OPTIONS FOR REFORMING AMERICA'S TAX CODE 3.0

A Policymaker's Guide to Tax Reform Trade-Offs

TAX FOUNDATION

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The Tax Foundation is the world's leading nonpartisan tax policy 501(c)(3) nonprofit.
For over 80 years, our mission has remained the same: to improve lives through tax policies that lead to greater economic growth and opportunity.
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Introduction

The One Big Beautiful Bill Act (OBBBA) of 2025 made many expiring parts of the federal tax code permanent. But that does not mean tax reform is over.

As of this book's publication, members of Congress are considering additional tax changes in 2026. The Trump administration imposed several rounds of tariffs in 2025, many of which were struck down by the Supreme Court's *Learning Resources* decision, but it plans to impose additional tariffs in 2026. The OBBBA created several provisions that are scheduled to expire after 2028, which means another debate over extending tax cuts is already on the horizon.

However, the bigger issue for tax policy over the next several years will be how it balances with the other side of the budget equation: spending.

According to the Congressional Budget Office (CBO), the main Social Security trust fund will run out of reserves in 2032, forcing an automatic benefit cut of more than 20 percent without congressional action. Medicare spending is projected to almost double in nominal dollars within the decade, and the Hospital Insurance Trust Fund will likely reach insolvency in the 2030s. At the same time, rising geopolitical tensions have created a demand for higher levels of defense spending.

The CBO projects that, under current law, publicly held debt as a share of GDP will rise to a new record high of more than 107 percent within the next four years and continue rising to more than 175 percent of GDP by 2056. While revenues are projected to grow as a share of GDP, spending grows faster so that deficits rise to 9.1 percent of GDP by 2056.

All this spending must be paid for by American taxpayers through higher taxes either today or in the future, as the accumulating federal debt is eventually paid down. Higher debt burdens can reduce economic growth, as higher borrowing can raise interest rates and crowd out private investment. Taxes can also reduce economic growth, as higher marginal tax rates reduce incentives to work and invest.

Many of the solutions to America's fiscal problems should come from the spending side of the federal budget, but revenues will be part of the toolkit too. Whether policymakers want to raise or lower taxes, they must consider how policy changes will impact not just federal tax revenue, but the US economy at large.

In this book, we present 86 potential changes to the federal tax code. We consider how the changes would impact federal revenue, the long-term debt trajectory, the distribution of after-tax income, and the US economy. With the information in this book, policymakers can weigh the trade-offs of each option.

This book is arranged into chapters by major tax type:

1. **Individual Income Taxes**
2. **Payroll Taxes**
3. **Business Income Taxes**
4. **Excise Taxes and Customs Duties**
5. **Estate and Gift Taxes**

Themes of This Book

Tax Policy Is About Trade-Offs

A famous economist once said, "There are no solutions, there are only trade-offs." That lesson is especially true in tax policy.

The scales of justice may have two trays, but tax policy has three that lawmakers must balance—revenue, equity, and economic growth.

In other words, in tax policy, policymakers must reckon with an ever-present trade-off between (1) how much revenue a tax will raise, (2) progressivity, or who will bear the burden of a tax, and (3) how a tax change will impact economic incentives.

After modeling more than 80 changes to the tax code, we have found that it is impossible to balance all three equally. Lawmakers will have to decide which of the three is most important based on their values and priorities.

For example, if lawmakers want to make the tax code more progressive and raise revenues, our modeling shows that they will likely have to give up some economic output, because higher tax rates dampen economic activity (especially higher taxes on capital and labor).

And less growth means raising less revenue.

If lawmakers want to generate more economic output, our modeling shows that they will likely have to give up some progressivity, and maybe some tax revenue—although, all things being equal, a larger economy will tend to generate more tax revenue than the baseline, making up for some of the lost revenue.

Our modeling also illustrates that, contrary to popular belief, few, if any, tax cuts pay for themselves. And even the most powerful, pro-growth tax reforms would not allow us to grow our way out of our debt problem.

Some Tax Policy Changes Affect the Economy More than Others

People's willingness to work and deploy capital drives economic growth. Changes in the tax treatment of capital and labor change the cost of capital and the cost of labor and therefore affect the size of the capital stock and the supply of labor.

Taxes influence people's decisions about joining the workforce and how many hours to work. Taxes also influence decisions about how much to invest in new plant and equipment and where to locate new investment. How much the capital stock and the labor supply expand, or contract, largely determines the level of output and income in the economy.

Importantly, under standard economic theory, taxes affect behavior when they apply "on the margin"—when they affect a person's decision about his next hour of labor or her next dollar of investment.

For instance, changes in marginal tax rates affect people's incentives differently than lump-sum tax credits. Imagine a policy that cuts the bottom tax bracket from 10 percent to 5 percent. Currently, taxpayers who fall into the bottom bracket keep 90 cents of every additional dollar they earn working. Under this proposed policy, taxpayers in the bottom bracket would keep 95 cents of every additional dollar they earn working. Thus, this policy would give low-income taxpayers a stronger incentive to increase their supply of labor, because they would be able to keep more of their additional earnings.

On the other hand, imagine a policy that gave a fully refundable $2,000 tax credit to every individual. That policy would cut taxes significantly for every single taxpayer. However, it would not have any effect on taxpayers' supply of labor. Taxpayers in the 10 percent bracket would still only receive 90 cents of each additional dollar they earn working. Because this policy would not change taxpayers' marginal tax rates, it would not alter labor supply incentives.

	Full Expensing for Structures	Employer-Side and Employee-Side Payroll Tax Cut
Gross Domestic Product	1.50%	+0.5%
Gross National Product	1.40%	+0.2%
Capital Stock	2.80%	+0.6%
Pre-Tax Wage Rate	1.20%	+<0.05%
Full-Time Equivalent Jobs	400,000	555,000
10-Year Primary Deficit Change, Conventional	-$433.5B	$2,468.0B
10-Year Primary Deficit Change, Dynamic	-$474.9B	$2,004.3B
10-Year Total Deficit Change, Conventional	$536.8B	$2,971.8B
10-Year Total Deficit Change, Dynamic	$648.8B	$2,415.1B

Note: A negative number is a decrease in the deficit.

Empirical evidence demonstrates that capital is far more sensitive to changes in tax policy than labor is, primarily because capital is far more mobile than labor. Capital can move quickly from jurisdiction to jurisdiction in search of lower tax costs, but it is more difficult for workers to move their families from place to place to lower their tax bills.

Accordingly, changes in the taxation of capital have a larger effect on the economy than changes in the taxation of labor. To illustrate, compare the following two options: introducing full expensing for all structures (Option 54) and reducing the employer-side and employee-side payroll tax by one percentage point each (Option 42). Expensing provides a tax cut for new capital investment, while lower payroll taxes provide a tax cut for labor income.

Full expensing for structures allows businesses to immediately deduct the cost of long-lived assets like factories, warehouses, offices, and apartment buildings, which increases the return to capital. Reducing the payroll tax by 1 percentage point increases the return to labor, as workers fully bear both sides of the payroll tax.

Compared to the payroll tax cut, expensing for structures would have a substantially larger positive effect on output (GDP, the final value of goods and services produced in America) as well as national income (GNP, the final value of goods and services owned by Americans), and yet would cost substantially less in terms of reduced federal revenue.

Full expensing for structures offers more "bang for the buck" than reducing the payroll tax because expensing reduces taxes on capital, while the payroll tax falls squarely on labor.

The Tax Base Is Just as Important as the Tax Rate

Changing a tax rate might seem like the easiest way to provide tax relief or increase revenue, but the tax rate only matters because of the tax base to which it applies.

Currently, numerous deductions, exclusions, and exemptions narrow the size of the US tax base and reduce the amount of economic activity subject to tax. A broader tax base could result in additional tax revenue without rate changes.

Broader tax bases and lower tax rates tend to be more economically efficient than systems with narrow tax bases and high tax rates. While the rule holds in general, not all measures to broaden the tax base are sound tax policy. For instance, broadening the business tax base by lengthening depreciation schedules would cause significant economic harm.

Changing a tax rate is simple, but defining what should be subject to a tax is a complex and nuanced task that hinges on one's view of an ideal tax base. Two primary approaches compete for this ideal: an income tax base and a consumption tax base.

Under an income tax base, individuals pay taxes on their consumption plus their change in wealth. Under a consumption tax base, individuals pay taxes only on their consumption.

To illustrate the difference between an income-based tax and a consumption-based tax, imagine a small business owner who earns $250,000 in net income, spends $200,000 of it on an investment, and consumes the remaining $50,000.

- Under an income-based tax, the business owner would pay taxes on both the $50,000 of consumption and the $200,000 increase in wealth.
- Under a consumption-based tax, the business owner would only pay taxes on the $50,000 of consumption and would not pay taxes on the investment until it yields a profit and is consumed in the future.

A consumption-based tax avoids double taxation of saving and investment, which otherwise imposes a higher effective tax rate on income saved and invested than income consumed immediately. For instance, in the example above, the income-based tax would apply to both the principal of the investment (the $200,000 spent today) and the profits of the investment (the profit that the investment would yield in the future). As a result, this double tax would make the business owner less likely to invest.

Income-based taxes often apply several layers of tax on the same investment. For instance, an individual's investment in a US corporation may be subject to four layers of taxation: once when the income is initially earned, through the individual income tax; a second time when the corporation earns a profit, through the corporate income tax; a third time when the profit is distributed to shareholders, through the individual income tax on dividends; and a fourth time when the individual dies, through the estate tax.

Supporters of income-based taxes argue they are more progressive than consumption-based taxes. Because high-income taxpayers are more likely to save and invest than low-income taxpayers, placing several layers of taxes (or higher effective tax rates) on investment increases the tax burden on the wealthy. However, it is also possible to make consumption-based taxes progressive without imposing higher marginal tax rates on investment.

Under current law, the US tax system is a hybrid between a pure income-based tax and a pure consumption-based tax. For instance, capital gains are included in the tax base (income feature) but taxed at a lower rate (consumption feature). Another example: businesses are unable to deduct the full cost of their capital investments immediately (income feature), but the tax code allows for accelerated depreciation schedules and full expensing of some assets (consumption feature).

Some of the options in this book would move the US tax system further toward an income tax base, while others would move it further toward a consumption tax base. Lawmakers should consider which direction they wish to move toward and the trade-offs involved with each approach.

Economic Effects Matter Across Time Horizons

Tax cuts seldom pay for themselves, particularly in the context of the current US tax system, where marginal tax rates are much lower than they once were.

Economic growth can substantially offset a portion of the lost revenue from a tax cut (or can cost a portion of the additional revenue from a tax increase), but it depends on the type of tax change and timeline being considered.

Tax changes that have a more powerful effect on economic growth will produce relatively more "dynamic feedback" than tax changes with smaller economic effects. Dynamic feedback does not necessarily mean that the tax affected by the policy change raises additional revenue itself. For instance, a reduction in the corporate tax rate would reduce corporate tax revenue even after accounting for growth. Further, on a dynamic basis, we would generally expect corporate tax revenue to fall by a greater extent (if investment increases, corporate deductions will be larger). Offsetting effects would instead stem from individual income and payroll tax revenues increasing as demand for labor increases.

Dynamic effects can take time to materialize, depending on whether they affect labor supply or capital investment. Labor can respond relatively quickly to tax changes, and a change in the labor supply today changes output today. Capital can take longer to respond, as investments take time to permit, plan, place in service, and begin to produce output. Investments also continue to produce output for many years after they are placed in service.

This "adjustment path" means the ultimate economic effects of changes in the tax treatment of capital do not materialize immediately. In early years, the dynamic feedback of tax changes to capital may be smaller, but they grow over time. This trend can sometimes be seen in the 10-year window. But it is even more important beyond the 10-year window and is reflected in our measure of the debt-to-GDP ratio in 2056.

A particularly pro-growth tax cut policy might have a large deficit-increasing impact in the short term, but over the course of decades, it may mostly offset its fiscal impact with economic growth and therefore not materially harm the US's long-term fiscal picture. Conversely, an economically harmful policy might reduce deficits in the short term, but it could reduce output enough to not materially improve the US's long-term fiscal picture.

How to Use This Book

The figures reported in this book were estimated using the Tax Foundation's General Equilibrium Model, with the goal of providing a comprehensive picture of how different tax changes would affect the US economy, federal tax revenue, the long-term debt-to-GDP trajectory, and the distribution of after-tax income.

Each option described in this book is accompanied by several statistics that summarize the projected long-run economic effects, 10-year revenue effects (calendar years), and distributional effects of the tax change relative to a current law baseline.

Long-Run Change in Gross Domestic Product (GDP)

This statistic conveys how much larger or smaller the US economy would be in the long run if a particular tax change were adopted. It measures the final value of goods and services produced within the United States (by Americans and foreigners) within a given time frame.

For instance, if an option results in a 1 percent increase in long-run GDP, this means that adopting the option would make the US economy 1 percent larger than otherwise. This statistic does not convey any information about how annual GDP growth would change along the adjustment path to the new level because of an option.

Long-Run Change in Gross National Product (GNP)

This statistic conveys how much larger or smaller American incomes would be because of a particular tax change. It is related to GDP but differs because it measures the income that Americans earn from the production of goods and services within the United States and abroad within a given time frame.

Some tax changes can create a wedge between GDP (American output) and GNP (American incomes). Taxes levied on domestic saving, such as capital gains taxes, would reduce the return to saving and the ownership of American investment by domestic residents. Additionally, higher deficits lead to higher government borrowing, which, in turn, could crowd out domestic savers. Because the US economy is open to international investment, foreign investors who are not subject to the tax may provide additional funds to finance domestic investments. In general, this limits the impact that taxes on saving have on GDP because foreign investors continue to fund investments, but the returns to those investments do not benefit Americans, resulting in lower GNP.

Long-Run Change in Capital Stock

This statistic conveys how much larger or smaller the US capital stock would be in the long run if a particular tax change were adopted. The capital stock is a measure of the level of fixed assets in the economy, including government-owned and privately owned. The private stock consists of four main asset types: equipment and software, nonresidential structures, residential structures, and intellectual property.

An increase (or decrease) in the after-tax rate of return to capital will drive an increase (or decrease) in the capital stock. An increase (or decrease) in the level of the capital stock permanently changes output, which increases (or decreases) the incomes for both owners of capital and workers.

Long-Run Change in Wages

This statistic conveys how much larger or smaller the level of real average hourly earnings for employees in all sectors would be in the long run if a particular tax change were adopted.

Long-Run Change in Full-Time Equivalent Jobs

This statistic conveys how much larger or smaller the labor supply would be if a particular tax change were adopted. The labor supply response is measured in hours worked, which is then converted into a measure of full-time equivalent jobs. For example, in 2024, the United States had roughly 161 million employees, but some of them worked part-time jobs. Converted to full-time equivalent employees, which expresses how many employees there would be if Americans worked the same total number of hours but only in full-time jobs, the United States had roughly 145 million full-time equivalent employees in 2024. Many of the options in this book would increase or decrease the capacity of the economy to employ labor, leading to additional or fewer full-time equivalent jobs.

10-Year Primary Deficit Change (Conventional)

This statistic conveys how much a tax policy change would increase or decrease the primary deficit (the difference between revenues and noninterest spending) if it had no macroeconomic effect (in other words, holding the size of the economy constant). It is measured in calendar years. In some cases, the change in revenue over the first 10 years may differ from the long-run change in revenue. This could be due to tax changes that "frontload" or "backload" the revenue impact or due to changes with other timing-related impacts, such as phaseouts or expirations that are scheduled to occur under current law. Except in the case of refundable tax credits, which affect government outlays, government spending is assumed to be unchanged. For some options, such as a value-added tax, this does not capture all the net budgetary effects.

10-Year Primary Deficit Change (Dynamic)

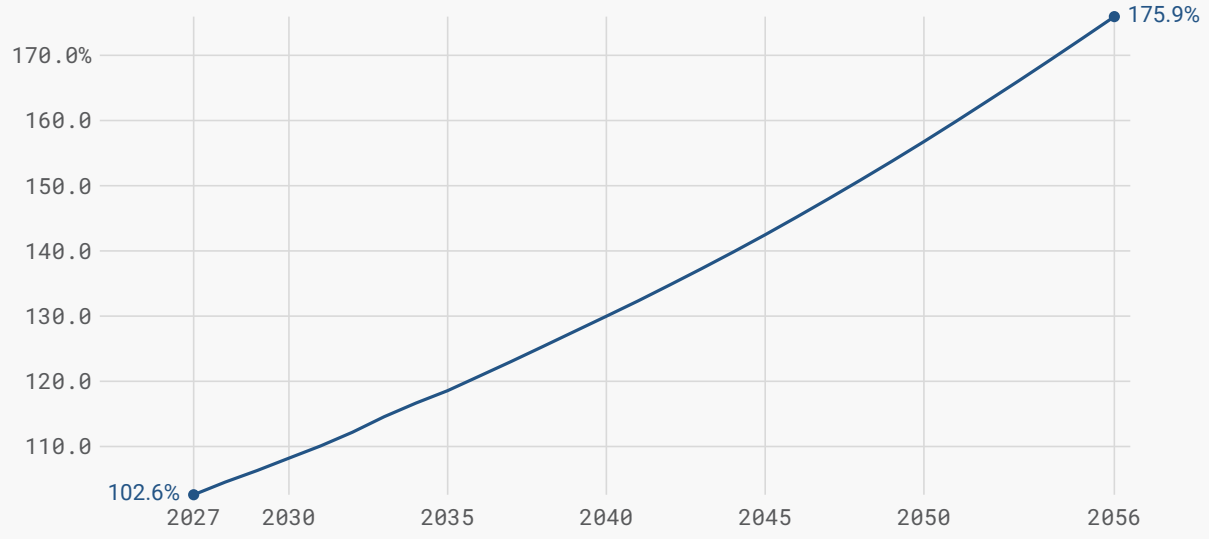
This statistic expresses how much a tax policy change would increase or decrease the primary deficit after considering its economic effects in calendar years. For instance, if cutting the income tax would lead to an increase in hours worked, in turn increasing payroll tax revenue, then it would make up for some of the revenue lost from the income tax cut. Dynamic revenue scores offer a more complete picture of how much federal revenue would change because of a tax change. Note that the long-run revenue change after all adjustments have occurred may be considerably different from the revenue change over the 10-year budget window because economic effects build over time. Except in the case of refundable tax credits, which affect government outlays, government spending is assumed to be unchanged. For some options, such as a value-added tax, this does not capture all the net budgetary effects.

