework would collapse the seven individual income tax rates to three (12, 25, and 35 percent), increase the standard deduction, eliminate personal exemptions, increase the child tax credit, eliminate most itemized deductions, repeal the individual and corporate alternative minimum taxes, repeal the estate tax, reduce the corporate tax rate from 35 to 20 percent, tax pass-through business income at a top rate of 25 percent, allow businesses to fully expense investment in equipment and machinery for at least five years, and adopt a territorial tax system that would exempt the foreign earnings of US corporations from US tax.

Many aspects of the plan were unspecified or left to be determined by the tax writing committees in Congress. The Tax Policy Center (TPC) has completed a preliminary analysis of the proposals contained in the unified framework based on previous proposals such as the House Republican leadership's "A Better Way" blueprint and the Trump administration's April outline. While the revenue, distributional, and economic effects are likely to change as policy makers negotiate the details, this analysis provides an estimate of the effects of the September 27 framework as we currently understand it.

This report presents results calculated in two ways: using conventional scoring methods that assume the tax proposals do not affect the overall level of economic activity, and incorporating macroeconomic feedbacks. Those macroeconomic feedbacks were estimated using both TPC's own models of the economy and the Penn Wharton Budget Model (PWBM), based on the revenue effects and marginal tax rates derived from the TPC microsimulation model. TPC's models and the PWBM using TPC inputs both estimate relatively modest effects of the Framework on the economy, despite modeling the economy in fundamentally different ways.[1]

RESULTS AT A GLANCE

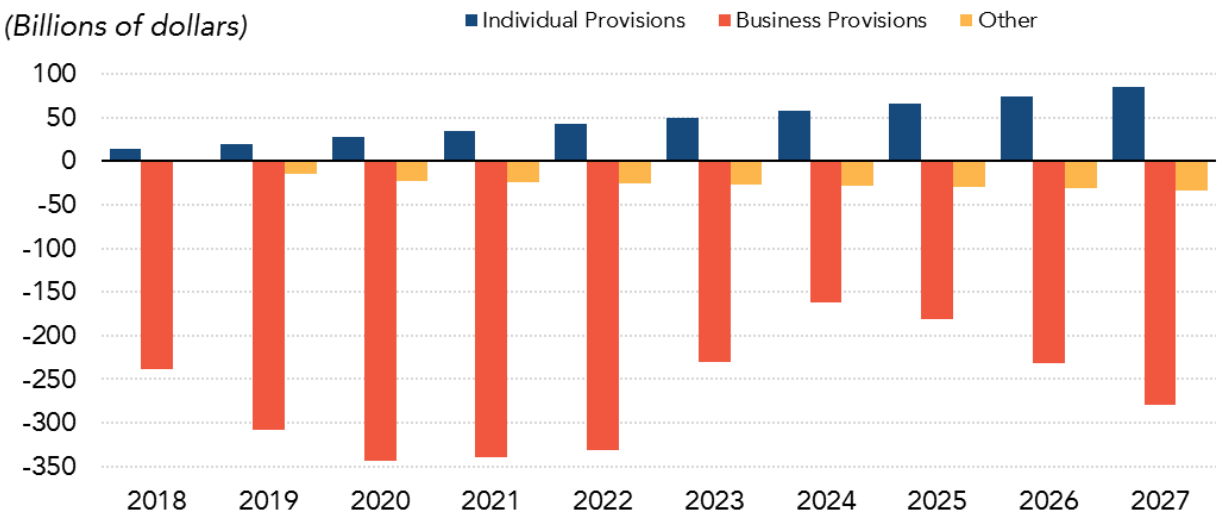
TPC estimates that, including macroeconomic effects, the proposal would reduce federal revenues by between $2.4 and $2.5 trillion over the first ten years and by about $3.4 trillion over the subsequent decade. Macroeconomic feedback is projected either to expand or reduce the revenue loss of the plan slightly over the first decade, and increase it over the second.

Excluding macroeconomic effects, the proposal would reduce federal revenues by $2.4 trillion over the first ten years and $3.2 trillion over the subsequent decade. The business income tax provisions—including those affecting corporations and pass-through businesses—would reduce revenues by $2.6 trillion over the first ten years. Elimination of estate and gift taxes would lose another $240 billion. The individual income tax provisions (excluding those related to business income) would increase revenues by about $470 billion over the same period.

FIGURE 1

Revenue Effects of Tax Proposals in the Unified Framework

FY 2018-27, excluding macroeconomic effects



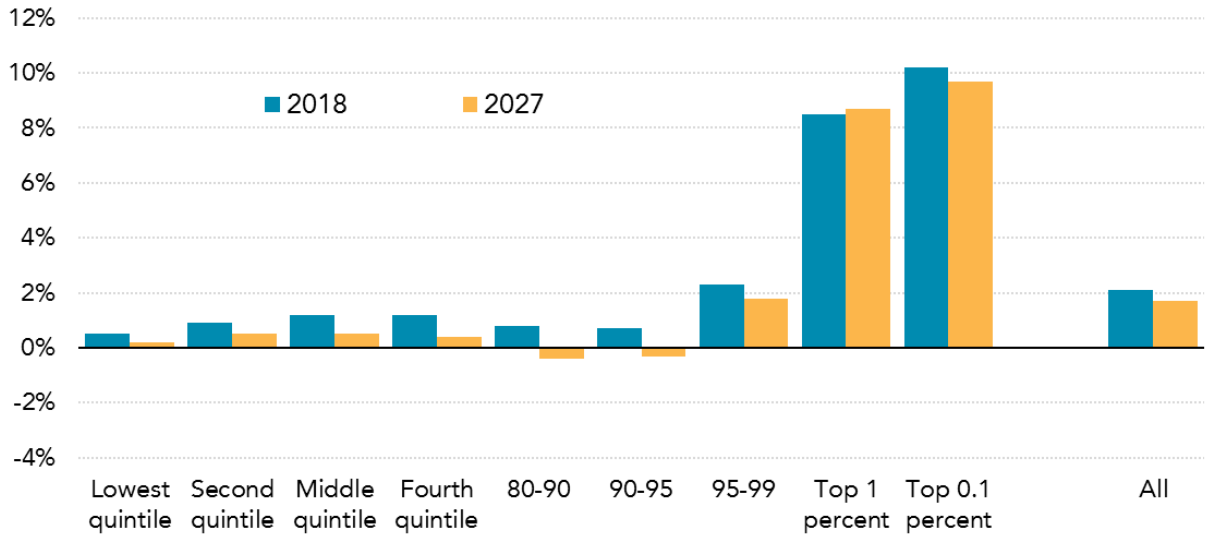
Source: Urban-Brookings Tax Policy Center (TPC) Microsimulation Model (version 0217-1) and TPC calculations.
Note: Other includes repealing the estate and GST (generation skipping transfer) taxes.

In 2018, the average tax bill for all income groups would decline. Taxpayers in the bottom 95 percent of the income distribution would see average after-tax incomes increase between 0.5 and 1.2 percent. Taxpayers in the top 1 percent (incomes above $730,000), would receive about 50 percent of the total tax benefit; their after-tax income would increase an average of 8.5 percent. Between 2018 and 2027, the average tax cut as a share of after-tax income would fall for all income groups other than the top 1 percent. In 2027, taxpayers between the 80th and 95th percentiles of income (between about $150,000 and $300,000) would experience a slight tax increase on average.

FIGURE 2

Percent Change in After-tax Income From Proposals in the Unified Framework

By expanded cash income percentile, 2018 and 2027



Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1).
Note: Estimates exclude macroeconomic effects.

OVERVIEW OF THE UNIFIED FRAMEWORK

The framework includes tax rates, standard deduction amounts, and other important tax policy parameters. However, it does not specify the income brackets to which the individual tax rates would apply, the maximum size and phase-out parameters of the increased child tax credit, or details about the treatment of tax expenditures and other preferences. Below we summarize the main proposals included in the unified framework. To perform our analysis, we made many key assumptions that are detailed in appendix A. We assume that all provisions (except the expensing of certain investments; see below) would be effective January 1, 2018.

Individual Provisions

The framework includes the following proposals that would change the individual income tax, excluding those related to pass-through income:

- Repeal the alternative minimum tax.
- Set individual income tax rates of 12, 25, and 35 percent. (The framework allows for a possible fourth rate above 35 percent if needed to achieve distributional goals. While the framework does not specify the income levels to which the rates would apply, we base our analysis on the brackets proposed in the House Republican leadership's "A Better Way" blueprint.)

- Increase the standard deduction to $12,000 for single filers and $24,000 for joint filers.
- Increase the child credit and raise the income level at which the credit phases out for joint filers.
- Create a $500 nonrefundable credit for "non-child dependents."
- Repeal all personal exemptions for taxpayers and dependents.
- Repeal most itemized deductions other than those for mortgage interest and charitable contributions.
- Repeal other exemptions, deductions, and credits. (The framework does not specify any of the exemptions, deductions, or credits that would be repealed, but does say it would retain incentives for retirement saving and education.)
- Use an alternative measure of inflation to index tax brackets and other tax parameters.

Business Provisions

The framework also includes the following business income tax provisions:

- Reduce the maximum tax rate on income from pass-through businesses to 25 percent. (The framework suggests it would adopt rules to prevent taxpayers from recharacterizing wage and other income as pass-through income but it offers no specifics.)
- Reduce the corporate income tax rate to 20 percent and repeal the corporate alternative minimum tax.
- Allow full expensing for new investments in depreciable property other than structures for at least five years (effective September 28, 2017).
- Partially limit the ability of corporations to deduct net interest. (The framework offered no specifics on how this limit might work.)
- Repeal the domestic production activities deduction (Section 199) and some business credits (excluding the research and experimentation (R&E) and low-income housing (LIHC) credits).
- Repeal other business-related special exclusions and deductions. (The framework does not specify any of the special exclusions or deductions that would be repealed.)
- Adopt a territorial system of taxing foreign-source income with provisions to limit avoidance and impose a one-time tax on unrepatriated foreign earnings.

Other Provisions

- Repeal the estate tax and generation-skipping transfer taxes.

REVENUE EFFECTS

Using conventional scoring methods, we estimate that the proposals contained in the framework would reduce federal tax revenues by $2.4 trillion over the first decade and by $3.2 trillion over the following decade (table 1).

Over the first 10 years, the individual income tax provisions—excluding those related to the taxation of corporations, pass-throughs, and estates—would raise $470 billion, the business provisions would reduce revenues by $2.6 trillion, and repealing the estate tax would cost another $240 billion. The revenue gain from these individual provisions would increase over the ten-year budget window. The revenue loss from the business income tax provisions would be higher in the first five years because expanded business expensing expires after that period.