10-Year Total Deficit Change (Conventional)

This statistic expresses the total change in deficits, including changes in interest costs, within the 10-year budget window in calendar years, before considering macroeconomic

Debt-to-GDP Ratio Projected to Reach 175.9% in 2056

Baseline Debt-to-GDP Ratio, Calendar Years 2027 through 2056



Source: Congressional Budget Office "Long-Term Budget Projections" converted to calendar year by Tax Foundation.

effects. Holding government spending constant, a change in tax revenue necessitates a change in government borrowing: if revenue goes down, then the government must borrow more to fill the gap, and if revenue goes up, then the government will borrow less. Accordingly, to evaluate the total impact of a tax change on the deficit, one must consider how it will change future interest payments, not just revenues.

10-Year Total Deficit Change (Dynamic)

This statistic combines the two points above, factoring in both how a change in the size of the economy may change revenue collections and how a change in revenue may change interest payments. As a result, it provides a more complete picture of how a policy would shape the overall fiscal picture within the 10-year budget window in calendar years.

Baseline, Conventional, and Dynamic Debt-to-GDP Ratios

The debt-to-GDP ratio compares the size of publicly held federal debt to the economy's annual output. It is a measure of the federal debt burden. We convert fiscal year projections from the CBO to calendar year projections.

Accordingly, the converted projections show that in 2036, the end of the current 10-year budget window, the debt-to-GDP ratio will reach 120.8 percent, and by 2056, it will reach 175.9 percent.

For each option, we estimate how the projected debt-to-GDP ratio changes across calendar years 2027 through 2056 on a conventional basis with interest cost changes (excluding the macroeconomic impact of the tax policy change) and a dynamic basis with interest cost changes (including the macroeconomic impact).

The estimates illustrate how both the revenue effects and the economic effects stemming from different tax policy changes must be considered to evaluate how an option changes the US fiscal position in the near term and the long term.

Change in After-Tax Income

Most tax changes deliver different costs and benefits to different groups of taxpayers.

Conventional distributional estimates show how after-tax income changes across the income scale, holding the size of the economy constant. To show how much an option would raise or lower taxes on each group, we calculate the tax change as a percentage of the group's after-tax income. We show the conventional distribution

in the first year and last year of the 10-year budget window to illustrate how the provision would impact taxpayer incomes over the budget window.

In addition to costing or benefiting taxpayers through higher or lower taxes, the options in this book would also cost and benefit taxpayers through economic effects. Dynamic distributional estimates show how the after-tax incomes of each group of taxpayers would change due to both direct tax changes and indirect economic effects.

To produce distributional tables, Tax Foundation ranks each tax unit by market income. Market income includes adjusted gross income (AGI) plus tax-exempt interest, non-taxable Social Security income, the employer share of payroll taxes, imputed corporate tax liability, employer-sponsored health insurance and other fringe benefits, and taxpayers' imputed contributions to defined-contribution pension plans. Market income levels are adjusted for the number of exemptions reported on each return to make tax units more comparable. After-tax income is market income less: individual income tax, corporate income tax, payroll taxes, estate and gift tax, customs duties, and excise taxes.

Caveats and Warnings

While the results capture important behavioral effects, including incentive effects of changes in marginal tax rates as well as some avoidance effects, the model does not capture all possible effects. For instance, the results do not capture the benefits of reduced compliance costs and other efficiencies of certain simplifying reforms, such as the repeal of estate and gift taxes, alternative minimum taxes for individuals and corporations, and other complex features of the code. Nor does it fully capture the tax planning and avoidance effects that may arise from novel policies, such as mark-to-market taxation. The model also assumes an open economy, such that taxes on US savers generally do not impact US economic output, a simplifying assumption that does not capture certain edge cases that may more closely resemble a closed economy.

Readers should not attempt to combine the revenue, economic, or distributional figures from multiple options. For instance, if Option A would raise $100 billion and Option B would raise $200 billion, it is not necessarily the case that implementing both Option A and Option B would raise $300 billion. The US tax system contains many components that interact with each other in complex ways.

If you are interested in assembling a tax plan of your own, please feel free to contact the Tax Foundation for assistance and model results at (202) 464-6200. Priority will be given to members of Congress and their staff.

Individual Income Taxes

The individual income tax is the largest source of federal revenue, accounting for approximately half of all federal tax collections. Because of its large base, even small changes to the individual income tax can lead to large swings in federal revenue and significant economic consequences.

The individual income tax is designed to impose a larger burden on taxpayers with higher incomes. In tax year 2023, taxpayers in the top 1 percent of the income distribution earned 20.6 percent of adjusted gross income but paid 38.4 percent of all federal individual income taxes. Meanwhile, taxpayers in the bottom 50 percent of the income distribution earned 12.3 percent of adjusted gross income and paid 3.3 percent of all federal individual income tax. Taxpayers making less than $25,000 typically owe no income tax at all; many end up receiving additional transfer payments through the income tax code, using refundable credits such as the earned income tax credit.

Most of the income that is subject to the individual income tax comes from wages and salaries. The individual income tax also applies to investment income, certain retirement income, and business income of individuals who participate in pass-through businesses. Because of this, the individual income tax impacts individuals' incentives to work, save, and invest. The components of the individual income tax that apply to investment and saving are generally more economically harmful than those that apply to labor income.

While the individual income tax is large, it suffers from an overly narrow base. The individual tax code contains more than 100 credits, deductions, exclusions, and other provisions that reduce tax payments.

These provisions add complexity to the tax filing process and sometimes produce perverse economic effects, often by favoring certain types of compensation or consumption over others. Not all deductions and exclusions are inappropriate; some are needed to measure income correctly and define the tax base, such as those that prevent the double taxation of saving.

This chapter contains options that change different aspects of the individual income tax code, ranging from rates and credits to deductions and the alternative minimum tax.

Individual Income Taxes: Rates

The individual income tax on ordinary income is currently levied at seven different rates, ranging from 10 percent to 37 percent. A critical feature of tax brackets is that each rate only applies to the taxable income within each bracket, not to income below it.

For example, a single taxpayer with $40,000 in taxable income would face a 10 percent tax rate on their first $12,400 and a 12 percent tax rate on their taxable income that falls between $12,400 and $50,400—in this case, their next $27,600. Earning income above a certain bracket threshold only subjects the income above that bracket threshold to the higher rate, with income below the threshold still facing the lower rates.

Ordinary income includes most kinds of personal income that taxpayers earn. Because ordinary income is such a large part of the tax base, changes to the rates on ordinary income tend to have large effects on the amount of revenue collected.

Because the current system of brackets is steeply graduated, a taxpayer's average rate is often much lower than his or her marginal rate. For example, a taxpayer may be in the 24 percent bracket for each additional dollar earned but still find that most of their income is taxed under the 12 or 22 percent brackets. Such a system can create high marginal tax rates, which disincentivize work, saving, and investment, while still levying low average tax rates, resulting in relatively less revenue.

This subchapter considers changes to the individual tax bracket rate structure. Some changes involve tweaking the rates within the seven existing brackets; others involve shrinking the number of brackets or even consolidating all brackets into a flat tax with only one rate.

1. Lower the Top Marginal Individual Income Tax Rate to 35 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.2%	**+0.1%**	**+0.3%**	**+0.1%**	**+148K**

The current top marginal income tax rate is 37 percent. In 2026, it applies to income above $626,351 for single filers and $751,601 for joint filers. This option permanently reduces the top rate to 35 percent, lowering marginal tax rates on labor income, pass-through business income, and other types of income earned by high-income taxpayers. Lowering marginal tax rates on pass-through business income decreases the cost of capital, increasing incentives to invest.

On a conventional basis, this option would increase the primary deficit by $625.3 billion over the budget window. Long-run GDP would rise by 0.2 percent, and long-run GNP by 0.1 percent. On a dynamic basis, the primary deficit would increase by $452.2 billion from 2027 through 2036, $173.1 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 179.1 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.3 percent. The top quintile of taxpayers would experience a 0.4 percent increase, whereas the bottom quintile would experience no change. On a long-run dynamic basis, taxpayers would see a 0.5 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$625.3B	+$452.2B
Total Deficit Change	+$753.8B	+$549.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	122.4%	121.7%
CY 2056	175.9%	181.2%	179.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	+0.3%	0.0%	+<0.05%	+0.1%	+1.0%	+1.4%	**+0.3%**
Conventional, 2036	0.0%	0.0%	0.0%	+<0.05%	+0.4%	0.0%	+<0.05%	+0.1%	+1.1%	+1.6%	**+0.3%**
Dynamic, Long-Run	+0.2%	+0.2%	+0.2%	+0.2%	+0.5%	+0.2%	+0.2%	+0.3%	+1.2%	+1.8%	**+0.5%**

2. Lower Individual Income Tax Rates by 10 Percent Across the Board

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+1.3%	**+0.9%**	**+1.6%**	**+0.2%**	**+1.3M**

This option reduces all seven marginal income tax rates by 10 percent. The top marginal income tax rate falls from 37 percent to 33.3 percent, and the bottom rate from 10 percent to 9 percent. This would lower marginal tax rates on labor income across the board, increasing incentives to work. Pass-through business income would also face lower marginal tax rates, reducing the cost of capital and expanding investment incentives.

On a conventional basis, this option would increase the primary deficit by $3,610.2 billion over the budget window. Long-run GDP would rise by 1.3 percent and long-run GNP by 0.9 percent. On a dynamic basis, the primary deficit would increase by $2,489.5 billion from 2027 through 2036, $1,120.7 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 194.4 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 1.9 percent. The top quintile of taxpayers would experience a 2.3 percent increase, whereas the bottom quintile would experience a less than 0.05 percent increase. On a long-run dynamic basis, taxpayers would see a 2.9 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$3,610.2B	+$2,489.5B
Total Deficit Change	+$4,342.2B	+$3,004.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	130.0%	125.6%
CY 2056	175.9%	206.6%	194.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+<0.05%	+0.2%	+0.6%	+1.0%	+2.1%	+1.4%	+1.7%	+2.2%	+3.2%	+2.8%	**+1.7%**
Conventional, 2036	+<0.05%	+0.3%	+0.8%	+1.2%	+2.3%	+1.6%	+1.9%	+2.4%	+3.4%	+3.1%	**+1.9%**
Dynamic, Long-Run	+1.1%	+1.3%	+1.8%	+2.2%	+3.4%	+2.6%	+3.0%	+3.6%	+4.5%	+4.3%	**+2.9%**

3. Raise Individual Income Tax Rates by 10 Percent Across the Board

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-1.3%	**-1.0%**	**-1.6%**	**-0.3%**	**-1.4M**

This option increases all seven marginal income tax rates by 10 percent. The top marginal income tax rate rises from 37 percent to 40.7 percent, and the bottom rate from 10 percent to 11 percent. Marginal income tax rates on labor would rise, reducing incentives to work. Marginal income tax rates on pass-through businesses would also rise, increasing the cost of capital and reducing incentives to invest.

On a conventional basis, this option would decrease the primary deficit by $3,158.1 billion over the budget window. Long-run GDP would fall by 1.3 percent, and long-run GNP by 1.0 percent. On a dynamic basis, the primary deficit would decrease by $1,888.2 billion from 2027 through 2036, $1,269.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 162.5 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 1.6 percent. The top quintile of taxpayers would experience a 2.1 percent decrease, whereas the bottom quintile would experience a slight decrease. On a long-run dynamic basis, taxpayers would see a 2.6 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$3,158.1B	-$1,888.2B
Total Deficit Change	-$3,796.9B	-$2,281.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	112.7%	117.4%
CY 2056	175.9%	149.0%	162.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-0.2%	-0.7%	-1.0%	-1.9%	-1.4%	-1.6%	-2.1%	-2.6%	-1.9%	**-1.4%**
Conventional, 2036	-<0.05%	-0.3%	-0.8%	-1.2%	-2.1%	-1.6%	-1.9%	-2.4%	-2.8%	-2.2%	**-1.6%**
Dynamic, Long-Run	-1.2%	-1.3%	-1.8%	-2.2%	-3.1%	-2.6%	-2.9%	-3.4%	-3.9%	-3.4%	**-2.6%**

4. Raise the Top Marginal Individual Income Tax Rate to 50 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-1.4%	**-1.2%**	**-2.0%**	**-0.6%**	**-1.0M**

The current top marginal income tax rate is 37 percent. In 2026, it applies to income above $626,351 for single filers and $751,601 for joint filers. This option permanently raises the top rate to 50 percent. Raising the top marginal tax rate would increase the tax burden on labor income and on pass-through business income, reducing incentives to work and invest.

On a conventional basis, this option would decrease the primary deficit by $1,603.8 billion over the budget window. Long-run GDP would fall by 1.4 percent, and long-run GNP would fall by 1.2 percent. On a dynamic basis, the primary deficit would decrease by $411.2 billion from 2027 through 2036, $1,192.6 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be unchanged from baseline, reaching 175.9 percent by 2056.

This option would primarily affect high-income taxpayers, reducing the after-tax income of the top quintile by 1.4 percent and of the top 0.1 percent by 6.4 percent in 2036. On a long-run dynamic basis, taxpayers would see a 1.9 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,603.8B	-$411.2B
Total Deficit Change	-$1,931.8B	-$521.2B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	116.7%	121.3%
CY 2056	175.9%	162.3%	175.9%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-1.3%	0.0%	0.0%	-0.2%	-3.8%	-5.5%	**-0.8%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-1.4%	0.0%	0.0%	-0.2%	-4.3%	-6.4%	**-0.8%**
Dynamic, Long-Run	-1.2%	-1.0%	-1.1%	-1.0%	-2.5%	-1.1%	-1.1%	-1.4%	-5.3%	-7.5%	**-1.9%**

5. Consolidate Individual Income Tax Brackets into Three Rates: 10, 25, and 35 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.1%	**+<0.05%**	**+0.3%**	**+0.1%**	**+29K**

This option creates a three-bracket income tax system: income currently taxed at 10 percent and 12 percent is taxed at 10 percent; income currently taxed at 22 percent, 24 percent, and 32 percent is taxed at 25 percent; and income taxed at 35 percent and 37 percent is taxed at 35 percent. Some individual taxpayers would experience increases in the tax rate they face at the margin, while others would experience decreases. Overall, marginal tax rates on labor and capital investment would be lower.

On a conventional basis, this option would increase the primary deficit by $738.0 billion over the budget window. Long-run GDP would rise by 0.1 percent, and long-run GNP would rise by less than 0.05 percent. On a dynamic basis, the primary deficit would increase by $686.5 billion from 2027 through 2036, $51.5 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 180.8 percent by 2056.

On average, in 2036, taxpayers would see a 0.3 percent increase in their after-tax incomes. The top quintile of taxpayers would experience a 0.2 percent increase, whereas the bottom quintile would experience a less than 0.05 percent increase. Taxpayers between the 80th and 95th percentiles would experience a decrease in after-tax income. On a long-run dynamic basis, taxpayers would see a 0.5 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$738.0B	+$686.5B
Total Deficit Change	+$894.0B	+$838.8B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	122.7%	122.4%
CY 2056	175.9%	181.8%	180.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+<0.05%	+0.1%	+0.6%	+0.5%	+0.2%	-0.3%	-0.6%	+0.1%	+1.2%	+1.5%	**+0.4%**
Conventional, 2036	+<0.05%	+0.1%	+0.7%	+0.3%	+0.2%	-0.5%	-0.7%	+0.3%	+1.3%	+1.6%	**+0.3%**
Dynamic, Long-Run	+0.1%	+0.2%	+0.8%	+0.4%	+0.3%	-0.4%	-0.5%	+0.4%	+1.4%	+1.8%	**+0.5%**

6. Move to a Flat 30 Percent Individual Income Tax Rate

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-2.7%	**-1.0%**	**-2.9%**	**0.0%**	**-3.5M**

This option applies a flat, 30 percent rate to taxable income. Lowering the top income tax rate on its own would cause many filers to be subject to the alternative minimum tax (AMT), muting the intended impact of the change, so this option also eliminates the AMT alongside the rate change. It leaves all other aspects of the individual income tax the same. Moving to a flat 30 percent tax rate on taxable income would increase marginal tax rates faced by most taxpayers, including lower- and middle-income taxpayers, reducing incentives to work and invest. The reduction in hours worked and in investment would shrink long-run output.

On a conventional basis, this option would decrease the primary deficit by $17,032.9 billion over the budget window. Long-run GDP would fall by 2.7 percent, while long-run GNP would fall by 1.0 percent. The gap between the effect on output and input is a result of the large change in the US budget deficit; a smaller budget deficit reduces interest payments to foreigners, which offsets some of the decline in GNP. On a dynamic basis, the primary deficit would decrease by $13,709.3 billion from 2027 through 2036, $3,323.6 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 64.3 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 8.5 percent. The top quintile of taxpayers would experience a 6.4 percent decrease, whereas the bottom quintile would experience a 0.6 percent decrease. But within the top quintile, the top 1 percent of taxpayers would experience an increase in after-tax income of at least 1.4 percent. On a long-run dynamic basis, taxpayers would see a 10.5 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$17,032.9B	-$13,709.3B
Total Deficit Change	-$20,528.4B	-$16,505.2B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	77.3%	88.2%
CY 2056	175.9%	34.1%	64.3%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.4%	-4.6%	-10.9%	-12.9%	-6.3%	-11.9%	-10.4%	-6.7%	+1.2%	+4.4%	**-8.0%**
Conventional, 2036	-0.6%	-6.4%	-12.5%	-13.4%	-6.4%	-12.1%	-10.5%	-6.3%	+1.4%	+4.9%	**-8.5%**
Dynamic, Long-Run	-2.9%	-7.9%	-14.2%	-15.2%	-8.7%	-14.0%	-12.5%	-8.6%	-1.1%	+2.2%	**-10.5%**

Individual Income Taxes: Capital Gains and Dividends

Under the current US tax code, long-term capital gains and qualified dividends face a separate bracket and rate schedule from ordinary income. Long-term capital gains are profits from selling an asset held for more than one year. Qualified dividends are payments made by US corporations and some foreign corporations to shareholders who have owned stock for a certain length of time.

These two forms of income are taxed under a bracket schedule with three rates: 0, 15, and 20 percent. Additionally, for taxpayers above a certain income threshold, long-term capital gains and dividend income can face a 3.8 percent surtax called the net investment income tax that brings the top federal rate up to a combined 23.8 percent.

Capital gains and dividends face lower rates for two primary reasons. First, dividends and capital gains that taxpayers receive may have already been subject to the corporate income tax. The lower rate on capital gains and dividend income helps mitigate the double tax on US corporate income. Second, individuals typically pay ordinary income taxes on the principal of the investment before investing. As a result, investment returns are already implicitly subject to one layer of individual taxation.