Over the following decade (fiscal years 2028–37), the individual provisions would raise much more revenue, $1.4 trillion, while the business provisions would lose much more revenue, $4.1 trillion, and estate tax repeal would cost an additional $440 billion. The resulting overall revenue loss would be $3.2 trillion.

TABLE 1

Revenue Effects of Tax Proposals in the Unified Framework

Billions of dollars, fiscal years 2018–37

Provision	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2018-27	2028-37
Individual Provisions												
Repeal individual alternative minimum tax	-26.6	-36.7	-39.3	-41.6	-43.7	-45.7	-47.9	-50.4	-52.7	-54.9	-439.5	-713.9
Individual income tax rates of 12, 25, and 35%	-70.1	-97.7	-102.4	-107.9	-113.9	-120.3	-127.5	-135.3	-143.2	-151.4	-1,169.6	-2,015.6
Increase standard deduction	-60.0	-79.8	-80.5	-81.5	-83.5	-85.4	-86.7	-89.2	-91.0	-92.8	-830.4	-1,120.7
Increase child credit to $1,500 and enact $500 non-child dependent credit	-20.5	-27.7	-27.8	-27.9	-28.0	-27.9	-27.9	-27.8	-27.8	-27.6	-271.0	-271.1
Repeal personal exemptions	104.2	142.7	147.7	152.8	157.9	163.0	169.5	175.2	180.6	187.4	1,581.1	2,292.7
Repeal state and local tax deduction	78.3	103.4	110.2	118.5	126.2	134.2	142.9	152.2	162.1	172.0	1,300.0	2,340.8
Repeal most other itemized deductions	8.3	12.0	13.5	14.9	16.5	18.1	19.7	21.6	24.1	26.7	175.5	375.6
Index tax system using chain-weighted CPI	1.1	3.5	6.2	7.7	10.7	13.0	16.0	19.5	22.2	25.1	125.0	484.9
Repeal other individual tax preferences	*Insufficient detail to estimate*											
Subtotal	**14.6**	**19.8**	**27.7**	**35.0**	**42.2**	**49.0**	**58.0**	**65.9**	**74.3**	**84.5**	**471.0**	**1,372.6**
Business Provisions												
Limit individual tax rate on pass-through income to 25% [a]	-38.2	-55.6	-61.4	-67.8	-75.0	-80.9	-87.0	-93.8	-101.1	-108.9	-769.6	-1,459.4
Reduce corporate rate to 20% and repeal corporate AMT	-87.6	-173.0	-204.3	-202.9	-205.4	-209.1	-215.2	-222.1	-230.2	-239.5	-1,989.4	-2,990.6
Expensing of equipment through 2022	-130.0	-109.5	-112.9	-104.6	-86.1	23.6	104.3	99.2	73.0	51.1	-191.9	146.6
Partial limit on the corporate deduction for net interest	*Insufficient detail to estimate*											
Enact territorial tax system	-3.7	-7.5	-8.6	-8.9	-9.2	-9.6	-9.9	-10.3	-10.8	-11.2	-89.6	-139.6
One-time deemed repatriation tax at reduced rates	9.0	18.1	20.1	20.1	20.1	20.1	20.1	20.1	11.1	2.0	160.9	0.0
Repeal certain business tax expenditures	10.1	19.6	22.9	24.0	24.6	25.1	25.6	26.2	26.7	27.2	232.1	307.3
Repeal other business tax preferences	*Insufficient detail to estimate*											
Subtotal	**-240.3**	**-307.9**	**-344.2**	**-340.0**	**-330.9**	**-230.7**	**-162.1**	**-180.8**	**-231.3**	**-279.3**	**-2,647.6**	**-4,135.7**
Other Provisions												
Repeal estate and GST taxes	0.0	-15.3	-22.8	-24.7	-25.8	-27.0	-28.5	-30.0	-31.6	-33.2	-238.9	-443.3
Subtotal	**0.0**	**-15.3**	**-22.8**	**-24.7**	**-25.8**	**-27.0**	**-28.5**	**-30.0**	**-31.6**	**-33.2**	**-238.9**	**-443.3**
Total Without Macroeconomic Feedback	**-225.7**	**-303.4**	**-339.4**	**-329.7**	**-314.5**	**-208.6**	**-132.5**	**-145.0**	**-188.7**	**-228.0**	**-2,415.5**	**-3,206.4**
Difference in Total Revenue Change Due to Macroeconomic Feedback												
TPC models	30.7	25.6	13.9	5.2	-1.7	-4.9	-3.9	-3.7	-4.0	-5.2	51.9	-155.3
PWBM using TPC inputs	3.7	5.8	7.4	2.1	0.5	-19.1	-21.2	-16.7	-9.8	-8.1	-55.5	-175.7
Total With Macroeconomic Feedback												
TPC models	**-195.0**	**-277.9**	**-325.5**	**-324.5**	**-316.2**	**-213.6**	**-136.4**	**-148.7**	**-192.7**	**-233.2**	**-2,363.6**	**-3,361.7**
PWBM using TPC inputs	**-222.0**	**-297.6**	**-332.0**	**-327.5**	**-314.0**	**-227.8**	**-153.7**	**-161.7**	**-198.5**	**-236.1**	**-2,471.0**	**-3,382.1**

Sources: Urban-Brookings Tax Policy Center (TPC) Microsimulation Model (version 0217-1) and TPC calculations.
Note: AMT = alternative minimum tax; CPI = consumer price index; GST = generation skipping transfer.