Capital gains taxes can have a substantial impact on realization behavior. Capital gains are only taxed when realized, meaning taxpayers get to choose when they pay their capital gains taxes. This ability to defer tax makes capital gains income significantly more responsive to tax changes than other types of income.

Taxes on capital gains and dividends primarily matter for incentives to save. Because the US is an open economy, and businesses can receive financing from both foreign and domestic savers, taxes on domestic saving have a relatively limited impact on business investment. If taxes discourage domestic saving, businesses can turn to foreigners for financing. Domestic production can continue, but the returns to that production may instead flow to foreigners, meaning taxes on savers can reduce domestic income even if they have a relatively limited effect on domestic production.

This subchapter considers several changes to the tax treatment of various forms of capital income. Most options are incremental changes to the existing framework: tweaking the rates for capital gains and dividends as well as the net investment income tax. However, we also include complete redesigns of capital gains taxation.

7. Lower the Top Tax Rate on Capital Gains and Dividends to 15 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**+<0.05%**	**0.0%**	**0.0%**	**0**

Long-term capital gains and qualified dividends face different brackets and rates than ordinary income, in part to offset some of the double taxation of saving and investment that occurs under the income tax system.

This option lowers the top rate on capital gains and qualified dividends from 20 percent to 15 percent. A lower top capital gains tax rate would reduce marginal tax rates on saving, increasing after-tax returns and boosting the incentive to save. Domestic saving would rise, and more of the returns to American investment would flow to Americans. At the same time, the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners. These two offsetting effects result in a slight rise in GNP.

On a conventional basis, this option would increase the primary deficit by $170.7 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would rise by less than 0.05 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.5 percent by 2056.

The benefits of a lower top capital gains tax rate are concentrated among high-income taxpayers. The top quintile of taxpayers would experience a 0.2 percent increase in 2036, while other groups would experience no change.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$170.7B	+$170.7B
Total Deficit Change	+$200.0B	+$200.0B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.2%	121.2%
CY 2056	175.9%	177.5%	177.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	+<0.05%	0.0%	0.0%	0.0%	+0.1%	+0.1%	**+<0.05%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	+0.2%	0.0%	0.0%	+<0.05%	+0.3%	+0.9%	**+0.1%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	+0.2%	0.0%	0.0%	+<0.05%	+0.3%	+0.9%	**+0.1%**

8. Raise the Top Tax Rate on Capital Gains and Dividends to 30 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-<0.05%**	**0.0%**	**0.0%**	**0**

Long-term capital gains and qualified dividends face different brackets and rates than ordinary income, in part to offset some of the double taxation of saving and investment that occurs under the income tax system.

This option raises the top rate on capital gains and qualified dividends from 20 percent to 30 percent. A higher top tax rate on capital gains would increase marginal tax rates on saving, reducing after-tax returns to saving and decreasing the incentive to save. Domestic saving would fall, and foreign investment into the US would increase, preventing a decline in output but causing more of the returns to American investment to flow to foreigners. The smaller budget deficit, however, would reduce federal government borrowing and interest payments to foreigners. These two effects largely offset, resulting in a slight decline in GNP.

A higher capital gains tax rate would also discourage capital gains realizations, leading to little revenue generated in the first few years of the budget window. On a conventional basis, this option would decrease the primary deficit by $362.5 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would decline by less than 0.05 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 172.8 percent by 2056.

Raising the top tax rate on capital gains affects high-income taxpayers. In 2036, the top quintile of taxpayers would experience a 0.3 percent decrease in after-tax income.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$362.5B	-$362.5B
Total Deficit Change	-$432.1B	-$432.0B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.9%	119.9%
CY 2056	175.9%	172.8%	172.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.1%	0.0%	0.0%	-<0.05%	-1.2%	+0.4%	**-0.1%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-0.3%	0.0%	0.0%	-0.1%	-0.9%	-1.2%	**-0.2%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	-0.3%	0.0%	0.0%	-0.1%	-0.9%	-1.2%	**-0.2%**

9. Tax Capital Gains and Dividends at Ordinary Income Tax Rates

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.1%	**-0.3%**	**-0.1%**	**-<0.05%**	**-64K**

Long-term capital gains and qualified dividends face different brackets and rates than ordinary income, in part to offset some of the double taxation of saving and investment that occurs under the income tax system.

This option taxes capital gains and dividends at ordinary income tax rates for all taxpayers. Taxing capital gains at ordinary income rates would interact with several parts of the current tax code, including the alternative minimum tax, in ways that increase marginal tax rates on labor and pass-through business income, discouraging work and investment. It would also increase marginal tax rates on saving, reducing the incentive to save. A higher capital gains tax rate would discourage capital gains realizations, leading to revenue losses in the first few years of the budget window, but revenue gains in later years. Although a smaller budget deficit would partially offset the decline in domestic saving, net GNP would fall because of the decline in economic output and lower domestic saving.

Over the decade, on a conventional basis, it would decrease the primary deficit by $137.0 billion over the budget window. Long-run GDP would fall by 0.1 percent and long-run GNP by 0.3 percent. On a dynamic basis, the primary deficit would decrease by $75.4 billion from 2027 through 2036, $61.6 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.8 percent by 2056.

Initially, reflecting the swing in realizations and initial revenue loss, some higher-income taxpayers would see increases in after-tax income, reflecting the change in capital gains realizations. Over time, however, taxpayers would see decreases in their after-tax incomes of 0.1 percent on average by 2036. The top quintile of taxpayers would experience a 0.1 percent decrease, whereas the bottom quintile would experience a less than 0.05 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.2 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$137.0B	-$75.4B
Total Deficit Change	-$140.7B	-$67.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.5%	120.7%
CY 2056	175.9%	174.1%	174.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-0.1%	-0.2%	-0.1%	+0.5%	0.0%	+0.2%	+0.2%	+0.9%	+2.6%	**+0.2%**
Conventional, 2036	-<0.05%	-0.2%	-0.2%	-0.1%	-0.1%	-0.1%	-<0.05%	-0.1%	-0.1%	-0.2%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.2%	-0.3%	-0.2%	-0.1%	-0.1%	-0.1%	-0.2%	-0.2%	-0.2%	**-0.2%**

10. Tax Carried Interest at Ordinary Income Tax Rates

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	**-<0.05%**	**-<0.05%**	**-<0.05%**	**-9K**

Carried interest is a form of compensation for investment managers at private equity firms and hedge funds. Many investment managers are often compensated according to a "two and twenty" arrangement: the investment managers are automatically paid 2 percent of all assets invested, and earn an additional 20 percent of whatever additional profits they help to bring in. This 20 percent fee is known as "carried interest."

The proper tax treatment of carried interest is a subject of debate. Specifically, it is not always clear whether carried interest should be treated as labor income or capital income. Under current US law, carried interest is treated as capital gains income and is taxed at the same lower rates as long-term capital gains. Some observers argue that because carried interest is a form of compensation for managers' talents and services, it is no different than any other form of labor income.

This option taxes carried interest as ordinary income for all taxpayers. This would increase marginal tax rates on income, reducing incentives to work and save, resulting in lower economic output. However, because carried interest is a relatively small portion of income, the overall macroeconomic effects would be small.

On a conventional basis, this option would decrease the primary deficit by $16.3 billion over the budget window. Long-run GDP and GNP would both be slightly lower. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be largely unchanged from baseline, reaching 175.9 percent by 2056.

Taxing carried interest as ordinary income would primarily affect taxpayers within the top quintile, decreasing after-tax income for this group by less than 0.5 percent.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$16.3B	-$6.1B
Total Deficit Change	-$19.6B	-$7.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.8%	120.8%
CY 2056	175.9%	175.8%	175.9%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-<0.05%	0.0%	0.0%	0.0%	-<0.05%	-0.1%	**-<0.05%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-<0.05%	0.0%	0.0%	0.0%	-<0.05%	-0.1%	**-<0.05%**
Dynamic, Long-Run	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-0.1%	**-<0.05%**

11. Eliminate the Net Investment Income Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**+<0.05%**	**0.0%**	**0.0%**	**0**

The Patient Protection and Affordable Care Act of 2010 (also known as the Affordable Care Act or Obamacare) introduced the net investment income tax (NIIT), a 3.8 percent income tax on certain types of investment income—including capital gains, dividends, interest, passive business income, and others—of high-income taxpayers. The NIIT applies when modified adjusted gross income exceeds $200,000 for single filers or $250,000 for joint filers. The thresholds are not inflation-indexed.

This option repeals the net investment income tax. Repealing the NIIT would increase incentives to save. Domestic saving would rise, and more of the returns to domestic investment would flow to Americans; however, the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners. The net effect is a slight rise in GNP.

On a conventional basis, this option would increase the primary deficit by $444.9 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would rise by less than 0.05 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 179.7 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.4 percent increase, whereas the bottom quintile would experience a 0.0 percent increase. On a long-run dynamic basis, taxpayers would see a 0.2 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$444.9B	+$444.9B
Total Deficit Change	+$536.6B	+$536.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.9%	121.9%
CY 2056	175.9%	179.7%	179.7%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	+<0.05%	+0.4%	+<0.05%	+0.2%	+0.4%	+0.6%	+1.3%	**+0.2%**
Conventional, 2036	0.0%	0.0%	0.0%	+<0.05%	+0.4%	+0.1%	+0.2%	+0.4%	+0.5%	+1.2%	**+0.2%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	+<0.05%	+0.4%	+0.1%	+0.2%	+0.4%	+0.5%	+1.2%	**+0.2%**

12. Expand the Net Investment Income Tax Base to Include Active Income

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.2%	**-0.1%**	**-0.4%**	**-0.2%**	**-54K**

The Patient Protection and Affordable Care Act of 2010 (also known as the Affordable Care Act or Obamacare) introduced the net investment income tax (NIIT), a 3.8 percent income tax on certain types of investment income—including capital gains, dividends, interest, passive business income, and others—of high-income taxpayers. The NIIT applies when modified adjusted gross income exceeds $200,000 for single filers or $250,000 for joint filers. The thresholds are not inflation-indexed.

This option expands the NIIT tax base to include active business income, increasing marginal tax rates on pass-through business income. This would discourage businesses from investing, shrinking the capital stock, wages, and economic output.

On a conventional basis, this option would decrease the primary deficit by $469.6 billion over the budget window. Long-run GDP would fall by 0.2 percent, and long-run GNP by 0.1 percent. On a dynamic basis, the primary deficit would decrease by $333.8 billion from 2027 through 2036, $135.8 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 173.8 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.4 percent decrease, whereas the bottom quintiles would be mostly unaffected. On a long-run dynamic basis, taxpayers would see a 0.4 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$469.6B	-$333.8B
Total Deficit Change	-$567.0B	-$409.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.6%	120.1%
CY 2056	175.9%	172.0%	173.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.4%	-<0.05%	-0.1%	-0.3%	-1.0%	-1.2%	**-0.2%**
Conventional, 2036	0.0%	0.0%	0.0%	-<0.05%	-0.4%	-0.1%	-0.1%	-0.3%	-0.9%	-1.1%	**-0.2%**
Dynamic, Long-Run	-0.2%	-0.1%	-0.2%	-0.2%	-0.6%	-0.2%	-0.3%	-0.5%	-1.1%	-1.3%	**-0.4%**

13. Index Capital Gains Realizations to Inflation

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-0.1%**	**0.0%**	**0.0%**	**0**

Capital gains (losses) are the increase (decrease) in the value of a capital asset between the time it was purchased and the time it was sold without any adjustment for inflation. Without an inflation adjustment, the capital gains tax falls on real gains as well as inflationary gains, which increases the effective tax rate on saving. If indexing capital gains were done alone without indexing other aspects of the tax code to inflation, it could worsen other distortions and create opportunities to shelter income.

This option indexes all capital gains to inflation, removing the tax on "fictitious" income, or gains driven by increases in the price level, and taxing real gains only. Indexing gains would lower the tax burden on saving and increase the incentive to save. Domestic saving would rise, and more of the returns to domestic investment would flow to Americans. However, the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners, resulting in a decline in GNP.

On a conventional basis, this option would increase the primary deficit by $796.5 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would fall by 0.1 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 182.3 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.4 percent. The top quintile of taxpayers would experience a 0.6 percent increase, whereas the bottom quintile would experience a less than 0.05 percent increase. On a long-run dynamic basis, taxpayers would see a 0.4 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$796.5B	+$796.5B
Total Deficit Change	+$968.0B	+$968.0B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	122.8%	122.8%
CY 2056	175.9%	182.3%	182.3%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+<0.05%	+<0.05%	+0.1%	+0.1%	+0.7%	+0.1%	+0.2%	+0.4%	+1.1%	+2.8%	**+0.5%**
Conventional, 2036	+<0.05%	+<0.05%	+0.1%	+0.1%	+0.6%	+0.1%	+0.2%	+0.3%	+0.9%	+2.4%	**+0.4%**
Dynamic, Long-Run	+<0.05%	+<0.05%	+0.1%	+0.1%	+0.6%	+0.1%	+0.2%	+0.3%	+0.9%	+2.4%	**+0.4%**

14. Eliminate the Capital Gains Exclusion on the Sale of a Principal Residence

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.2%	**-<0.05%**	**-0.5%**	**-0.1%**	**-39K**

A taxpayer who sells an asset is typically required to pay capital gains taxes on the profit from the sale. The Taxpayer Relief Act of 1997 created an exception for taxpayers who sell homes that they have owned and lived in for at least two years, excluding up to $250,000 of gains for single homeowners or $500,000 of gains for married homeowners from the tax.

This option repeals the exclusion, subjecting all capital gains from home sales to capital gains tax. Repealing the exclusion would increase the tax burden on saving and investing in homeowner-occupied housing, and potentially increase the lock-in effect, discouraging some homeowners from selling their homes. The smaller budget deficit resulting from the increase in revenue would reduce federal government borrowing and interest payments to foreigners, offsetting some of the decline in GNP.

On a conventional basis, this option would decrease the primary deficit by $794.4 billion over the budget window. Long-run GDP would fall by 0.2 percent, while long-run GNP would decline slightly. On a dynamic basis, the primary deficit would decrease by $670.9 billion from 2027 through 2036, $123.5 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would reach 169.8 percent by 2056.

On average, taxpayers would see decreases in their after-tax incomes in 2036 of 0.5 percent. The top quintile of taxpayers would experience a 0.8 percent decrease, whereas the bottom quintile would experience no change. On a long-run dynamic basis, taxpayers would see a 0.6 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$794.4B	-$670.9B
Total Deficit Change	-$943.9B	-$798.1B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	118.8%	119.3%
CY 2056	175.9%	168.3%	169.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	-<0.05%	-<0.05%	-0.5%	-0.1%	-0.2%	-0.7%	-1.0%	-0.8%	**-0.3%**
Conventional, 2036	0.0%	0.0%	-<0.05%	-0.1%	-0.8%	-0.1%	-0.3%	-0.9%	-1.8%	-1.4%	**-0.5%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.2%	-0.9%	-0.2%	-0.5%	-1.0%	-1.9%	-1.5%	**-0.6%**

15. Eliminate Step-Up in Basis on Capital Gains at Death

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-0.1%**	**0.0%**	**0.0%**	**0**

Under current law, the tax basis of property transferred to an heir at death is "stepped up" to its current market value, such that only the asset appreciation after the inheritance faces capital gains tax upon sale. Step-up in basis ensures that when an asset is passed to an heir, the value of the asset is not subject to both the estate tax and the capital gains tax. It has been critiqued for discouraging taxpayers from realizing capital gains and for benefiting high-income taxpayers, allowing some capital gains to fully escape taxation.

This option repeals step-up in basis and transfers the original owner's cost basis to heirs. Eliminating step-up in basis would raise the effective tax rate on saving. Domestic saving would fall, but foreign investment into the US would increase, preventing a decline in output but causing more of the returns to American investment to flow to foreigners. The smaller budget deficit would reduce federal government borrowing as well as interest payments to foreigners, but GNP would still decline by 0.1 percent.

On a conventional basis, this option would decrease the primary deficit by $206.4 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.3 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, whereas the bottom four quintiles would be unaffected on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$206.4B	-$206.4B
Total Deficit Change	-$250.9B	-$250.9B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.3%	120.3%
CY 2056	175.9%	174.3%	174.3%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.2%	-<0.05%	-<0.05%	-0.1%	-0.4%	-1.0%	**-0.1%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-0.1%	0.0%	-<0.05%	-0.1%	-0.3%	-0.9%	**-0.1%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	-0.1%	0.0%	-<0.05%	-0.1%	-0.3%	-0.9%	**-0.1%**

16. Introduce Mark-to-Market Taxation of Capital Gains

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-0.1%**	**0.0%**	**0.0%**	**0**

Under the current tax system, investors are generally not required to pay taxes on capital gains until they sell their assets. The ability to defer taxes on capital gains reduces the effective tax rate on gains and creates a lock-in effect as investors can minimize their tax liability by holding their assets for longer periods.

This option implements mark-to-market taxation of capital gains for taxpayers with over $1 billion in assets or $100 million in income for three consecutive years, subjecting capital gains of high-income taxpayers to taxation on an annual basis. Mark-to-market would remove investors' choice about when to pay taxes on gains, thus eliminating the lock-in effect created by the ability to defer taxes, but would lead to new problems, including administrative complexity, especially for illiquid assets, and reduced incentives to save.

On a conventional basis, this option would decrease the primary deficit by $628.3 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would fall by 0.1 percent. Incorporating changes in interest costs, the debt-to-GDP ratio would reach 172.6 percent by 2056.

The tax increase would be concentrated among taxpayers in the top 0.01 percent, who would see a decrease in after-tax income of 8.3 percent in the first year of the policy, stabilizing to a 2.2 percent decline in the long run.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$628.3B	-$627.2B
Total Deficit Change	-$801.8B	-$800.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.1%	119.1%
CY 2056	175.9%	172.6%	172.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-1.0%	0.0%	0.0%	0.0%	0.0%	-8.3%	**-0.6%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-0.2%	0.0%	0.0%	0.0%	0.0%	-2.2%	**-0.1%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	-0.2%	0.0%	0.0%	0.0%	0.0%	-2.2%	**-0.1%**

Individual Income Taxes: Credits

Tax credits are provisions that subtract from a taxpayer's tax liability directly. For example, if a taxpayer receives a credit of $1,000, the taxpayer's total taxes owed would be reduced by $1,000.