(a) Includes revenue effects of taxpayers re-characterizing wage income to qualify for the lower rate on pass-through income of (in billions of dollars):
FY2018 -1.6, FY2019 -4.0, FY2020 -6.8, FY2021 -10.1, FY2022 -13.7, FY2023 -15.6, FY2024 -17.0, FY2025 -18.3, FY2026 -19.9, FY2027 -21.4, FY2018-2027 -128.5, FY2028-2037 -298.5.

DISTRIBUTIONAL EFFECTS

In 2018, taxes would decline by nearly $1,600 on average, increasing after-tax incomes by 2.1 percent (table 2). Taxpayer groups in the bottom 95 percent of the income distribution would see modest tax cuts, averaging 1.2 percent of after-tax income or less. The benefit would be largest for taxpayers in the top 1 percent (those making more than $730,000), who would see their after-tax income increase 8.5 percent.

In 2018, about 12 percent of taxpayers would face a tax increase of roughly $1,800 on average. More than a third of taxpayers making between about $150,000 and $300,000 would pay more, mainly because most itemized deductions would be repealed.

In 2027, the overall average tax cut would be smaller than in 2018, increasing after-tax incomes 1.7 percent (table 3). Taxpayer groups in the bottom 80 percent of the income distribution—those making less than about $150,000—would receive average tax cuts of 0.5 percent or less of after-tax income. Taxpayers making between about $150,000 and $300,000 would on average pay about $800 more in taxes than under current law. About 80 percent of the total benefit would accrue to taxpayers in the top 1 percent, whose after-tax income would increase 8.7 percent. An alternative presentation of the distributional effects of the framework is available in appendix B.

By 2027, taxes would rise for roughly one-quarter of taxpayers, including nearly 30 percent of those with incomes between about $50,000 and $150,000 and 60 percent of those making between about $150,000 and $300,000. The number of taxpayers with a tax increase rises over time. This is because the plan would replace personal exemptions, which are indexed for inflation, with additional credits for children and non-child dependents that are not indexed for inflation. In addition, indexing tax brackets and other parameters to the slower-growing chained Consumer Price Index means that over time more income is subject to tax at higher rates.

TABLE 2

Distribution of Federal Tax Change From Proposals in the Unified Framework

By expanded cash income percentile, 2018[a]

Expanded cash income percentile[b]	Tax units with tax cut or increase				Percent change in after-tax income[c]	Share of total federal tax change (%)	Average federal tax change	Average federal tax rate[d]	
	With tax cut		With tax increase					Change (% points)	Under the proposal (%)
	Percent of tax units	Average tax cut	Percent of tax units	Average tax increase					
Lowest quintile	70.9	-90	1.2	280	0.5	1.1	-60	-0.4	3.7
Second quintile	87.9	-370	6.4	530	0.9	4.1	-290	-0.8	7.9
Middle quintile	85.4	-940	13.5	1,000	1.2	8.2	-660	-1.0	12.8
Fourth quintile	79.4	-1,860	20.4	1,790	1.2	11.6	-1,110	-1.0	16.4
Top quintile	67.5	-13,930	32.3	2,880	3.3	74.5	-8,470	-2.4	23.0
All	78.4	-2,290	12.2	1,840	2.1	100.0	-1,570	-1.7	18.1
Addendum									
80-90	67.0	-2,810	32.7	2,280	0.8	5.1	-1,140	-0.6	19.5
90-95	59.5	-4,490	40.2	2,920	0.7	3.3	-1,500	-0.6	21.4
95-99	73.5	-11,560	26.5	3,320	2.3	12.8	-7,620	-1.7	23.5
Top 1 percent	89.3	-146,470	10.7	17,970	8.5	53.3	-129,030	-5.7	26.8
Top 0.1 percent	97.5	-747,580	2.4	265,040	10.2	30.3	-722,510	-6.8	26.6

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1)

Notes: Number of Alternative Minimum Tax (AMT) taxpayers (millions): Baseline: 5.2; Proposal: 0.

(a) Calendar year. Baseline is current law. Estimates exclude macroeconomic effects.

(b) Percentiles include both filing and non-filing 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. 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 2017 dollars): 20% $25,000; 40% $48,600; 60% $86,100; 80% $149,400; 90% $216,800; 95% $307,900; 99% $732,800; 99.9% $3,439,900. For a description of expanded cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm

(c) 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.