Typically, tax credits cannot reduce a taxpayer's tax bill below zero, but a few special credits, known as refundable tax credits, can give a taxpayer an income tax bill of less than zero. They are called refundable because they often result in the IRS sending out refund checks to taxpayers.

The earned income tax credit (EITC) and the child tax credit (CTC) are the two most claimed tax credits. In 2026, the CTC has a maximum value of $2,200, with up to $1,700 refundable, and both amounts are indexed to inflation. The EITC is fully refundable and varies by filing status and number of children. The premium tax credit, a subsidy for purchasing health insurance on Affordable Care Act marketplaces, is also refundable.

The major refundable tax credits act as part of the broader safety net for low- and middle-income taxpayers. Other smaller tax credits (such as the lifelong learning credit and the retirement savings credit) serve as subsidies for more narrowly targeted activities. Many tax credits in the individual income tax targeted at green energy, such as the clean vehicle tax credit, were repealed in the One Big Beautiful Bill Act of 2025.

While credits can greatly reduce a taxpayer's liability, their economic effects are more ambiguous. Most credits (and importantly, the major ones) phase out at higher income levels, which creates a marginal tax penalty on additional work. Some, like the EITC, also phase in, which creates a marginal incentive for work for lower-income taxpayers.

This subchapter contains a series of potential changes—increases, decreases, and structural overhauls—of the major individual income tax credits.

17. Double the Earned Income Tax Credit for Workers Without Qualifying Children

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-<0.05%	-<0.05%	-<0.05%	-10K

The earned income tax credit (EITC) is a targeted subsidy for low-income working families. The value of the EITC is a fixed percentage of earned income until the credit reaches its maximum. The EITC stays at its maximum value as earned income continues to increase, until earnings reach a phaseout threshold, above which the credit drops by a fixed percentage for each additional dollar of income over the phaseout threshold. The EITC is a fully refundable credit. The EITC's rates and thresholds depend on a taxpayer's filing status and number of qualifying children.

This option doubles the phase-in rate of the EITC for childless filers from its current 7.65 percent to 15.3 percent, increasing the maximum EITC for taxpayers without qualifying children to $1,075 in 2027. The change would decrease marginal tax rates on taxpayers in the EITC phase-in range but increase marginal tax rates on taxpayers in the phaseout range.

On a conventional basis, this option would increase the primary deficit by $121.3 billion over the budget window. Long-run GDP and GNP would decline slightly. On a dynamic basis, the primary deficit would increase by $136.8 billion from 2027 through 2036, $15.5 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.6 percent by 2056.

Expanding the EITC would benefit taxpayers in the bottom two quintiles. In 2036, the bottom quintile would experience an increase in after-tax income of 1.6 percent, while the top three quintiles would see no change.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$121.3B	+$136.8B
Total Deficit Change	+$147.5B	+$166.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.1%	121.2%
CY 2056	175.9%	176.5%	176.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+1.7%	+0.2%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**+0.1%**
Conventional, 2036	+1.6%	+0.1%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**+<0.05%**
Dynamic, Long-Run	+1.6%	+0.1%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**+<0.05%**

18. Make the Child Tax Credit Refundable from the First Dollar of Earnings

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-<0.05%	-<0.05%	-<0.05%	-6K

The child tax credit reduces income tax liability by a maximum of $2,200 (inflation-adjusted) for each qualifying child under age 17. It phases out by $50 for every $1,000 of adjusted gross income above $200,000 for single parents and $400,000 for married couples filing jointly. If a taxpayer's tax liability is smaller than the value of the credit, a limited amount of the credit can be refunded, calculated as 15 percent of their income that exceeds $2,500, up to a maximum of $1,700 per child (also inflation-adjusted).

This option reduces the refundability threshold so that the credit phases in from the first dollar of earnings, instead of $2,500 of earned income. This would shift the phase-in range of the credit downward, changing marginal tax rates faced by lower-income taxpayers.

On a conventional basis, this option would increase the primary deficit by $25.8 billion over the budget window. Long-run GDP and GNP would decline slightly. On a dynamic basis, the primary deficit would increase by $36.7 billion from 2027 through 2036, $10.9 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.2 percent by 2056.

This option would affect taxpayers in the bottom quintile, increasing after-tax incomes of this group by 0.4 percent in 2027 and 0.3 percent in 2036.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$25.8B	+$36.7B
Total Deficit Change	+$31.6B	+$44.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.9%	120.9%
CY 2056	175.9%	176.0%	176.2%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.4%	+<0.05%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**+<0.05%**
Conventional, 2036	+0.3%	+<0.05%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**+<0.05%**
Dynamic, Long-Run	+0.3%	+<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**0.0%**

19. Make the Child Tax Credit Fully Refundable

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.1%	**-0.1%**	**-0.1%**	**-<0.05%**	**-40K**

The child tax credit reduces income tax liability by a maximum of $2,200 (inflation-adjusted) for each qualifying child under age 17. It phases out by $50 for every $1,000 of adjusted gross income above $200,000 for single parents and $400,000 for married couples filing jointly. If a taxpayer's tax liability is smaller than the value of the credit, a limited amount of the credit can be refunded, calculated as 15 percent of their income that exceeds $2,500, up to a maximum of $1,700 per child (inflation-adjusted).

This option makes the credit fully refundable, removing the phase-in with earned income and the limitation on how much is refundable. While full refundability would increase the tax benefit lower-income taxpayers receive from the credit, it would also increase marginal tax rates on earned income by removing the phase-in.

On a conventional basis, this option would increase the primary deficit by $272.4 billion over the budget window. Long-run GDP and GNP would fall by 0.1 percent. On a dynamic basis, the primary deficit would increase by $334.9 billion from 2027 through 2036, $62.5 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.6 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would be unaffected, whereas the bottom quintile would experience a 2.9 percent increase. On a long-run dynamic basis, taxpayers would see a 0.1 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$272.4B	+$334.9B
Total Deficit Change	+$332.0B	+$406.1B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.5%	121.7%
CY 2056	175.9%	177.0%	177.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+3.7%	+0.5%	+<0.05%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**+0.2%**
Conventional, 2036	+2.9%	+0.3%	+<0.05%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**+0.2%**
Dynamic, Long-Run	+2.9%	+0.2%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**+0.1%**

20. Reduce the Child Tax Credit to $1,000

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	+0.1%	-0.1%	-<0.05%	-5K

Currently, the child tax credit reduces income tax liability by a maximum of $2,200 (inflation-adjusted) for each qualifying child under age 17. It phases out by $50 for every $1,000 of adjusted gross income above $200,000 for single parents and $400,000 for married couples filing jointly. If a taxpayer's tax liability is smaller than the value of the credit, a limited amount of the credit can be refunded, calculated as 15 percent of their income that exceeds $2,500, up to a maximum of $1,700 per child (inflation-adjusted).

This option reduces the child tax credit to $1,000 and does not inflation-adjust it going forward. The smaller credit would limit taxpayer exposure to both the phase-in and the phaseout ranges of the credit, reducing both the positive and negative work incentives created by the credit's effects on marginal tax rates.

On a conventional basis, this option would decrease the primary deficit by $928.1 billion over the budget window. Long-run output would decrease slightly, while long-run GNP would rise by 0.1 percent as the additional revenue raised would decrease federal government borrowing and interest payments to foreigners. On a dynamic basis, the primary deficit would decrease by $901.4 billion from 2027 through 2036, $26.7 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 170.2 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.4 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, whereas the bottom quintile would experience a 1.5 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.4 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$928.1B	-$901.4B
Total Deficit Change	-$1,121.7B	-$1,090.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	118.4%	118.5%
CY 2056	175.9%	169.9%	170.2%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-1.1%	-1.9%	-0.9%	-0.5%	-0.1%	-0.3%	-0.1%	-<0.05%	0.0%	0.0%	**-0.4%**
Conventional, 2036	-1.5%	-2.0%	-0.9%	-0.4%	-0.1%	-0.2%	-<0.05%	0.0%	0.0%	0.0%	**-0.4%**
Dynamic, Long-Run	-1.5%	-2.0%	-0.9%	-0.5%	-0.1%	-0.3%	-0.1%	-<0.05%	-<0.05%	-<0.05%	**-0.4%**

21. Reform the Earned Income Tax Credit and Child Tax Credit

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-0.1%	-<0.05%	-<0.05%	-14K

This option reforms the earned income tax credit (EITC) and child tax credit (CTC) by removing the EITC's variation for number of dependents and expanding the CTC.

Under this option, the EITC phases in at 10 percent up to $1,000 for single filers and $2,000 for joint filers (inflation-adjusted) and phases out at 10 percent beginning at $20,000 single and $40,000 joint. This option makes the CTC fully refundable, with a maximum credit of $3,750 and an additional $750 credit for children under 6. The increases in the credit amounts above the baseline child tax credit ($2,200 in 2026) phase out at 5 percent when income exceeds $85,000 single or $170,000 joint.

These changes would increase average CTC size for lower-income taxpayers but would increase marginal tax rates by eliminating the phase-in and extending the phaseout ranges. Combined with changes in the EITC, marginal tax rates on income would rise slightly overall, while benefits from the refundable credits would also rise overall.

On a conventional basis, this option would increase the primary deficit by $631.8 billion over the budget window. Long-run output would decline slightly, and long-run GNP would decline by 0.1 percent as the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners. On a dynamic basis, the primary deficit would increase by $689.3 billion from 2027 through 2036, $57.5 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 179.2 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.3 percent, with the bottom three quintiles experiencing the largest benefit. On a long-run dynamic basis, taxpayers would see a 0.3 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$631.8B	+$689.3B
Total Deficit Change	+$789.7B	+$859.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	122.5%	122.7%
CY 2056	175.9%	178.9%	179.2%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+3.0%	+1.5%	+1.2%	+0.5%	+<0.05%	+<0.05%	0.0%	0.0%	0.0%	0.0%	**+0.6%**
Conventional, 2036	+0.7%	+0.6%	+0.7%	+0.1%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**+0.3%**
Dynamic, Long-Run	+0.7%	+0.6%	+0.6%	+0.1%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**+0.3%**

Individual Income Taxes: Deductions and Exclusions

Deductions reduce a taxpayer's taxable income. The current tax code offers two primary ways for taxpayers to take deductions: the standard deduction or itemized deductions. Most taxpayers choose the standard deduction, a flat deduction that varies by filing status ($16,100 for single filers and $32,200 for married filers in 2026). Other taxpayers choose to itemize deductions, listing their deductible expenditures on Schedule A.

The largest itemized deductions are for state and local taxes paid, mortgage interest paid, and charitable contributions. Itemizing is popular among higher-income taxpayers because they often have significant deductible expenses in these categories. The Tax Cuts and Jobs Act (TCJA) of 2017 expanded the standard deduction and limited several itemized deductions, causing itemization to fall from 30 percent to 10 percent of taxpayers.

The One Big Beautiful Bill Act temporarily relaxed the TCJA's limits to the deduction for state and local taxes, increasing itemization from 10 percent before 2025 to around 14 percent in 2026. It also expanded the standard deduction and imposed a new limitation on the overall value of itemized deductions for higher-income taxpayers.

In addition to the standard deduction or itemized deductions, the tax code provides other deductions to all taxpayers, or, occasionally, to standard deduction taxpayers only. New temporary provisions, like deductions for some tip and overtime income, are available to taxpayers regardless of itemization decision, but face income limits. And a new charitable deduction is available to non-itemizing taxpayers.

The individual income tax code also contains several exclusions. An exclusion refers to any income that taxpayers are not required to report or pay taxes on. The largest of these is the exclusion of employer-provided health insurance, which makes up a significant share of labor compensation but is not subject to tax.

Deductions and exclusions are worthy of scrutiny because they narrow the US tax base and often create distortions by favoring some forms of labor income over others, or some types of economic activity over others. They are more valuable to taxpayers facing higher marginal rates; a taxpayer in the top bracket saves 37 cents for every dollar of deduction taken, while a taxpayer in the 10 percent bracket saves only 10 cents for each dollar of deduction.

This subchapter includes several changes to deductions and exclusions, ranging from tinkering around the margins by raising or reducing existing deduction values to more dramatic reforms like eliminating the employer-sponsored health insurance exclusion entirely.

22. Increase the Standard Deduction by 25 Percent for All Filing Groups

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-0.1%	-0.3%	-0.1%	+111K

In 2026, the standard deduction is $16,100 for single taxpayers, $32,200 for married filing jointly, and $24,150 for head of household taxpayers. The standard deduction is adjusted for inflation annually.

This option raises all three standard deduction values by 25 percent and continues to inflation-adjust them going forward. A higher standard deduction would push some taxpayers into lower marginal tax brackets, leading to a reduction in the marginal tax rate on income. At the same time, inducing some taxpayers to switch from itemizing their deductions to taking the standard deduction would increase marginal tax rates on certain types of activity, including charitable giving and housing.

On a conventional basis, this option would increase the primary deficit by $1,351.4 billion over the budget window. Long-run GDP would decline slightly, while long-run GNP would fall by 0.1 percent as the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 187.2 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.7 percent. The middle quintiles would benefit the most, with after-tax income increasing between 1.0 percent and 1.1 percent in 2036. The top quintile of taxpayers would experience a 0.5 percent increase, whereas the bottom quintile would experience a 0.1 percent increase, as most already have little to no tax liability. On a long-run dynamic basis, taxpayers would see a 0.7 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$1,351.4B	+$1,348.6B
Total Deficit Change	+$1,621.6B	+$1,616.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	124.2%	124.2%
CY 2056	175.9%	187.2%	187.2%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+0.8%	+1.0%	+0.9%	+0.3%	+0.7%	+0.4%	+0.2%	+0.1%	+<0.05%	**+0.6%**
Conventional, 2036	+0.1%	+1.1%	+1.1%	+1.0%	+0.5%	+0.8%	+0.6%	+0.4%	+0.1%	+<0.05%	**+0.7%**
Dynamic, Long-Run	+0.1%	+1.1%	+1.1%	+1.0%	+0.5%	+0.8%	+0.6%	+0.4%	+0.1%	+<0.05%	**+0.7%**

23. Restore the Personal Exemption

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.3%	**-<0.05%**	**+0.3%**	**+<0.05%**	**+290K**

Before the Tax Cuts and Jobs Act of 2017, personal and dependent exemptions provided an adjustment for household size by allowing taxpayers to exempt $4,050 in income per person. The exemptions phased out for higher-income taxpayers. The exemption was temporarily repealed in the Tax Cuts and Jobs Act of 2017 and permanently repealed in the One Big Beautiful Bill Act of 2025.

This option restores personal and dependent exemptions at $5,400 per person in 2027, inflation-adjusted moving forward. A higher personal exemption would drop some taxpayers into lower tax brackets, reducing marginal tax rates on both labor and capital income. However, this option also restores the personal exemption phaseout, which would increase marginal tax rates for some higher-income taxpayers.

On a conventional basis, this option would increase the primary deficit by $2,622.7 billion over the budget window. Long-run GDP would rise by 0.3 percent, while long-run GNP would fall slightly as the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners. On a dynamic basis, the primary deficit would increase by $2,370.8 billion from 2027 through 2036, $251.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 194.4 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 1.3 percent. The middle quintile would experience the largest increase of 1.9 percent, while the top quintile of taxpayers, limited by the phaseout, would experience a 0.9 percent increase, and the bottom quintile, already with little to no tax liability, would experience a 0.1 percent increase. On a long-run dynamic basis, taxpayers would see a 1.5 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$2,622.7B	+$2,370.8B
Total Deficit Change	+$3,163.7B	+$2,861.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	127.5%	126.5%
CY 2056	175.9%	197.0%	194.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+1.1%	+1.9%	+1.8%	+0.9%	+1.5%	+1.1%	+0.9%	+0.4%	+0.1%	**+1.2%**
Conventional, 2036	+0.1%	+1.7%	+1.9%	+1.8%	+0.9%	+1.4%	+1.1%	+0.9%	+0.4%	+0.1%	**+1.3%**
Dynamic, Long-Run	+0.3%	+1.9%	+2.1%	+2.0%	+1.1%	+1.7%	+1.3%	+1.1%	+0.6%	+0.3%	**+1.5%**

24. Tighten the Limitation on Itemized Deductions

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-<0.05%	-0.1%	-<0.05%	-13K

The One Big Beautiful Bill Act of 2025 introduced a new limitation on itemized deductions for high-income taxpayers in the 37 percent tax bracket, limiting the value of their itemized deductions to 35 percent. Instead of $1 of itemized deduction reducing taxable income by 37 cents, it only reduces it by 35 cents.

This option tightens the itemized deduction limitation to 28 cents on the dollar, affecting taxpayers in the 32 percent bracket, 35 percent bracket, and 37 percent bracket. Reducing the value of itemized deductions would impact economic output through two channels. First, it would increase how much income is subject to tax, raising marginal tax rates on labor and pass-through business income. Second, it would increase the tax burden on economic activity that benefits from itemized deductions, including charitable giving and investment in owner-occupied housing. The resulting reductions in hours worked and the capital stock would shrink economic output.

On a conventional basis, this option would decrease the primary deficit by $169.0 billion over the budget window. Long-run GDP and GNP would decline slightly. On a dynamic basis, the primary deficit would decrease by $139.0 billion from 2027 through 2036, $30.0 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 175.0 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, whereas other groups would be unaffected. On a long-run dynamic basis, taxpayers would see a 0.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$169.0B	-$139.0B
Total Deficit Change	-$207.4B	-$171.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.4%	120.5%
CY 2056	175.9%	174.7%	175.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.2%	-<0.05%	-0.1%	-0.3%	-0.3%	-0.3%	**-0.1%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-0.1%	0.0%	-0.1%	-0.2%	-0.2%	-0.2%	**-0.1%**
Dynamic, Long-Run	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-0.1%	-0.2%	-0.3%	-0.3%	**-0.1%**

25. Eliminate the Home Mortgage Interest Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.4%	**-0.2%**	**-1.1%**	**-0.3%**	**-115K**

The home mortgage interest deduction is an itemized deduction that allows taxpayers to deduct mortgage interest on up to $750,000 in principal. The One Big Beautiful Bill Act made the temporary $750,000 cap permanent instead of allowing the cap to rise back to $1 million at the end of 2025.

This option eliminates the itemized deduction for mortgage interest. Compared to other tax changes, limiting itemized deductions for housing-related expenses has a particularly harmful effect on economic output because it affects multiple margins of economic activity. First, it raises the cost of capital for investment in owner-occupied housing, thus reducing investment in that category. Second, it also raises marginal tax rates on tax filers, reducing returns to work and investment. Third, it would also reduce the use of itemized deductions, which indirectly raises the tax burden on housing investment, as fewer filers take the itemized deduction for state and local taxes (SALT) paid. Notably, the effects of this option are smaller after 2029, when the SALT deduction limit returns to $10,000, which reduces the number of taxpayers who benefit from the mortgage interest deduction.