(d) 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 3

Distribution of Federal Tax Change From Proposals in the Unified Framework

By expanded cash income percentile, 2027[a]

Expanded cash income percentile[b]	Tax units with tax cut or increase				Percent change in after-tax income[c]	Share of total federal tax change (%)	Average federal tax change	Average federal tax rate[d]	
	With tax cut		With tax increase					Change (% points)	Under the proposal (%)
	Percent of tax units	Average tax cut	Percent of tax units	Average tax increase					
Lowest quintile	62.6	-100	9.3	190	0.2	0.8	-50	-0.2	4.1
Second quintile	71.6	-460	19.8	510	0.5	3.0	-230	-0.5	8.4
Middle quintile	70.8	-1,100	27.8	1,290	0.5	4.9	-420	-0.5	13.4
Fourth quintile	66.5	-1,920	33.1	2,510	0.4	4.3	-450	-0.3	16.7
Top quintile	46.4	-27,910	53.4	4,400	3.0	86.6	-10,610	-2.2	24.0
All	64.7	-3,480	25.3	2,220	1.7	100.0	-1,690	-1.4	18.8
Addendum									
80-90	41.4	-3,250	58.4	3,710	-0.4	-3.5	820	0.4	20.1
90-95	38.4	-5,110	61.5	4,420	-0.3	-1.5	760	0.2	22.1
95-99	59.6	-16,200	40.3	4,990	1.8	11.9	-7,640	-1.4	24.2
Top 1 percent	90.1	-234,050	9.8	39,350	8.7	79.7	-207,060	-5.8	27.6
Top 0.1 percent	97.0	-1,071,340	3.0	549,600	9.7	39.6	-1,022,120	-6.4	27.4

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1)

Notes: Number of Alternative Minimum Tax (AMT) taxpayers (millions): Baseline: 5.6; Proposal: 0.

(a) Calendar year. Baseline is current law. Estimates exclude macroeconomic effects.

(b) Percentiles include both filing and non-filing 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. 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 2017 dollars): 20% $28,100; 40% $54,700; 60% $93,200; 80% $154,900; 90% $225,400; 95% $304,600; 99% $912,100; 99.9% $5,088,900. For a description of expanded cash income, see http://www.taxpolicycenter.org/TaxModel/income.cfm

(c) 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.

(d) 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.

DYNAMIC EFFECTS ON THE ECONOMY

In addition to the conventional estimates presented above, which are based on fixed economic assumptions, TPC also estimated the Unified Framework taking into account macroeconomic feedback effects. Those "dynamic" estimates reflect the proposal's short-run impact on aggregate demand as well as its longer-term effects on saving, investment, and labor supply. TPC's models and the PWBM reflect the middle range of estimates from economic research on the impact of fiscal policy on the economy, and are similar to models used by the nonpartisan analysts at the Joint Committee on Taxation and the Congressional Budget Office.

Aggregate Demand

The Framework would increase aggregate demand, and therefore output, in two main ways. First, by reducing average tax rates for most households, it would increase after-tax incomes. By spending some of that additional income, households would increase demand for goods and services. However, these economic benefits would be relatively modest because most tax reductions would accrue to high-income households, who spend a smaller share of any increases in after-tax income than lower-income households. Second, by allowing businesses to elect to expense investment over the next five years, the Framework would encourage firms to increase their near-term investment spending, further increasing demand. This effect would raise output relative to its potential level for several years until higher interest rates and prices caused output to return to its long-run potential level. Because the economy is near full employment, the impact of increased demand on output would be smaller, and diminish more quickly, than it would if the economy were in recession.

Saving and Investment

The Framework would, on average, increase tax rates on various types of investment income for lower income households, but reduce them for higher income households (table 4). Since most investment income is earned by higher income households, those changes would on average reduce taxes on investment income, increasing the after-tax rate of return to saving. This would encourage households to save a larger share of their income, increasing the amount of saving and investment in the US economy.

The overall effect of taxes on incentives to save and invest can be shown through marginal effective tax rates (METRs) on new investments. The METR is a forward-looking measure of how taxes affect the rate of return of a hypothetical marginal investment project (i.e., one that would just break even). We compare the METR for different investments under the Framework with the METR under current law. Largely because the plan would reduce the corporate income tax rate and the top rate on business income of individuals and temporarily allow businesses to

expense investment, METRs on most new business investment would decrease significantly—from 17.0 to 12.7 percent, on average (table 5). That decline would encourage saving, foreign capital inflows, and investment.

Although the framework would increase incentives to save and invest, it would also substantially increase budget deficits unless offset by spending cuts. Higher deficits would push up interest rates, which would crowd out investment. Thus, while the plan would initially increase investment, TPC estimates that rising interest rates would eventually negate the incentive effects of lower tax rates on capital and decrease investment below baseline levels in later years.

Labor Supply

The Framework would modestly reduce effective tax rates on labor income (i.e., wages and salaries for employees and self-employment income for others), primarily by reducing marginal income tax rates for most workers (table 6). Because they increase the after-tax wage rate, lower marginal tax rates on labor income increase labor supply, mostly by encouraging lower-earning spouses to work more hours. Along with increased investment, which raises worker productivity and wages, these effects would initially raise workers' earnings and therefore tax receipts. However, because the plan causes budget deficits that would eventually reduce investment and the capital stock, it would also ultimately depress both market wages and labor supply.

Output and Revenues

TPC and PWBM using TPC inputs estimate that the Framework would boost GDP by between 0.3 and 0.9 percent in fiscal year 2018. In 2027 the estimated effect on GDP would range from a reduction of 0.1 percent to an increase of 0.3 percent, and in 2037 it would range from a reduction of 0.4 percent to a reduction of 0.1 percent (table 7). The estimated effects on output become more negative over time primarlily due to the crowding out effects of rising deficits.

Because the Framework is estimated to increase net inflows of foreign capital investment, it would also increase payments of profits and interest to foreign investors out of domestic production. Those payments do not affect GDP, but do reduce gross national product (GNP), which is a better measure of the proposal's effect on US incomes. TPC's models estimate that the Framework would reduce GNP by about 0.2 percent in 2027 and 0.6 percent in 2037 (compared with estimated reductions of 0.1 percent and 0.4 percent for GDP in those years).

The economic effects of the Framework would in turn alter the revenue effect of the proposal, increasing them (relative to revenues before macro feedback) by between $4 billion and $31 billion in fiscal year 2018. Between 2018 and 2027 the estimated feedback effect ranges from an increase of $52 billion to a decrease of $56 billion, and between 2028 and 2037 it ranges from a decrease of $155 billion to a decrease of $176 billion (table 1).

Why Are the Estimated Effects on Output and Revenues Modest?

The macroeconomic effects estimated by TPC and PWBM using TPC inputs are broadly similar to those estimated by private economic forecasters.[2] In addition, TPC and PWBM have in the past estimated effects similar to the nonpartisan analyses of the Joint Committee on Taxation and the Congressional Budget Office. However, some analysts have predicted the changes proposed in the Unified Framework would have much larger effects. The estimates of TPC and PWBM using TPC inputs are more modest for several reasons.

First, the proposed cuts in business taxation affect only a fraction of the capital stock. For example, reductions in the corporate income tax rate do not directly affect the cost of investing in residential housing, which accounts for about a third of net investment and the capital stock (table 8). And the proposal to temporarily allow expensing would apply only to investment in equipment, which accounts for only about a quarter of net investment. Thus, TPC estimates that the METR on new investment would fall by only about 4 percentage points—much smaller than the Framework's proposed 15 percentage point reduction in the statutory corporate tax rate.

This reduction in the METR implies a roughly 5 percent increase in the after-tax rate of return to investment, less than a third of the amount calculated by using the change in the statutory corporate rate. A smaller increase in the after-tax return implies a smaller increase in incentives to save and invest, and a smaller impact on the economy.

Second, as noted earlier, increased government borrowing eventually pushes up interest rates, discouraging investment. We model the US as a large open economy that has access to foreign sources of investment finance, but where domestic rates of return can be influenced by large domestic policy and economic changes.

The PWBM models this by blending results based on a small open economy (where international capital flows keep domestic after-tax rates of return equal to a fixed world rate) and a closed economy (where policy changes leave capital flows unchanged). TPC bases its estimates of the impact of policy on capital flows with a fixed rule of thumb where about 24 cents of each dollar increase in the deficit is financed by inflows of foreign capital.

TABLE 4

Effective Marginal Individual Income Tax Rates on Capital Income

In percent, 2018[a]

Expanded cash income percentile[b,c]	Tax units (thousands)	Long-term capital gains			Qualified dividends			Interest income		
		Current law	Unified Framework	Change (percentage points)	Current law	Unified Framework	Change (percentage points)	Current law	Unified Framework	Change (percentage points)
Lowest quintile	48,780	1.4	2.2	0.9	0.5	0.6	0.1	1.6	1.8	0.2
Second quintile	38,760	1.5	2.3	0.8	1.0	1.4	0.5	7.0	7.6	0.6
Middle quintile	34,280	7.2	8.4	1.2	9.2	9.9	0.8	18.1	18.1	-0.1
Fourth quintile	28,870	10.4	11.8	1.4	11.0	12.0	1.0	22.5	21.5	-1.0
Top quintile	24,300	22.7	21.8	-0.9	22.1	21.0	-1.1	34.0	32.4	-1.6
All	176,100	20.7	20.1	-0.6	19.4	18.7	-0.7	27.1	26.0	-1.1
Addendum										
80–90	12,490	14.4	14.9	0.5	14.5	14.9	0.4	24.6	24.6	0.0
90–95	6,020	17.2	16.6	-0.7	16.7	16.2	-0.5	28.7	26.4	-2.3
95–99	4,650	23.3	19.8	-3.5	22.8	19.1	-3.8	35.1	32.3	-2.9
Top 1 percent	1,140	23.7	23.2	-0.5	23.9	23.3	-0.6	36.7	35.2	-1.5
Top 0.1 percent	120	23.7	23.3	-0.4	23.9	23.5	-0.4	36.0	35.0	-1.0

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1).

(a) Projections are for calendar year 2018. Effective marginal tax rates are weighted by the appropriate income source.

(b) Includes both filing and non-filing 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

(c) 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 2017 dollars): 20% $25,000; 40% $48,600; 60% $86,100; 80% $149,400; 90% $216,800; 95% $307,900; 99% $732,800; 99.9% $3,439,900.