On a conventional basis, this option would decrease the primary deficit by $367.9 billion over the budget window. Long-run GDP would fall by 0.4 percent and long-run GNP by 0.2 percent. On a dynamic basis, the primary deficit would increase by $12.9 billion from 2027 through 2036, meaning the losses in other tax revenues from the reduction in work and investment dominate the revenue raised by eliminating the itemized deduction. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.4 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent, a smaller effect than earlier in the budget window when more taxpayers are expected to itemize. On a long-run dynamic basis, taxpayers would see a 0.4 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$367.9B	+$12.9B
Total Deficit Change	-$463.0B	-$8.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.8%	121.2%
CY 2056	175.9%	173.6%	177.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-<0.05%	-0.1%	-0.2%	-0.5%	-0.4%	-0.7%	-0.7%	-0.2%	-<0.05%	**-0.3%**
Conventional, 2036	-<0.05%	-<0.05%	-<0.05%	-0.1%	-0.1%	-0.1%	-0.2%	-0.2%	-0.1%	-<0.05%	**-0.1%**
Dynamic, Long-Run	-0.3%	-0.3%	-0.3%	-0.4%	-0.5%	-0.4%	-0.5%	-0.5%	-0.4%	-0.3%	**-0.4%**

26. Eliminate the Charitable Contributions Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.2%	**-0.1%**	**-0.5%**	**-0.1%**	**-66K**

The tax code features two deductions for charitable contributions. The larger of the two is an itemized deduction, which is subject to two major limitations. Taxpayers can only deduct their charitable contributions that exceed 0.5 percent of their adjusted gross income, and taxpayers may only deduct cash charitable contributions of up to 60 percent of their adjusted gross income, and only 50 percent for non-cash contributions. The One Big Beautiful Bill Act of 2025 also introduced a new limit to all itemized deductions, limiting their maximum benefits to 35 cents per dollar of deduction, even for taxpayers in the top tax bracket of 37 percent.

This option repeals the itemized deduction for charitable contributions. Repealing the deduction would increase marginal tax rates on tax filers, reducing returns to work and investment. Further, by indirectly reducing the value of other itemized deductions, like the mortgage interest deduction and state and local tax (SALT) deduction, it would also raise the cost of capital for owner-occupied housing, reducing investment. Notably, the effects of this option are smaller after 2029, as the SALT deduction limit returns to $10,000 then, which reduces the number of taxpayers who benefit from the charitable contribution itemized deduction.

On a conventional basis, this option would decrease the primary deficit by $481.3 billion over the budget window. Long-run GDP would fall by 0.2 percent, and long-run GNP would fall by 0.1 percent. On a dynamic basis, the primary deficit would decrease by $330.9 billion from 2027 through 2036, $150.4 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.0 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.3 percent decrease, while the bottom quintile would be unaffected. On a long-run dynamic basis, taxpayers would see a 0.3 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$481.3B	-$330.9B
Total Deficit Change	-$587.1B	-$409.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.5%	120.1%
CY 2056	175.9%	172.2%	174.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	-<0.05%	-0.1%	-0.1%	-0.4%	-0.2%	-0.3%	-0.4%	-0.5%	-0.7%	**-0.3%**
Conventional, 2036	0.0%	-<0.05%	-0.1%	-0.1%	-0.3%	-0.2%	-0.2%	-0.3%	-0.4%	-0.6%	**-0.2%**
Dynamic, Long-Run	-0.1%	-0.2%	-0.2%	-0.3%	-0.4%	-0.3%	-0.4%	-0.4%	-0.6%	-0.8%	**-0.3%**

27. Eliminate the State and Local Tax Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.2%	**-0.1%**	**-0.5%**	**-0.1%**	**-53K**

The itemized deduction for state and local taxes (SALT) paid allows taxpayers to deduct state and local property taxes, plus either income or sales taxes. In 2026, it is capped at $40,400 for both single and joint taxpayers, and that cap phases down to $10,000 for taxpayers earning above $505,000. The cap is scheduled to rise by 1 percent per year through 2029, after which it will revert to $10,000 for all taxpayers.

This option eliminates the deduction for state and local taxes paid. Eliminating the SALT deduction would increase marginal tax rates on taxpayers who take the deduction, including on labor and pass-through business income, and on investment in owner-occupied housing. Additionally, eliminating the SALT deduction would lead to fewer taxpayers itemizing and taking the mortgage interest deduction, which would further increase the cost of capital for investment in owner-occupied housing.

On a conventional basis, this option would decrease the primary deficit by $207.2 billion over the budget window. Long-run GDP would fall by 0.2 percent, and long-run GNP by 0.1 percent. On a dynamic basis, the primary deficit would decrease by $23.0 billion from 2027 through 2036, $184.2 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.4 percent by 2056.

On average, taxpayers would see decreases in their after-tax incomes in 2036 of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, whereas the bottom quintile would experience a less than 0.05 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.2 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$207.2B	-$23.0B
Total Deficit Change	-$262.5B	-$40.0B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.2%	120.9%
CY 2056	175.9%	174.7%	176.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	0.0%	-<0.05%	-0.1%	-0.3%	-0.2%	-0.5%	-0.5%	-<0.05%	0.0%	**-0.2%**
Conventional, 2036	-<0.05%	-<0.05%	-<0.05%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-<0.05%	-<0.05%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.2%	-0.2%	-0.2%	-0.2%	-0.2%	-0.2%	-0.1%	**-0.2%**

28. Eliminate the State and Local Tax Deduction Cap

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+1.1%	**+0.8%**	**+2.9%**	**+0.7%**	**+553K**

The itemized deduction for state and local taxes (SALT) paid allows taxpayers to deduct state and local property taxes, plus either income or sales taxes. In 2026, it is capped at $40,400 for both single and joint taxpayers, and that cap phases down to $10,000 for taxpayers earning above $505,000. The cap is scheduled to rise by 1 percent per year through 2029, after which it will revert to $10,000 for all taxpayers.

This option eliminates the cap on the SALT deduction. Eliminating the SALT deduction cap would reduce marginal tax rates on taxpayers who take the deduction, including on labor and pass-through business income, and on investment in owner-occupied housing. Additionally, expanding the deductibility of property taxes would lead to more taxpayers itemizing and taking the mortgage interest deduction, which would indirectly reduce the cost of capital for investment in owner-occupied housing.

On a conventional basis, this option would increase the primary deficit by $916.3 billion over the budget window. Long-run GDP would rise by 1.1 percent, and long-run GNP would rise by 0.8 percent. On a dynamic basis, the primary deficit would increase by $264.0 billion from 2027 through 2036, $652.3 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.3 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.5 percent. The top quintile of taxpayers, who are more likely to itemize, would experience a 0.8 percent increase, whereas the bottom quintile, who are less likely to itemize, would experience a slight increase. On a long-run dynamic basis, taxpayers would see a 1.4 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$916.3B	+$264.0B
Total Deficit Change	+$1,088.9B	+$335.9B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	123.1%	120.4%
CY 2056	175.9%	184.0%	174.3%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	+<0.05%	+0.5%	+<0.05%	+<0.05%	+0.6%	+1.3%	+1.1%	**+0.3%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+0.1%	+0.8%	+0.2%	+0.5%	+1.0%	+1.3%	+1.2%	**+0.5%**
Dynamic, Long-Run	+1.0%	+0.8%	+0.9%	+1.0%	+1.7%	+1.2%	+1.5%	+2.0%	+2.3%	+2.2%	**+1.4%**

29. Eliminate the Income Tax Exclusion for Municipal Bond Interest

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	+<0.05%	-0.1%	-<0.05%	-11K

The exemption for municipal bond interest has been a feature of the individual income tax since its inception in 1913. It provides an indirect tax subsidy to state and local governments by reducing their borrowing costs. The tax exemption incentivizes investors to accept lower interest rates on tax-exempt bonds than on taxable bonds. The lower interest rate offsets much of the tax benefit for investors, who tend to be high-income individuals and corporations, allowing state and local governments to capture the benefit.

This option eliminates the tax exclusion for municipal bond interest on a prospective basis. This would increase marginal tax rates on individual and corporate income, resulting in a small negative effect on total economic output. It would also increase borrowing costs for state and local governments.

On a conventional basis, this option would decrease the primary deficit by $157.8 billion over the budget window. Long-run GDP would fall by less than 0.05 percent, while long-run GNP would rise by less than 0.05 percent. On a dynamic basis, the primary deficit would decrease by $155.2 billion from 2027 through 2036, $2.6 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.2 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, and the bottom quintile would also experience a 0.1 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$157.8B	-$155.2B
Total Deficit Change	-$181.3B	-$178.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.4%	120.4%
CY 2056	175.9%	174.1%	174.2%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-0.1%	-0.1%	-0.1%	-0.2%	-0.1%	-0.1%	-0.1%	-0.3%	-0.4%	**-0.1%**
Conventional, 2036	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.2%	-0.3%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.2%	-0.3%	**-0.1%**

30. Cap the Employer-Sponsored Health Insurance Income Tax Exclusion

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.1%	**-<0.05%**	**-0.1%**	**0.0%**	**-93K**

The tax code contains several preferences for healthcare, and the largest is the tax exclusion for employer-sponsored health insurance (ESI) premiums. The exclusion for ESI has been in place since World War II, and it incentivizes employers to shift pay packages toward untaxable ESI benefits rather than taxable wages and salaries. The exclusion distorts the labor market and the healthcare market, as it favors costly insurance coverage tied to employment rather than coverage that travels from one job to the next or direct payments to healthcare providers.

This option imposes a cap on the tax exclusion beginning at the 80th percentile of premiums, subjecting premiums over $14,816 for single plans and $38,185 for family plans to the income tax. The thresholds would be adjusted for wage growth moving forward. The tax increase would be concentrated on upper-income taxpayers and would increase the marginal tax rate on labor income. Hours worked and economic output would therefore fall. Treating at least some portion of ESI the same way as wages and salaries would improve the neutrality of the tax code.

On a conventional basis, this option would decrease the primary deficit by $318.5 billion over the budget window. Long-run GDP would fall by 0.1 percent, and long-run GNP by less than 0.05 percent. On a dynamic basis, the primary deficit would decrease by $242.6 billion from 2027 through 2036, $75.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.0 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.3 percent decrease, whereas the bottom quintile would experience no change. On a long-run dynamic basis, taxpayers would see a 0.2 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$318.5B	-$242.6B
Total Deficit Change	-$383.8B	-$292.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.0%	120.3%
CY 2056	175.9%	173.2%	174.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.2%	-<0.05%	-0.2%	-0.6%	-0.3%	-0.1%	**-0.1%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-0.3%	-<0.05%	-0.2%	-0.6%	-0.4%	-0.1%	**-0.2%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.1%	-0.3%	-0.1%	-0.2%	-0.7%	-0.5%	-0.1%	**-0.2%**

31. Eliminate the Employer-Sponsored Health Insurance Income Tax Exclusion

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-1.1%	**-0.8%**	**-1.2%**	**0.0%**	**-1.4M**

The tax code contains several preferences for healthcare, and the largest is the tax exclusion for employer-sponsored health insurance (ESI) premiums. The exclusion for ESI has been in place since World War II, and it incentivizes employers to shift pay packages toward untaxable ESI benefits rather than taxable wages and salaries. The exclusion distorts the labor market and the healthcare market, as it favors costly insurance coverage tied to employment rather than coverage that travels from one job to the next or direct payments to healthcare providers.

This option fully eliminates the income tax exclusion and includes the full value of ESI in taxable income for the individual income tax. This would increase the tax burden on labor income across the income spectrum, reducing returns to labor, hours worked, and economic output. It would improve the neutrality of the tax code by treating ESI the same way as wages and salaries. The reduction in the federal budget deficit would reduce federal government borrowing as well as interest payments to foreigners, offsetting some of the decline in GNP.

On a conventional basis, this option would decrease the primary deficit by $3,580.7 billion over the budget window. Long-run GDP would fall by 1.1 percent, and long-run GNP would fall by 0.8 percent. On a dynamic basis, the primary deficit would decrease by $2,419.7 billion from 2027 through 2036, $1,161.0 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 157.9 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 1.8 percent. The top quintile of taxpayers would experience a 2.0 percent decrease, and the bottom quintile would also experience a 0.2 percent decrease. On a long-run dynamic basis, taxpayers would see a 2.6 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$3,580.7B	-$2,419.7B
Total Deficit Change	-$4,314.9B	-$2,920.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	111.6%	115.9%
CY 2056	175.9%	146.3%	157.9%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-1.1%	-1.1%	-1.8%	-1.9%	-2.1%	-2.3%	-2.5%	-1.2%	-0.2%	**-1.7%**
Conventional, 2036	-0.2%	-1.0%	-1.2%	-1.8%	-2.0%	-2.1%	-2.4%	-2.6%	-1.3%	-0.2%	**-1.8%**
Dynamic, Long-Run	-1.1%	-1.8%	-2.0%	-2.6%	-2.9%	-3.0%	-3.2%	-3.5%	-2.2%	-1.2%	**-2.6%**

32. Eliminate the Income Tax Exclusion for Other Employer Fringe Benefits

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.2%	**-0.1%**	**-0.2%**	**0.0%**	**-219K**

The tax code currently excludes a variety of fringe benefits from income tax, distorting the incentives employers face when determining the makeup of employee compensation. Exclusions for disability insurance, life insurance, commuter benefits, educational assistance, tuition reduction benefits, on-site gyms, meals and lodging, employer awards, and other miscellaneous benefits favor these compensation types over taxable salaries and wages. Over time, fringe benefits have grown as a share of total labor compensation, due in part to this distortionary tax treatment.

This option removes the income tax exclusion for all the fringes listed above and includes their full value in taxable income for income tax purposes. This would increase the tax burden on labor income across the income spectrum, reducing returns to labor, hours worked, and economic output. It would improve the neutrality of the tax code by treating fringes the same way as wages and salaries.

On a conventional basis, this option would decrease the primary deficit by $571.6 billion over the budget window. Long-run GDP would fall by 0.2 percent, and long-run GNP by 0.1 percent. On a dynamic basis, the primary deficit would decrease by $396.8 billion from 2027 through 2036, $174.8 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 173.0 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.3 percent. The top quintile of taxpayers would experience a 0.3 percent decrease, whereas the bottom quintile would experience a slight decrease. On a long-run dynamic basis, taxpayers would see a 0.4 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$571.6B	-$396.8B
Total Deficit Change	-$688.9B	-$479.1B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.3%	120.0%
CY 2056	175.9%	171.2%	173.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-0.1%	-0.1%	-0.2%	-0.3%	-0.3%	-0.3%	-0.4%	-0.3%	-0.2%	**-0.3%**
Conventional, 2036	-<0.05%	-0.1%	-0.2%	-0.3%	-0.3%	-0.3%	-0.3%	-0.4%	-0.4%	-0.2%	**-0.3%**
Dynamic, Long-Run	-0.2%	-0.3%	-0.3%	-0.4%	-0.5%	-0.4%	-0.5%	-0.5%	-0.5%	-0.4%	**-0.4%**

33. Make Permanent the Enhanced Senior Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+<0.05%	**-<0.05%**	**+<0.05%**	**+<0.05%**	**+5K**

The One Big Beautiful Bill Act of 2025 provided a new deduction of $6,000 for individuals 65 or older available for tax years 2025 through 2028. The deduction is available to itemizers and non-itemizers, but it begins to phase out when modified adjusted gross income exceeds $75,000 for single taxpayers or $150,000 for joint filers.

This option makes the new $6,000 senior deduction permanent. For some taxpayers, the senior deduction lowers marginal tax rates, but for others who are subject to the phaseout, it creates higher marginal tax rates on income. These two effects largely cancel, resulting in little overall impact on marginal tax rates and economic output.

On a conventional basis, this option would increase the primary deficit by $137.9 billion over the budget window. Long-run GDP would rise by less than 0.05 percent, while long-run GNP would fall slightly. On a dynamic basis, the primary deficit would increase by $132.5 billion from 2027 through 2036, $5.4 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.0 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.1 percent. Because of the phaseout at the top and low taxable income at the bottom, the main beneficiaries of the change are the middle three quintiles. On a long-run dynamic basis, taxpayers would see a 0.1 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$137.9B	+$132.5B
Total Deficit Change	+$162.1B	+$155.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.1%	121.1%
CY 2056	175.9%	177.1%	177.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**0.0%**
Conventional, 2036	+<0.05%	+0.3%	+0.2%	+0.1%	+<0.05%	+<0.05%	0.0%	0.0%	0.0%	0.0%	**+0.1%**
Dynamic, Long-Run	+<0.05%	+0.3%	+0.2%	+0.1%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	**+0.1%**

34. Make Permanent the Deduction of Overtime Pay from Taxable Income

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.1%	**+0.1%**	**+0.2%**	**+<0.05%**	**+186K**

The One Big Beautiful Bill Act of 2025 created a temporary deduction for some overtime pay, available for tax years 2025 through 2028. It allows taxpayers to deduct the part of overtime compensation that exceeds their standard hourly rate (typically, the "half" of time-and-a-half pay), up to $12,500 for single filers or $25,000 for joint filers. The deduction begins to phase out when modified adjusted gross income exceeds $150,000 for single filers or $300,000 for joint filers.

This option makes the overtime pay deduction permanent. The deduction reduces how much income is subject to tax, and it may also push some taxpayers into lower tax brackets, reducing marginal tax rates on some income. The phaseout raises marginal tax rates for other taxpayers. Overall, the deduction lowers marginal tax rates on income, increasing after-tax returns to work. As a result, hours worked would increase, and economic output would expand.