TABLE 5

Marginal Effective Tax Rates on New Investment

In percent, 2018

Category	Current Law	Unified Framework			
		With expensing of equipment		Without expensing of equipment	
		Percent	Change (percentage points)	Percent	Change (percentage points)
Overall	**17.0**	**12.7**	**-4.3**	**14.5**	**-2.5**
Business	**23.4**	**15.6**	**-7.8**	**18.1**	**-5.3**
Corporate	25.1	17.0	-8.1	19.2	-5.9
Equipment	20.1	5.8	-14.3	15.9	-4.2
Structures	27.5	20.5	-7.0	20.5	-7.0
Intellectual property products	7.0	9.9	3.0	9.9	3.0
Inventories	38.2	27.0	-11.2	27.0	-11.2
Pass-through	20.5	13.4	-7.2	16.2	-4.3
Equipment	16.3	-0.3	-16.5	12.8	-3.5
Structures	22.6	17.7	-4.9	17.7	-4.9
Intellectual property products	3.9	4.7	0.8	4.7	0.8
Inventories	32.4	25.3	-7.2	25.3	-7.2
Owner-occupied housing	**-2.1**	**3.9**	**6.0**	**3.9**	**6.0**
Addendum					
Corporate (equity financed)	31.3	20.0	-11.3	21.8	-9.5
Corporate (debt financed)	-2.4	6.6	9.0	10.4	12.8

Source: Urban-Brookings Tax Policy Center calculations. See Rosenberg and Marron (2015) for discussion.
Notes: s.d. = standard deviation. Estimates for are calendar year 2018.

TABLE 6

Effective Marginal Individual Income Tax Rates on Wages, Salaries, and Self-Employment Income

In percent, 2018[a]

Expanded cash income percentile[b,c]	Tax units (thousands)	Individual income tax			Individual income tax plus payroll tax		
		Current law	Unified Framework	Change (percentage points)	Current law	Unified Framework	Change (percentage points)
Lowest quintile	48,780	2.8	2.2	-0.6	16.6	16.0	-0.6
Second quintile	38,760	16.2	14.3	-1.8	29.9	28.1	-1.8
Middle quintile	34,280	19.1	17.7	-1.5	32.7	31.2	-1.5
Fourth quintile	28,870	20.2	19.5	-0.7	33.8	33.1	-0.7
Top quintile	24,300	31.0	29.4	-1.6	38.3	36.7	-1.6
All	176,100	24.7	23.4	-1.4	35.0	33.7	-1.4
Addendum							
80–90	12,490	25.6	25.5	-0.1	36.5	36.4	-0.1
90–95	6,020	27.7	26.7	-1.1	35.5	34.5	-1.1
95–99	4,650	33.3	32.2	-1.1	38.8	37.7	-1.1
Top 1 percent	1,140	38.8	34.1	-4.6	42.7	38.1	-4.6
Top 0.1 percent	120	39.2	34.1	-5.1	43.0	37.9	-5.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1).

(a) Projections are for calendar year 2018. Effective marginal tax rates are weighted by the wages and salaries.

(b) Includes both filing and non-filing 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

(c) 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 2017 dollars): 20% $25,000; 40% $48,600; 60% $86,100; 80% $149,400; 90% $216,800; 95% $307,900; 99% $732,800; 99.9% $3,439,900.

TABLE 7

Dynamic Effects of Unified Framework on GDP

FY 2018–37

	Fiscal Year										
	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2037
	GDP ($ billions)										
Before macro feedback	19,926	20,661	21,378	22,168	23,037	23,948	24,899	25,889	26,917	27,985	41,419
After macro feedback											
TPC models	20,098	20,807	21,457	22,198	23,027	23,920	24,877	25,868	26,894	27,955	41,256
PWBM using TPC inputs	19,989	20,747	21,458	22,238	23,100	24,002	24,957	25,954	26,987	28,056	41,379
	Exhibit: Percentage change in GDP due to macro feedback (%)										
TPC models	0.9	0.7	0.4	0.1	0.0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.4
PWBM using TPC inputs	0.3	0.4	0.4	0.3	0.3	0.2	0.2	0.2	0.3	0.3	-0.1

Source: Congressional Budget Office (2016a, 2016b); TPC Keynesian and neoclassical models; Penn-Wharton Budget Model (PWBM) overlapping generations model.

TABLE 8

Domestic Investment and Net Capital Stock by Type, 2016

	Net Investment	Net Stock
All domestic (billions)	750.2	59,237.8
Percent of all domestic:		
Private domestic		
Nonresidential		
Equipment	24%	11%
Structures	15%	23%
Intellectual property products	13%	5%
Residential	32%	34%
Inventories	5%	4%
Government	11%	23%

Source: Bureau of Economic Analysis.

NOTES

[1] See Page, Benjamin R. and Kent Smetters. 2016. "Dynamic Analysis of Tax Plans: An Update." Washington DC: Urban Institute.

[2] See analysis by Moody's Analytics (https://www.economy.com/dismal/analysis/free/298300/US-Macro-Outlook-An-Unpalatable-Tax-Plan/) and Goldman Sachs (https://www.washingtonpost.com/news/wonk/wp/2017/10/09/goldman-sachs-predicts-dinky-boost-from-trumps-tax-cuts/?utm_term=.db63885618e9).

APPENDIX A. DETAILED ASSUMPTIONS USED FOR MODELING THE UNIFIED FRAMEWORK

Many aspects of the unified framework were not fully specified or left to be determined by the tax writing committees in Congress. TPC's preliminary analysis made the following assumptions:

Individual income tax structure: Our analysis uses the bracket thresholds proposed in the 2016 House Republican leadership's "A Better Way" tax plan:

TABLE A1

Tax Rate Structure

Taxable Income ($)				Current law marginal rate (%)	Proposed marginal rate (%)
Single Filers		Married Couples Filing Jointly			
Over	But not over	Over	But not over		
0	9,325	0	18,650	10	12
9,325	37,950	18,650	75,900	15	
37,950	91,900	75,900	153,100	25	25
91,900	191,650	153,100	233,350	28	
191,650	416,700	233,350	416,700	33	35
416,700	418,400	416,700	470,700	35	
418,400	and over	470,700	and over	39.6	

Notes: Income thresholds are based on current law brackets for tax year 2017.