On a conventional basis, this option would increase the primary deficit by $372.4 billion over the budget window. Long-run GDP and GNP would rise by 0.1 percent. On a dynamic basis, the primary deficit would increase by $238.2 billion from 2027 through 2036, $134.2 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.6 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.2 percent. The main beneficiaries would be the middle three quintiles, as the bottom quintile already has little to no tax liability, and the top quintile is limited by the phaseout. On a long-run dynamic basis, taxpayers would see a 0.3 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$372.4B	+$238.2B
Total Deficit Change	+$436.2B	+$279.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.7%	121.2%
CY 2056	175.9%	179.1%	177.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**0.0%**
Conventional, 2036	+<0.05%	+0.2%	+0.2%	+0.4%	+0.1%	+0.3%	+0.1%	+<0.05%	0.0%	0.0%	**+0.2%**
Dynamic, Long-Run	+0.1%	+0.3%	+0.4%	+0.5%	+0.2%	+0.5%	+0.2%	+0.1%	+0.1%	+0.1%	**+0.3%**

35. Make Permanent the Deduction of Tip Income from Taxable Income

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+<0.05%	**+<0.05%**	**+<0.05%**	**+<0.05%**	**+34K**

The One Big Beautiful Bill Act of 2025 created a deduction for qualified tips received in occupations that customarily and regularly receive tips for tax years 2025 through 2028. The maximum annual deduction is limited to $25,000, and the deduction phases out when modified adjusted gross income exceeds $150,000 for single filers or $300,000 for joint filers. The deduction complicates the tax code, worsens equity between workers who make similar income but through different forms of compensation, and incentivizes tipped income over other types of taxable compensation. The deduction lowers marginal tax rates on tipped income, but because the deduction phases out, it raises marginal tax rates on workers with income in the phaseout range.

This option makes the deduction for qualified tips permanent. On net, the deduction would have a slightly positive effect on economic output by reducing marginal tax rates on tipped income.

On a conventional basis, this option would increase the primary deficit by $45.9 billion over the budget window. Long-run GDP and GNP would rise slightly. On a dynamic basis, the primary deficit would increase by $20.9 billion from 2027 through 2036, $25.0 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would reach 176.0 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of less than 0.05 percent. Taxpayers in the second and third quintiles would see the largest benefit.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$45.9B	+$20.9B
Total Deficit Change	+$54.0B	+$24.8B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.9%	120.8%
CY 2056	175.9%	176.3%	176.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**0.0%**
Conventional, 2036	0.0%	+0.1%	+0.1%	+<0.05%	+<0.05%	+<0.05%	0.0%	0.0%	0.0%	0.0%	**+<0.05%**
Dynamic, Long-Run	+<0.05%	+0.1%	+0.1%	+0.1%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	**+<0.05%**

36. Make Permanent the Deduction for Auto Loan Interest Paid

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-<0.05%	-<0.05%	-<0.05%	-17K

The One Big Beautiful Bill Act of 2025 created a temporary deduction for auto loan interest paid. The deduction is available to all taxpayers regardless of whether they itemize. It allows a deduction of up to $10,000 per tax return in interest paid on auto loans for new vehicles assembled in the US. The deduction phases out for taxpayers with modified adjusted gross income (MAGI) exceeding $100,000 for single filers or $200,000 for joint filers, and fully phases out when income reaches $150,000 for single filers or $250,000 for joint filers. The deduction lowers marginal tax rates on income and reduces the cost of purchasing qualifying vehicles. It is scheduled to be in effect for tax years 2025 through 2028, after which it expires.

This option makes the deduction for auto loan interest paid permanent. By reducing the cost of a narrow type of consumption, the option would increase returns to labor, but the phaseout would create higher effective marginal tax rates for some taxpayers as well, resulting in a nearly negligible impact on economic output.

On a conventional basis, this option would increase the primary deficit by $33.7 billion over the budget window. Long-run GDP and GNP would both decline slightly. On a dynamic basis, the primary deficit would increase by $44.5 billion from 2027 through 2036, $10.8 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.4 percent by 2056.

On average, in 2036, taxpayers would see slight increases in their after-tax incomes. Taxpayers in the top 10 percent would not benefit due to the phaseout, while all other income groups would see small increases in after-tax income on a conventional basis. On a long-run dynamic basis, taxpayers would see a slight decline in after-tax income on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$33.7B	+$44.5B
Total Deficit Change	+$39.5B	+$52.0B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.9%	120.9%
CY 2056	175.9%	176.2%	176.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**0.0%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	0.0%	0.0%	0.0%	0.0%	**+<0.05%**
Dynamic, Long-Run	0.0%	0.0%	+<0.05%	+<0.05%	0.0%	+<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**-<0.05%**

37. Tax All Social Security Benefits for Higher-Income Earners

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-<0.05%	-<0.05%	-<0.05%	-16K

Social Security benefits have been partially taxable since 1983. Tax liability depends on combined income, defined as adjusted gross income, tax-exempt interest, and half of Social Security benefits. Single filers earning below $25,000 (joint below $32,000) owe no tax on benefits. For single filers earning between $25,000 and $34,000 ($32,000 and $44,000 joint), up to 50 percent of benefits are taxable.

Above those thresholds, up to 85 percent of benefits are taxable. This treatment is similar to the treatment of other retirement income: post-tax retirement contributions are not taxed upon withdrawal, while pre-tax contributions are taxed upon withdrawal. Employer contributions to Social Security are like pre-tax contributions, and the resulting benefits should be subject to tax, while employee contributions are like post-tax contributions, and the resulting benefits should not be subject to tax.

This option taxes all Social Security benefits for high-income taxpayers, phasing in between $125,000 and $150,000 for single filers or $250,000 to $275,000 for joint filers. Raising the portion of benefits included in taxable income would increase marginal tax rates on income and discourage work amongst retirees. As a result, hours worked and economic output would fall.

On a conventional basis, this option would decrease the primary deficit by $102.7 billion over the budget window. Long-run GDP and GNP would fall slightly. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 175.1 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent, with the changes concentrated among upper-income taxpayers. On a long-run dynamic basis, taxpayers would see a 0.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$102.7B	-$87.8B
Total Deficit Change	-$121.8B	-$104.2B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.5%	120.6%
CY 2056	175.9%	174.9%	175.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.1%	-<0.05%	-0.1%	-0.1%	-0.1%	-<0.05%	**-<0.05%**
Conventional, 2036	0.0%	0.0%	0.0%	-<0.05%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-<0.05%	**-0.1%**
Dynamic, Long-Run	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-0.1%	-0.2%	-0.1%	-0.1%	-<0.05%	**-0.1%**

Individual Income Taxes: Other

The number of potential changes to the individual income tax is practically infinite. This chapter considers four possible structural changes that do not fit properly in other subchapters.

The first is repealing the alternative minimum tax, or AMT. The AMT is effectively a second tax system running parallel to the ordinary individual income tax. It has lower rates and limited deductions. Some taxpayers must calculate their tax liabilities under both the individual income tax and the AMT and pay the higher of the two. By requiring many taxpayers to calculate liability twice, the AMT imposes significant compliance costs in the tax filing process.

The second is the creation of universal savings accounts. The US tax code features around a dozen tax-advantaged savings accounts for specific purposes, such as retirement (the most common), healthcare expenses, and education. These accounts provide neutral tax treatment to saving, eliminating the additional tax penalty on saving that would otherwise occur under an income tax. They accomplish this through different methods: some, like individual retirement accounts, offer either an immediate deduction for contributions and taxation upon withdrawal, or immediate taxation on contributions and exempt withdrawals. Health savings accounts, in contrast, allow deductions for contributions and exemptions for withdrawals, providing a double benefit. A universal savings account would be subject to only one layer of tax, and unlike the current complex savings vehicles, would permit withdrawals for any reason.

This chapter also includes the option to institute a wealth tax. While a wealth tax is a tax on wealth, and not income, it fits best here among the various chapters in this book. The key point to consider with a tax on wealth is that a low tax rate on wealth translates to a very high tax rate on income.

Finally, this chapter considers introducing an employee compensation tax as a replacement for the employer-side payroll tax. It would apply to all forms of employee compensation, not just wages. This base-broadening measure would include employer-sponsored health insurance and other fringe benefits in its tax base.

38. Eliminate the Individual Alternative Minimum Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+<0.05%	**-<0.05%**	**+<0.05%**	**+<0.05%**	**-4K**

The alternative minimum tax (AMT) entered the tax code in 1969 following testimony from the Secretary of the Treasury that 155 high-income individuals had no income tax liability in 1967. It requires some taxpayers to calculate their tax liability under a separate set of rules that capture more income than the ordinary system by providing a larger exemption amount but fewer tax preferences. When calculating their alternative minimum taxable income, taxpayers must add back many preferences, including the standard deduction, the itemized deduction for state and local taxes (SALT) paid, and many others. The AMT then applies a different rate schedule (26 percent and 28 percent) to the resulting measure of income. Taxpayers pay either their ordinary individual income tax liability or their AMT liability, whichever is greater.

This option eliminates the AMT. Some taxpayers who would be in higher tax brackets, such as the 35 or 37 percent brackets under the regular income tax, are currently taxed under the AMT's 26 or 28 percent brackets. As a result, while eliminating the AMT would reduce average tax rates, leading to lower revenue, it would increase marginal tax rates for some taxpayers.

However, by removing the AMT's limitation on certain itemized deductions, this option would reduce the tax burden on investment in owner-occupied housing. On net, these economic effects roughly offset. These estimates do not account for a reduction in compliance costs that would result from eliminating the AMT.

On a conventional basis, this option would increase the primary deficit by $271.1 billion over the budget window. Long-run GDP would rise slightly, while long-run GNP would fall slightly, reflecting the larger budget deficit. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 178.1 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.1 percent, concentrated among high-income taxpayers.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$271.1B	+$268.9B
Total Deficit Change	+$327.0B	+$324.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.5%	121.5%
CY 2056	175.9%	178.2%	178.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	+0.1%	0.0%	+<0.05%	+0.1%	+0.2%	+0.1%	**+0.1%**
Conventional, 2036	0.0%	0.0%	0.0%	+<0.05%	+0.1%	0.0%	+<0.05%	+0.1%	+0.2%	+0.1%	**+0.1%**
Dynamic, Long-Run	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+<0.05%	+<0.05%	+0.1%	+0.2%	+0.1%	**+0.1%**

39. Create Universal Savings Accounts

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+<0.05%	**-<0.05%**	**+<0.05%**	**+<0.05%**	**+8K**

Current law provides at least 11 different types of tax-advantaged saving vehicles, each with a variety of rules and limitations: four main types of retirement saving provisions, four more for saving related to education and disabilities (including the One Big Beautiful Bill Act's Trump Accounts), three more for saving related to health and dependent care, and one for saving related to emergencies. Other countries have found a simpler, more widely available solution to boost saving for taxpayers across income levels. Universal savings accounts (USAs) are tax-advantaged savings vehicles with unrestricted use of funds, allowing participants to save for a variety of reasons, including retirement, education, housing, health, unemployment, and emergencies.

This option establishes Roth-style universal savings accounts, permitting individuals to contribute $10,200 post-tax to a USA in 2027, indexed to inflation thereafter. Unused "contribution room" can be carried forward to the next year. Earnings on contributions grow tax-free. Withdrawals are allowed at any time for any reason without penalty or further taxation and are added back to contribution room. For example, if an individual withdraws $1,000, contribution room increases by $1,000.

USAs would reduce the tax burden on saving, especially for low- and middle-income taxpayers. Domestic saving would rise, and more of the returns to domestic investment would flow to Americans. However, the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners, resulting in a decline in GNP. USAs would also slightly decrease marginal tax rates on income, leading to a small expansion in economic output.

On a conventional basis, this option would increase the primary deficit by $161.8 billion over the budget window. Long-run GDP would rise slightly, while long-run GNP would fall slightly. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 178.5 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.1 percent, and that would rise on a long-run dynamic basis to an average increase of 0.3 percent.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$161.8B	+$159.9B
Total Deficit Change	+$185.6B	+$183.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.2%	121.2%
CY 2056	175.9%	178.6%	178.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	0.0%	**+<0.05%**
Conventional, 2036	+<0.05%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+<0.05%	**+0.1%**
Dynamic, Long-Run	+<0.05%	+0.1%	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	+0.1%	+0.1%	**+0.3%**

40. Introduce a Wealth Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-0.1%**	**0.0%**	**0.0%**	**0**

Wealth taxes are imposed on the market value of total assets minus the market value of total liabilities owned by households. In the US, comprehensive wealth taxes have never been implemented, while most European wealth taxes have been repealed due to administrative complexities and disappointing revenue gains.

Wealth taxes impose a heavier tax burden than may be apparent. For example, consider an investor who owns a long-term bond with a fixed rate of return of 5 percent each year. A 5 percent annual wealth tax would equal a 100 percent income tax rate because the wealth tax would take all this taxpayer's capital income.

This option imposes a 5 percent annual tax on net wealth above $1 billion. A wealth tax rate this high would invite substantial avoidance behavior, significantly reducing the revenue potential of the tax with an estimated avoidance rate of approximately 33 percent. It would also discourage saving among high-income taxpayers, leading to significant declines in wealth from increased consumption.

Domestic saving would fall, but foreign investment into the US would increase, preventing a decline in output but causing more of the returns to American investment to flow to foreigners. The smaller budget deficit would reduce federal government borrowing as well as interest payments to foreigners, but GNP would still decline on net by 0.1 percent. A wealth tax would almost certainly have large transitional effects, including dramatic swings in foreign capital flows and the trade deficit. These estimates do not account for the increase in compliance costs that would result from a wealth tax regime.

On a conventional basis, this option would decrease the primary deficit by $1,506.9 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 167.1 percent by 2056.

A wealth tax would be concentrated on the top 0.1 percent of tax filers, decreasing this group's after-tax income by nearly 10 percent in the long run.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,506.9B	-$1,506.9B
Total Deficit Change	-$1,837.6B	-$1,837.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	116.9%	116.9%
CY 2056	175.9%	167.1%	167.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-1.5%	0.0%	0.0%	0.0%	0.0%	-12.6%	**-0.9%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-1.0%	0.0%	0.0%	0.0%	0.0%	-9.9%	**-0.6%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	-1.0%	0.0%	0.0%	0.0%	0.0%	-9.9%	**-0.6%**

41. Create an Employment Compensation Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.9%	**-0.6%**	**-1.3%**	**-0.4%**	**-650K**

This option replaces the current employer-side Social Security and Medicare payroll taxes with a 7.65 percent tax on all employee compensation.

The current payroll tax base excludes certain types of non-wage-and-salary forms of employee compensation, most notably employer-sponsored health insurance, employer contributions to retirement accounts, and other fringe benefits, and the Social Security tax base is capped at $184,500 for 2026 (a cap that is adjusted for inflation every year). The employee compensation tax under this option would apply to all types of compensation without any cap.

Though the tax would be imposed on employers, its economic burden would fall on workers. By applying to a larger base of labor income without any caps, the employee compensation tax would increase marginal tax rates on labor income, discouraging work and decreasing economic output. Compared to other types of taxes, however, the employee compensation tax would be relatively efficient because the entire burden would fall on labor, which is less responsive to taxation than capital, and relatively neutral, because it would not favor certain types of employee compensation over others.

On a conventional basis, this option would decrease the primary deficit by $2,707.1 billion over the budget window. Long-run GDP would fall by 0.9 percent, and long-run GNP would fall by 0.6 percent. On a dynamic basis, the primary deficit would decrease by $1,968.1 billion from 2027 through 2036, $739.0 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 162.5 percent by 2056.

On average, taxpayers would see decreases in their after-tax incomes in 2036 of 1.2 percent. The top quintile of taxpayers would experience a 1.4 percent decrease, whereas the bottom quintile would experience a 0.7 percent decrease. On a long-run dynamic basis, taxpayers would see a 1.9 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$2,707.1B	-$1,968.1B
Total Deficit Change	-$3,260.9B	-$2,384.8B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	113.9%	116.7%
CY 2056	175.9%	154.0%	162.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.7%	-1.0%	-1.2%	-1.3%	-1.2%	-1.4%	-1.4%	-1.3%	-1.0%	-0.5%	**-1.2%**
Conventional, 2036	-0.7%	-1.0%	-1.2%	-1.3%	-1.3%	-1.4%	-1.4%	-1.3%	-1.1%	-0.6%	**-1.2%**
Dynamic, Long-Run	-1.4%	-1.6%	-1.9%	-2.0%	-2.0%	-2.1%	-2.1%	-2.1%	-1.9%	-1.4%	**-1.9%**

Payroll Taxes

Payroll taxes are the second largest source of federal revenue, after the individual income tax. In 2025, payroll taxes brought in $1.75 trillion, or 33 percent of all federal revenue. Many American taxpayers pay much more in federal payroll taxes than they do in income taxes.

The federal government levies five different payroll taxes.

The Social Security payroll tax applies to an individual's first $184,500 of wages in 2026 (the threshold is inflation-adjusted annually) at a rate of 12.4 percent, split between employees and employers. The same wage threshold applies when calculating Social Security benefits, capping how much high-income retirees receive in line with the cap on the taxes they paid. The Medicare payroll tax applies to all labor earnings at a rate of 2.9 percent. Self-employed workers are subject to the same taxes under the Self-Employed Contributions Act (SECA), although they may deduct the employer-side portion, 7.65 percent, for income tax purposes.

Altogether, the total payroll tax is 15.3 percent of wage and salary income for most earners. In addition, the Affordable Care Act imposed a payroll tax of 0.9 percent on wages and self-employment income of taxpayers earning above $200,000 for single filers and $250,000 for joint filers (the thresholds are not inflation-adjusted). Cumulatively, the Medicare and Social Security payroll taxes are known as FICA, or Federal Insurance Contribution Act, taxes.

Finally, the first $7,000 of an employee's annual wages or salary, unadjusted for inflation, is subject to the 6 percent Federal Unemployment Tax Act (FUTA) tax, used to fund the federal unemployment insurance program. Employers pay this, and, as such, it does not appear as withheld income on a paystub. Employers may claim a 5.4 percent credit for state unemployment taxes paid, effectively reducing the FUTA rate to 0.6 percent.

Though the payroll tax is split between employees and employers, economic theory suggests that employees ultimately bear the employer-side payroll tax burden through lower wages. Economists consider payroll taxes to be among the least harmful ways of raising revenue. This is because payroll taxes only apply to labor income, rather than to capital income. The supply of labor is less responsive to taxation than the supply of capital, thus taxes on labor are less economically harmful per dollar of revenue raised than taxes on capital.

FICA and other payroll taxes support the Social Security and Medicare trust funds, which face large and growing imbalances projected to lead to insolvency by 2032. The essential problem is that spending is projected to grow faster than revenues due to rising costs and an aging population. This chapter considers options to change payroll tax rates and to expand the payroll tax base.

42. Reduce the Employer and Employee Payroll Tax Rate by 1 Percentage Point

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.5%	**+0.2%**	**+0.6%**	**+<0.05%**	**+555K**

The Social Security payroll tax applies to an individual's first $184,500 of wages in 2026 (the threshold is inflation-adjusted annually) at a rate of 12.4 percent, split between employees and employers. Though employers are legally responsible for paying their portion of the payroll tax, the long-term burden of both sides of the payroll tax falls on employees in the form of lower wages. Compared to other tax types, the payroll tax is relatively efficient because the entire burden falls on labor, which is less responsive to taxation than capital.

This option reduces both the employee and employer Social Security payroll tax from 6.2 percent to 5.2 percent, yielding a combined Social Security payroll tax rate of 10.4 percent on the first $184,500 of wages (in 2026, indexed to inflation annually). Lowering payroll taxes would increase the incentive to work, thereby increasing economic output and after-tax incomes.

On a conventional basis, this option would increase the primary deficit by $2,468.0 billion over the budget window. Long-run GDP would rise by 0.5 percent, and long-run GNP by 0.2 percent. On a dynamic basis, the primary deficit would increase by $2,004.3 billion from 2027 through 2036, $463.7 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 191.2 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 1.1 percent. The top quintile of taxpayers would experience a 1.0 percent increase, while the bottom quintile would experience a 1.2 percent increase. On a long-run dynamic basis, taxpayers would see a 1.5 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$2,468.0B	+$2,004.3B
Total Deficit Change	+$2,971.8B	+$2,415.1B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	127.1%	125.3%
CY 2056	175.9%	196.0%	191.2%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+1.2%	+1.2%	+1.4%	+1.4%	+0.9%	+1.4%	+1.3%	+0.9%	+0.3%	+0.1%	**+1.1%**
Conventional, 2036	+1.2%	+1.2%	+1.4%	+1.4%	+1.0%	+1.4%	+1.3%	+0.9%	+0.3%	+0.1%	**+1.1%**
Dynamic, Long-Run	+1.6%	+1.6%	+1.8%	+1.8%	+1.4%	+1.8%	+1.7%	+1.3%	+0.8%	+0.5%	**+1.5%**

43. Increase the Employer and Employee Payroll Tax Rate by 1 Percentage Point

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.5%	**-0.2%**	**-0.6%**	**-<0.05%**	**-578K**

The Social Security payroll tax applies to an individual's first $184,500 of wages in 2026 (the threshold is inflation-adjusted annually) at a rate of 12.4 percent, split between employees and employers. Though employers are legally responsible for paying their portion of the payroll tax, the long-term burden of both sides of the payroll tax falls on employees in the form of lower wages. Compared to other tax types, the payroll tax is relatively efficient because the entire burden falls on labor, which is less responsive to taxation than capital.

This option increases both the employee and employer Social Security payroll tax from 6.2 percent to 7.2 percent, yielding a combined Social Security payroll tax rate of 14.4 percent on the first $184,500 of wages (in 2026, indexed to inflation annually). Raising payroll tax rates would reduce the incentive to work, thereby reducing economic output and after-tax incomes.

On a conventional basis, this option would decrease the primary deficit by $2,432.4 billion over the budget window. Long-run GDP would fall by 0.5 percent, and long-run GNP by 0.2 percent. On a dynamic basis, the primary deficit would decrease by $1,919.4 billion from 2027 through 2036, $513.0 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 161.4 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 1.1 percent. The top quintile of taxpayers would experience a 0.9 percent decrease, while the bottom quintile would experience a 1.2 percent decrease. On a long-run dynamic basis, taxpayers would see a 1.5 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$2,432.4B	-$1,919.4B
Total Deficit Change	-$2,928.8B	-$2,313.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	114.6%	116.5%
CY 2056	175.9%	156.2%	161.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-1.2%	-1.2%	-1.4%	-1.4%	-0.9%	-1.4%	-1.3%	-0.9%	-0.3%	-0.1%	**-1.1%**
Conventional, 2036	-1.2%	-1.2%	-1.3%	-1.4%	-0.9%	-1.4%	-1.3%	-0.9%	-0.3%	-0.1%	**-1.1%**
Dynamic, Long-Run	-1.6%	-1.5%	-1.7%	-1.7%	-1.4%	-1.8%	-1.7%	-1.3%	-0.8%	-0.5%	**-1.5%**

44. Expand the Payroll Tax Cap to Cover 90 Percent of Wages

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.7%	**-0.7%**	**-0.9%**	**-<0.05%**	**-891K**

The Social Security payroll tax and self-employment tax apply to an individual's first $184,500 of wages in 2026 (the threshold is inflation-adjusted annually) at a rate of 12.4 percent, split between employees and employers. The same wage threshold applies when calculating Social Security benefits, capping how much high-income retirees receive in line with the cap on the taxes they paid. In 2023, 83 percent of wages and salaries were subject to the payroll tax, but the share has generally been declining since the 1983 Social Security Amendments, the last major reform to Social Security that addressed short-term insolvency concerns.

This option increases the payroll tax cap to cover 90 percent of wages, setting the cap at $346,000 beginning in 2027 and indexing it for wage growth moving forward. This option does not change the calculation for Social Security benefits. Expanding the Social Security payroll tax and self-employment tax to cover a greater amount of labor income would reduce incentives to work, shrinking hours worked and long-run economic output.

On a conventional basis, this option would decrease the primary deficit by $1,295.3 billion over the budget window. Long-run GDP and long-run GNP would fall by 0.7 percent. On a dynamic basis, the primary deficit would decrease by $482.2 billion from 2027 through 2036, $813.1 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 173.7 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.6 percent. The top quintile of taxpayers would experience a 0.9 percent decrease, whereas the bottom quintile would experience no change. On a long-run dynamic basis, taxpayers would see a 1.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,295.3B	-$482.2B
Total Deficit Change	-$1,562.8B	-$584.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	117.5%	120.5%
CY 2056	175.9%	165.7%	173.7%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	-<0.05%	-1.0%	-0.3%	-1.0%	-2.0%	-1.1%	-0.2%	**-0.6%**
Conventional, 2036	0.0%	0.0%	0.0%	-<0.05%	-0.9%	-0.2%	-0.9%	-1.9%	-1.2%	-0.2%	**-0.6%**
Dynamic, Long-Run	-0.6%	-0.6%	-0.6%	-0.6%	-1.5%	-0.8%	-1.5%	-2.5%	-1.8%	-0.9%	**-1.1%**

45. Apply the Payroll Tax to Earnings Above $400,000

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.7%	**-0.5%**	**-0.7%**	**0.0%**	**-843K**

The Social Security payroll tax and self-employment tax apply to an individual's first $184,500 of wages in 2026 (the threshold is inflation-adjusted annually) at a rate of 12.4 percent, split between employees and employers. The same wage threshold applies when calculating Social Security benefits, capping how much high-income retirees receive in line with the cap on the taxes they paid.

This option expands the Social Security payroll tax and self-employment tax to apply to all labor income above $400,000, but not to any labor income in between the current threshold and $400,000, creating a so-called "donut hole." Over time, because of inflation adjustments to the current wage base, the donut hole would close, and all labor income would be subject to the tax. This option does not change the calculation for Social Security benefits. By increasing marginal tax rates on labor income, this option would discourage work among high-income individuals, reducing long-run economic output.

On a conventional basis, this option would decrease the primary deficit by $1,476.5 billion over the budget window. Long-run GDP would fall by 0.7 percent, and long-run GNP by 0.5 percent. On a dynamic basis, the primary deficit would decrease by $819.6 billion from 2027 through 2036, $656.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 170.1 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.8 percent. The top quintile of taxpayers would experience a 1.3 percent decrease, whereas the bottom quintile would experience no change. On a long-run dynamic basis, taxpayers would see a 1.3 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,476.5B	-$819.6B
Total Deficit Change	-$1,761.8B	-$978.2B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	117.1%	119.5%
CY 2056	175.9%	163.1%	170.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.9%	0.0%	-<0.05%	-0.8%	-2.9%	-2.4%	**-0.6%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-1.3%	-<0.05%	-0.2%	-1.3%	-3.7%	-3.1%	**-0.8%**
Dynamic, Long-Run	-0.6%	-0.5%	-0.5%	-0.5%	-1.8%	-0.5%	-0.7%	-1.8%	-4.2%	-3.6%	**-1.3%**

46. Eliminate the Employer-Sponsored Health Insurance Payroll Tax Exclusion

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.2%	**-<0.05%**	**-0.2%**	**0.0%**	**-283K**

The tax code contains several preferences for healthcare, and the largest is the income and payroll tax exclusion for employer-sponsored health insurance (ESI) premiums. The exclusion for ESI has been in place since World War II, and it incentivizes employers to shift pay packages toward untaxable ESI benefits rather than taxable wages and salaries.

This option fully eliminates the payroll tax exclusion and includes the full value of ESI in taxable income for the payroll tax without changing the current $184,500 (inflation-adjusted) wage cap. This would increase the tax burden on labor income, reducing returns to labor, hours worked, and economic output. Some taxpayers, however, would see a reduction in marginal tax rates because including the value of their employer-sponsored health insurance in the payroll tax base would put their total income above the wage limit, offsetting some of the negative effect on output. Eliminating the payroll tax exclusion would improve the neutrality of the tax code by treating ESI the same way as wages and salaries for payroll tax purposes.

On a conventional basis, this option would decrease the primary deficit by $1,834.5 billion over the budget window. Long-run GDP would fall by 0.2 percent, and long-run GNP by less than 0.05 percent. On a dynamic basis, the primary deficit would decrease by $1,610.5 billion from 2027 through 2036, $224.0 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 163.4 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.9 percent. The top quintile of taxpayers would experience a 0.6 percent decrease, while the bottom quintile would experience a 0.5 percent decrease. On a long-run dynamic basis, taxpayers would see a 1.0 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,834.5B	-$1,610.5B
Total Deficit Change	-$2,210.3B	-$1,941.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	116.1%	116.9%
CY 2056	175.9%	161.1%	163.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.5%	-1.3%	-1.2%	-1.3%	-0.6%	-1.1%	-0.8%	-0.3%	-0.1%	-<0.05%	**-0.8%**
Conventional, 2036	-0.5%	-1.1%	-1.2%	-1.3%	-0.6%	-1.1%	-0.8%	-0.4%	-0.1%	-<0.05%	**-0.9%**
Dynamic, Long-Run	-0.7%	-1.2%	-1.4%	-1.4%	-0.8%	-1.3%	-1.0%	-0.6%	-0.3%	-0.2%	**-1.0%**

47. Eliminate the Payroll Tax Exclusion for Other Employer Fringe Benefits

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	0.0%	-<0.05%	0.0%	-44K

The tax code currently excludes a variety of fringe benefits from income and payroll tax, distorting the incentives employers face when determining the makeup of employee compensation. Exclusions for disability insurance, life insurance, commuter benefits, educational assistance, tuition reduction benefits, on-site gyms, meals and lodging, employer awards, and other miscellaneous benefits favor these types of compensation over taxable salaries and wages. Over time, fringe benefits have comprised an increasingly larger share of total labor compensation, due in part to this distortionary tax treatment.

This option removes the payroll tax exclusion for all the fringes listed above. This would increase the tax burden on labor income, reducing returns to labor, hours worked, and economic output. Some taxpayers, however, would see a reduction in marginal tax rates because including the value of their fringe benefits in the payroll tax base would put their total income above the wage limit, offsetting some of the negative effect on output. It would improve the neutrality of the tax code by treating fringes the same way as wages and salaries for payroll tax purposes.

On a conventional basis, this option would decrease the primary deficit by $269.8 billion over the budget window. Long-run GDP would decline slightly, while long-run GNP would remain unchanged. On a dynamic basis, the primary deficit would decrease by $235.3 billion from 2027 through 2036, $34.5 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.1 percent by 2056.

On average, taxpayers would see decreases in their after-tax incomes of 0.1 percent on a conventional basis in 2036 and on a long-run dynamic basis.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$269.8B	-$235.3B
Total Deficit Change	-$324.8B	-$283.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.1%	120.2%
CY 2056	175.9%	173.7%	174.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-0.1%	-0.2%	-0.2%	-0.1%	-0.2%	-0.1%	-0.1%	-<0.05%	-<0.05%	**-0.1%**
Conventional, 2036	-0.1%	-0.1%	-0.2%	-0.2%	-0.1%	-0.2%	-0.1%	-0.1%	-<0.05%	-<0.05%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.2%	-0.2%	-0.2%	-0.1%	-0.2%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**

Business Income Taxes

Businesses in the United States can be split into two major categories: pass-through businesses and C corporations. Pass-through business profits are taxed through the individual income tax on owners' tax returns, while C corporation profits are taxed through the corporate income tax at the entity level as well as through capital gains and dividends taxes at the shareholder level.

Both the tax rate and the tax base affect the incentives businesses face.

Pass-through businesses face a top statutory tax rate of 37 percent at the federal level. In combination with state-level tax rates, pass-through businesses face an average top combined statutory rate of 45.5 percent in 2026. The Tax Cuts and Jobs Act (TCJA) of 2017 created a special deduction, Section 199A, allowing pass-through business owners to deduct up to 20 percent of qualified business income (QBI), amounting to a 20 percent reduction in marginal tax rates on pass-through income.

The TCJA cut the federal corporate tax rate from 35 percent in 2017, the highest in the Organisation for Economic Co-operation and Development (OECD) at the time, to 21 percent beginning in 2018, leaving the US above average but lower than several other OECD countries.

Currently, the United States ranks near the middle of all countries with a combined federal and state statutory rate of 25.57 percent, before considering shareholder-level taxes.

Beyond rates, how the tax code defines business profits matters too. The extent to which businesses can fully and immediately deduct investment costs drives decisions to locate and expand investment in the United States. The One Big Beautiful Bill Act of 2025 provided full and immediate deductions for short-lived capital investment (100 percent bonus depreciation) and domestic research and development expenses, but most structures investment remains subject to longer cost recovery schedules.

Other components of the business tax system, including deductions for interest costs, loss deductions, minimum taxes, and the treatment of overseas income, also affect incentives and compliance costs. Different tax treatment of business income based on business form, industry, and other characteristics adds complexity to the tax system and disadvantages certain businesses over others.

This chapter includes a wide range of changes to business taxes, including changes to rates, deductions, credits, international provisions, and broader structural reforms.

Business Income Taxes: Rates

Before the Tax Cuts and Jobs Act of 2017, the federal corporate income tax rate of 35 percent was one of the highest in the world. Today, the US federal corporate tax rate is 21 percent. When taking into account state- and local-level corporate taxes, the US has a weighted average corporate tax rate of 25.57 percent, which is closer to global averages. With the 2017 reforms, the US followed a broader, decades-long trend of reductions in statutory corporate tax rates around the world.

The high pre-TCJA tax rate posed multiple problems: it discouraged real business investment in the US, and it encouraged companies to shift their profits to other jurisdictions. Economists generally find that corporate taxes are more economically harmful than other taxes because they discourage business investment, a central determinant of the long-run size of the economy. Evidence indicates the TCJA's reforms helped drive investment and reduce profit shifting.

This subchapter includes proposals to change the tax rates that apply to corporate income. The corporate income tax largely falls on investment, so changes in the corporate tax rate have significant impacts on the size of the capital stock, worker productivity, and thus total economic output.

This subchapter also considers changes to the stock buyback tax rate. Introduced in 2022, the stock buyback tax is a one percent tax on the corporate repurchasing of shares. Stock buybacks are another way firms can return value to shareholders, so the stock buyback tax represents yet another layer of tax on capital.

Lastly, this subchapter includes the option of introducing a value-added tax at a rate of 10 percent. Value-added taxes are legally paid by businesses, but economically, they fall on consumption. The US is one of the only countries without a value-added tax.

48. Lower the Corporate Income Tax Rate to 15 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.4%	**+0.3%**	**+0.5%**	**+0.3%**	**+94K**

The Tax Cuts and Jobs Act of 2017 lowered the corporate tax rate from 35 percent to 21 percent. Prior to that change, the US had one of the highest statutory corporate tax rates in the world. Now, the US rate is slightly above average among OECD countries. The statutory corporate tax rate affects profit-shifting behavior as well as incentives to invest in the US.

This option lowers the corporate tax rate to 15 percent. A lower corporate tax rate would increase returns on both past and future investment activity. Lowering the cost of capital would increase incentives to invest in the US. In turn, the capital stock would expand, increasing demand for labor, which boosts wages and hours worked.

On a conventional basis, this option would increase the primary deficit by $1,104.6 billion over the budget window. Long-run GDP would rise by 0.4 percent, and long-run GNP by 0.3 percent. On a dynamic basis, the primary deficit would increase by $744.7 billion from 2027 through 2036, $359.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 181.1 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.5 percent. The top quintile of taxpayers would experience a 0.6 percent increase, while the bottom quintile would experience a 0.4 percent increase. On a long-run dynamic basis, taxpayers would see a 0.8 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$1,104.6B	+$744.7B
Total Deficit Change	+$1,334.6B	+$910.8B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	123.6%	122.2%
CY 2056	175.9%	185.0%	181.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.4%	+0.3%	+0.3%	+0.2%	+0.7%	+0.3%	+0.4%	+0.6%	+1.2%	+1.9%	**+0.6%**
Conventional, 2036	+0.4%	+0.4%	+0.4%	+0.4%	+0.6%	+0.4%	+0.5%	+0.6%	+0.8%	+1.2%	**+0.5%**
Dynamic, Long-Run	+0.8%	+0.7%	+0.7%	+0.7%	+0.9%	+0.7%	+0.8%	+0.9%	+1.1%	+1.4%	**+0.8%**

49. Raise the Corporate Income Tax Rate to 28 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.5%	**-0.3%**	**-1.1%**	**-0.4%**	**-134K**

The Tax Cuts and Jobs Act of 2017 lowered the corporate tax rate from 35 percent to 21 percent. Prior to that change, the US had one of the highest statutory corporate tax rates in the world. Now, the US rate is slightly above average among OECD countries.

This option raises the corporate tax rate to 28 percent. A higher corporate tax rate would increase the cost of capital, reducing incentives to invest in the US. The capital stock would shrink, and demand for labor would fall, reducing wages and hours worked. A higher corporate tax rate would also increase profit-shifting incentives.

On a conventional basis, this option would decrease the primary deficit by $1,410.0 billion over the budget window. Long-run GDP would fall by 0.5 percent, and long-run GNP by 0.3 percent.