Standard deduction: Our analysis sets the standard deduction amounts (for tax year 2018) at: $12,000 for single filers, $24,000 for married couples filing jointly, and $18,000 for head of household filers.

Child tax credit: Our analysis increases the child tax credit to $1,500 (up from $1,000 under current law), and increases the income level at which the credit begins to phase out for married couples filing jointly to $150,000 (double the level for single filers). Statements by President Trump have suggested the child tax credit might be increased above the $1,500 level included in the 2016 House Republican leadership "A Better Way" blueprint. The increase in the child tax credit is nonrefundable (while the first $1,000 per child remains partially refundable as under current law).

Credit for non-child dependents: Our analysis allows for a $500 non-refundable credit for all dependents age 17 or older, who would be ineligible for the child tax credit. The credit is not indexed for inflation and is assumed to phase out along with the child tax credit.

Index tax system with alternative measure of inflation: Our analysis would substitute the current measure of inflation with the chain-weighted consumer price index for all urban consumers (CCPI-U). Based on the Congressional Budget Office's estimates, we assume the CCPI-U will grow 0.25 percentage points slower per year over the forecast period than the CPI-U. That means that tax rate brackets, standard deduction amounts, and other indexed tax parameters will grow more slowly over time, subjecting more income to tax at higher tax rates and reducing the value of indexed tax credits.

Limit the individual tax rate on pass-through income to 25 percent: Our analysis limits the maximum individual income tax rate on pass-through income to 25 percent. Income that would qualify for that rate would include all net income from sole proprietorships, farms, rental real estate, partnerships and S corporations. The framework suggested the plan would adopt rules to prevent taxpayers from recharacterizing wage and other income as pass-through income but offered no specifics. Our analysis incorporates the effect that the tax rate differential between ordinary and pass-through income would have on reported incomes.

Allow full expensing of equipment for at least five years: Our analysis allows for full expensing of equipment and machinery (generally assets with a recovery period of 20 years or less) placed in service between September 28, 2017 and December 31, 2022.

Partially limit the ability of corporations to deduct net interest expense: The framework does not offer any specifics on this proposal, leaving it to the tax writing committees to determine. Therefore, we do not include it in our preliminary analysis, but will incorporate it when additional details are provided.

Repeal certain business tax expenditures: Our analysis eliminates the domestic production activities deduction (Section 199) and all business credits other than the R&E and LIHC credits. The framework does not offer specifics on any other business tax expenditures to be repealed, so we could not include these repeals in our preliminary analysis but will incorporate them when additional details are provided.

Enact a territorial tax system with a one-time deemed repatriation tax: Our estimates assume that the proposed rules for protecting the US tax base under the territorial system would be effective. The deemed repatriation tax is assumed to have the same rates as the 2014 proposal of former Ways and Means Chairman Dave Camp, and will be similarly payable over eight years.

TABLE B1

Alternative Ways of Presenting Change in Distribution of Tax Burdens

By expanded cash income percentile

Expanded cash income percentile[b]	Percent change in after-tax income[c]	Share of total federal tax change (%)	Average federal tax change[d]		Share of federal taxes	
			Dollars	Percent	Change (% points)	Under the proposal (%)
Panel A: 2018[a]						
Lowest quintile	0.5	1.1	-60	-10.4	0.0	0.9
Second quintile	0.9	4.1	-290	-9.3	0.0	3.8
Middle quintile	1.2	8.2	-660	-7.2	0.2	10.1
Fourth quintile	1.2	11.6	-1,110	-5.5	0.6	18.7
Top quintile	3.3	74.5	-8,470	-9.6	-0.7	66.5
All	2.1	100.0	-1,570	-8.6	0.0	100.0
Addendum						
80-90	0.8	5.1	-1,140	-3.1	0.9	15.1
90-95	0.7	3.3	-1,500	-2.6	0.7	11.4
95-99	2.3	12.8	-7,620	-6.9	0.3	16.4
Top 1 percent	8.5	53.3	-129,030	-17.6	-2.6	23.5
Top 0.1 percent	10.2	30.3	-722,510	-20.4	-1.7	11.1
Panel B: 2027[a]						
Lowest quintile	0.2	0.8	-50	-5.4	0.0	1.0
Second quintile	0.5	3.0	-230	-5.0	0.1	4.1
Middle quintile	0.5	4.9	-420	-3.4	0.4	10.2
Fourth quintile	0.4	4.3	-450	-1.7	0.9	17.3
Top quintile	3.0	86.6	-10,610	-8.5	-1.3	67.4
All	1.7	100.0	-1,690	-6.7	0.0	100.0
Addendum						
80-90	-0.4	-3.5	820	1.8	1.2	14.4
90-95	-0.3	-1.5	760	1.1	0.8	10.3
95-99	1.8	11.9	-7,640	-5.3	0.2	15.4
Top 1 percent	8.7	79.7	-207,060	-17.4	-3.5	27.2
Top 0.1 percent	9.7	39.6	-1,022,120	-19.0	-1.8	12.2

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1)

(a) Calendar year. Baseline is current law.

(b) Percentiles include both filing and non-filing 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. 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.

(c) 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.

(d) 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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