On a dynamic basis, the primary deficit would decrease by $1,006.3 billion from 2027 through 2036, $403.7 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 169.3 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.7 percent. The top quintile of taxpayers would experience a 0.8 percent decrease, while the bottom quintile would experience a 0.6 percent decrease. On a long-run dynamic basis, taxpayers would see a 1.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,410.0B	-$1,006.3B
Total Deficit Change	-$1,703.5B	-$1,230.9B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	117.2%	118.7%
CY 2056	175.9%	164.5%	169.3%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.5%	-0.4%	-0.3%	-0.3%	-0.9%	-0.4%	-0.5%	-0.7%	-1.5%	-2.4%	**-0.7%**
Conventional, 2036	-0.6%	-0.5%	-0.5%	-0.5%	-0.8%	-0.5%	-0.6%	-0.7%	-1.1%	-1.5%	**-0.7%**
Dynamic, Long-Run	-1.0%	-0.9%	-0.9%	-0.9%	-1.2%	-1.0%	-1.0%	-1.1%	-1.4%	-1.8%	**-1.1%**

50. Introduce a 10 Percent Value-Added Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-2.6%	**-1.1%**	**-2.1%**	**+0.1%**	**-2.5M**

The United States is one of the few countries in the world that does not have a value-added tax (VAT). A VAT is like a sales tax in that it is designed to tax all final consumption. Typically, VATs are administered through a credit-invoice system, in which companies at every step of the supply chain charge VAT to their customers and receive a credit for VAT paid on business inputs. VATs are usually border-adjusted, meaning they tax imports but exempt exports.

This option introduces a VAT of 10 percent on a broad base, covering approximately 72 percent of US GDP. As such, even a low-rate tax could raise a significant amount of revenue. In practice, most VATs exempt certain sectors of the economy, such as nonprofits and healthcare. A VAT with large exemptions would raise much less revenue. A VAT would reduce after-tax returns to labor. As a result, it would have a negative impact on incentives to work, reducing hours worked and total economic output.

On a conventional basis, this option would decrease the primary deficit by $16,291.2 billion over the budget window. Long-run GDP would fall by 2.6 percent, and long-run GNP by 1.1 percent.

The gap between the effect on output (GDP) and income (GNP) is a result of the large change in the US budget deficit; a smaller budget deficit reduces interest payments to foreigners, which increases GNP.

On a dynamic basis, the primary deficit would decrease by $12,959.0 billion from 2027 through 2036, $3,332.2 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 71.6 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 8.1 percent. The top quintile of taxpayers would experience a 7.9 percent decrease, while the bottom quintile would experience an 8.1 percent decrease. On a long-run dynamic basis, taxpayers would see a 10.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$16,291.2B	-$12,959.0B
Total Deficit Change	-$19,621.8B	-$15,605.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	79.2%	90.0%
CY 2056	175.9%	44.0%	71.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-8.3%	-7.7%	-8.4%	-8.3%	-7.8%	-8.4%	-8.4%	-8.1%	-7.3%	-5.9%	**-8.2%**
Conventional, 2036	-8.1%	-7.6%	-8.2%	-8.1%	-7.9%	-8.3%	-8.3%	-8.0%	-7.4%	-6.2%	**-8.1%**
Dynamic, Long-Run	-10.1%	-9.4%	-10.3%	-10.1%	-9.9%	-10.3%	-10.4%	-10.1%	-9.4%	-8.1%	**-10.1%**

51. Increase the Stock Buyback Excise Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.1%	**-0.1%**	**-0.2%**	**-0.1%**	**-32K**

Corporations can return after-tax profits to shareholders through dividends or stock buybacks (also called share repurchases). When firms issue dividends, all taxable shareholders immediately incur tax liability, but when firms repurchase stock, only shareholders who sell face an immediate tax liability, while other shareholders can continue to defer taxation on their capital gains. This results in more favorable tax treatment for share repurchases than for dividends.

The Inflation Reduction Act of 2022 introduced a 1 percent excise tax on stock buybacks. The excise tax lessens the difference in the treatment of dividends and share repurchases, but it causes other distortions, including applying to gross returns and worsening the biases between debt and equity financing and between corporate and noncorporate entities. The excise tax increases the cost of financing for corporations, reducing investment, the capital stock, and economic output.

This option raises the stock buyback excise tax to 4 percent. This would reduce incentives to invest in the United States, shrinking the capital stock and economic output.

On a conventional basis, this option would decrease the primary deficit by $373.6 billion over the budget window. Long-run GDP would fall by 0.1 percent, and so would long-run GNP. On a dynamic basis, the primary deficit would decrease by $292.7 billion from 2027 through 2036, $80.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.0 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.2 percent decrease, whereas the bottom quintile would experience a 0.1 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.3 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$373.6B	-$292.7B
Total Deficit Change	-$453.3B	-$357.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.8%	120.2%
CY 2056	175.9%	173.0%	174.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-0.1%	-0.1%	-0.1%	-0.3%	-0.1%	-0.1%	-0.2%	-0.5%	-0.7%	**-0.2%**
Conventional, 2036	-0.1%	-0.1%	-0.1%	-0.1%	-0.2%	-0.1%	-0.1%	-0.2%	-0.3%	-0.4%	**-0.2%**
Dynamic, Long-Run	-0.2%	-0.2%	-0.2%	-0.2%	-0.3%	-0.2%	-0.3%	-0.3%	-0.4%	-0.5%	**-0.3%**

52. Repeal the Stock Buyback Excise Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+<0.05%	**0.0%**	**+0.1%**	**+<0.05%**	**+10K**

Corporations can return after-tax profits to shareholders through dividends or stock buybacks (also called share repurchases). When firms issue dividends, all taxable shareholders immediately incur tax liability, but when firms repurchase stock, only shareholders who sell face an immediate tax liability, while other shareholders can continue to defer taxation on their capital gains. This results in more favorable tax treatment for share repurchases than for dividends.

The Inflation Reduction Act of 2022 introduced a 1 percent excise tax on stock buybacks. The excise tax lessens the difference in the treatment of dividends and capital gains but introduces and worsens biases between debt and equity financing and between corporate and noncorporate taxation. The excise tax increases the cost of financing for corporations, reducing investment, the capital stock, and economic output.

This option repeals the stock buyback excise tax, which would increase incentives to invest, expanding the capital stock and economic output.

On a conventional basis, this option would increase the primary deficit by $118.5 billion over the budget window. Long-run GDP would rise slightly, while long-run GNP would be unaffected. On a dynamic basis, the primary deficit would increase by $93.2 billion from 2027 through 2036, $25.3 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.6 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent increase, whereas the bottom quintile would experience a less than 0.05 percent increase. On a long-run dynamic basis, taxpayers would see a 0.1 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$118.5B	+$93.2B
Total Deficit Change	+$144.6B	+$113.9B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.1%	121.0%
CY 2056	175.9%	176.8%	176.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+<0.05%	+0.1%	+0.1%	+0.1%	+0.2%	**+0.1%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+<0.05%	+<0.05%	+0.1%	+0.1%	+0.1%	**+0.1%**
Dynamic, Long-Run	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	**+0.1%**

Business Income Taxes: Capital Investment and Cost Recovery

When a business makes an investment—in assets such as equipment, machinery, buildings, or intellectual property via research and development (R&D)—the US tax code does not always allow it to deduct the full cost of the investment immediately. Instead, businesses may be required to spread the deduction over multiple years, according to a set of more than a dozen depreciation schedules.

Requiring businesses to take deductions over time penalizes investment. A deduction today is worth more than a deduction 5 or 15 years from now. Accordingly, taking deductions over time means companies cannot fully recover the real value of their investments after factoring in inflation and opportunity cost, creating a tax penalty.

Because investment is one of the main drivers of economic growth and relatively sensitive to tax policy, even small changes to the tax treatment of investment create large economic effects. Lengthening depreciation schedules decreases overall investment and leads to a smaller economy. On the other hand, expensing—simply allowing businesses to deduct the full cost of investment immediately—is one of the most cost-effective policy tools for encouraging investment and economic growth.

Recent years have seen significant improvements in cost recovery policy. The One Big Beautiful Bill Act of 2025 permanently reintroduced 100 percent bonus depreciation for investments in assets with 20-year schedules or shorter, and full expensing for domestic R&D, eliminating tax penalties on large swaths of investment. The law also created a temporary, narrow provision allowing full expensing for certain manufacturing buildings through 2028, but most buildings are still subject to long depreciation schedules. Investment in foreign R&D by US companies must be deducted over 15 years.

This subchapter considers several options for changing how the US allows companies to deduct investment costs. Some options add to recent improvements; others are reversions to less favorable cost recovery rules.

53. Enact Full Expensing for All Capital Investment

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+2.7%	**+2.5%**	**+5.0%**	**+2.2%**	**+706K**

Businesses can deduct ordinary business costs from revenue to determine taxable income and tax owed. But when businesses make a capital investment, they may only be able to deduct a portion of the cost immediately, with the rest deducted over future years on future tax returns. Delaying deductions prevents businesses from fully recovering investment costs because inflation and the time value of money erode the real value of the deductions.

The One Big Beautiful Bill Act of 2025 permanently gave businesses the ability to fully expense investment in short-lived assets like equipment and machinery, as well as domestic research and development. It also temporarily introduced full expensing for manufacturing structures, which will be available until the end of 2028. But most long-lived assets must still be deducted over decades-long depreciation schedules.

This option introduces full expensing for all capital investment, allowing full and immediate deductions for all investment costs rather than requiring depreciation deductions over time. By eliminating the tax penalty that arises from spreading deductions over time, this option would lower the cost of capital and increase the incentive to invest, boosting the capital stock, wages, and economic output. Because the change primarily affects the timing of deductions, it does not have a substantial revenue cost over the long run.

On a conventional basis, this option would increase the primary deficit by $1,369.6 billion over the budget window. Long-run GDP would rise by 2.7 percent, and long-run GNP by 2.5 percent. On a dynamic basis, the primary deficit would decrease by $321.1 billion from 2027 through 2036, $1,690.7 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 160.4 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.5 percent. The top quintile of taxpayers would experience a 0.6 percent increase, while the bottom quintile would experience a 0.4 percent increase. On a long-run dynamic basis, taxpayers would see a 2.5 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$1,369.6B	-$321.1B
Total Deficit Change	+$1,714.2B	-$244.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	124.4%	117.6%
CY 2056	175.9%	184.0%	160.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.7%	+0.7%	+0.5%	+0.5%	+1.7%	+0.5%	+0.8%	+1.4%	+3.2%	+4.3%	**+1.3%**
Conventional, 2036	+0.4%	+0.3%	+0.2%	+0.2%	+0.6%	+0.3%	+0.4%	+0.5%	+0.9%	+1.2%	**+0.5%**
Dynamic, Long-Run	+2.6%	+2.2%	+2.4%	+2.3%	+2.7%	+2.4%	+2.5%	+2.7%	+3.0%	+3.3%	**+2.5%**

54. Enact Full Expensing for All Structures

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+1.5%	**+1.4%**	**+2.8%**	**+1.2%**	**+400K**

Under current law, when a business invests in a building, it is not recognized as an expense on a business's tax return in the same year. Instead, the business deducts a share of the investment cost each year over multiple decades: 39 years for commercial structures and 27.5 years for residential structures. Due to inflation and the time value of money, the present value of the deductions is worth less than the original investment cost. The only exception is manufacturing structures, which are eligible for immediate expensing until the end of 2028.

This option introduces full expensing for all new investment in structures, allowing full and immediate deductions rather than requiring depreciation deductions over time. By eliminating the tax penalty from long depreciation schedules, this option would lower the cost of capital and increase incentives to invest.

On a conventional basis, this option would increase the primary deficit by $536.6 billion over the budget window. Long-run GDP would rise by 1.5 percent, and long-run GNP by 1.4 percent. On a dynamic basis, the primary deficit would decrease by $433.5 billion from 2027 through 2036, $970.3 billion less than the conventional estimate. Notably, faster cost recovery is largely a timing change, meaning it has little revenue change over the long term. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 166.0 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.3 percent increase, while the bottom quintile would experience a 0.2 percent increase. On a long-run dynamic basis, taxpayers would see a 1.4 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$536.8B	-$433.5B
Total Deficit Change	+$648.8B	-$474.9B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	122.2%	118.3%
CY 2056	175.9%	179.5%	166.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+0.1%	+0.1%	+0.1%	+0.3%	+0.1%	+0.2%	+0.3%	+0.7%	+0.9%	**+0.2%**
Conventional, 2036	+0.2%	+0.2%	+0.1%	+0.1%	+0.3%	+0.1%	+0.2%	+0.3%	+0.5%	+0.6%	**+0.2%**
Dynamic, Long-Run	+1.5%	+1.2%	+1.3%	+1.3%	+1.5%	+1.3%	+1.4%	+1.5%	+1.7%	+1.8%	**+1.4%**

55. Adopt a Neutral Cost Recovery System for All Structures

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+1.5%	**+1.5%**	**+2.8%**	**+1.2%**	**+400K**

Under current law, when a business invests in a building, it is not recognized as an expense on a business's tax return in the same year. Instead, the business deducts a share of its cost each year over multiple decades: 39 years for commercial structures and 27.5 years for residential structures. Due to inflation and the time value of money, the present value of the deductions is worth less than the original investment cost. The only exception is manufacturing structures, which are eligible for immediate expensing until the end of 2028.

This option makes all structures eligible for a neutral cost recovery system. Businesses would still take deductions over asset lives but get to adjust those deductions for both inflation and a real rate of return to preserve the real value of deductions over time. By eliminating the tax penalty from long depreciation schedules, this option would lower the cost of capital and increase incentives to invest.

On a conventional basis, this option would increase the primary deficit by $2.2 billion over the budget window. Outside the budget window, the costs would grow as the neutral cost recovery adjustments compound. While its revenue effects are backloaded, economically, neutral cost recovery has similar effects as full expensing. Both long-run GDP and long-run GNP would rise by 1.5 percent. On a dynamic basis, the primary deficit would decrease by $964.6 billion from 2027 through 2036, $966.8 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 163.8 percent by 2056.

On average, taxpayers would see small increases in their after-tax incomes in 2036, as the conventional revenue change of the adjustments is small within the budget window. On a long-run dynamic basis, taxpayers would see a 1.5 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$2.2B	-$964.6B
Total Deficit Change	-$1.8B	-$1,121.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.8%	116.9%
CY 2056	175.9%	177.1%	163.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-0.1%	**-<0.05%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	**+<0.05%**
Dynamic, Long-Run	+1.5%	+1.3%	+1.4%	+1.3%	+1.6%	+1.4%	+1.5%	+1.6%	+1.8%	+1.9%	**+1.5%**

56. Make Full Expensing for Manufacturing Structures Permanent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.2%	**+0.2%**	**+0.4%**	**+0.2%**	**+50K**

Under current law, when a business invests in a building, it is not recognized as an expense on a business's tax return in the same year. Instead, the business deducts a share of its cost each year over multiple decades: 39 years for commercial structures and 27.5 years for residential structures. Due to inflation and the time value of money, the present value of the deductions is worth less than the original investment cost.

The One Big Beautiful Bill Act of 2025 introduced a new provision allowing full expensing for structures involved in manufacturing. The provision is temporary, active for projects that begin construction between January 19, 2025, and January 1, 2029, and projects must also enter service before January 1, 2031.

This option makes expensing for manufacturing structures permanent. By eliminating the tax penalty on this particular asset class, this provision lowers the cost of capital and increases the incentive to invest.

On a conventional basis, this option would increase the primary deficit by $88.8

\\\ billion over the budget window. Long-run GDP and long-run GNP would rise by 0.2 percent. On a dynamic basis, the primary deficit would decrease by $5.9 billion from 2027 through 2036, $94.7 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 175.0 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent increase, whereas the bottom quintile would experience a smaller increase. On a long-run dynamic basis, taxpayers would see a 0.2 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$88.8B	-$5.9B
Total Deficit Change	+$104.1B	-$2.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.0%	120.6%
CY 2056	175.9%	176.6%	175.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	**0.0%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+<0.05%	+<0.05%	+0.1%	+0.1%	+0.1%	**+0.1%**
Dynamic, Long-Run	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	+0.2%	**+0.2%**

57. Move to the Alternative Depreciation System

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-2.0%	**-1.8%**	**-3.7%**	**-1.6%**	**-544K**

Under current law, when a business invests in a physical asset like a building or a machine, it typically deducts the cost of the asset according to the Modified Accelerated Cost Recovery System, or MACRS. Several provisions allow certain types of assets to be deducted immediately.

The Alternative Depreciation System, or ADS, is a different set of cost recovery rules for investments in physical assets used in limited circumstances. ADS typically requires deductions to be spread over more years than MACRS (up to 50 years for some assets), and unlike MACRS, ADS requires straight-line deductions rather than larger deductions in earlier years. Due to inflation and the time value of money, the present value of the deductions spread over many years or decades is worth less than the original investment cost.

This option implements ADS for all assets and eliminates provisions like bonus depreciation and research and development expensing. By extending asset lives, implementing ADS would create large tax penalties for capital investment, raising the cost of capital and reducing the capital stock, wages, and economic output.

On a conventional basis, this option would decrease the primary deficit by $2,505.6 billion over the budget window. Long-run GDP would fall by 2.0 percent and long-run GNP by 1.8 percent. On a dynamic basis, the primary deficit would decrease by $1,034.9 billion from 2027 through 2036, $1,470.7 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 181.3 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.7 percent. The top quintile of taxpayers would experience a 0.9 percent decrease, while the bottom quintile would experience a 0.7 percent decrease. On a long-run dynamic basis, taxpayers would see a 2.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$2,505.6B	-$1,034.9B
Total Deficit Change	-$3,109.6B	-$1,395.1B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	114.2%	120.0%
CY 2056	175.9%	162.4%	181.3%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-1.3%	-1.0%	-0.8%	-0.7%	-2.3%	-0.8%	-1.2%	-2.0%	-4.4%	-6.0%	**-1.8%**
Conventional, 2036	-0.7%	-0.5%	-0.4%	-0.4%	-0.9%	-0.5%	-0.6%	-0.9%	-1.5%	-1.9%	**-0.7%**
Dynamic, Long-Run	-2.2%	-1.9%	-1.9%	-1.9%	-2.3%	-1.9%	-2.1%	-2.3%	-2.7%	-3.0%	**-2.1%**

58. Eliminate the Section 199A Pass-Through Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.5%	**-0.3%**	**-0.9%**	**-0.4%**	**-143K**

The Tax Cuts and Jobs Act of 2017 introduced the Section 199A pass-through deduction, and the One Big Beautiful Bill Act extended it permanently. It provides a 20 percent deduction for qualified business income earned by pass-through business owners. For single filers earning above $201,775 (joint filers above $403,500; both inflation-adjusted), the deduction is subject to limitations. If income is derived from certain types of service businesses, the deduction phases out and is disallowed. For others, the deduction is limited based on the amount of wages paid and the original cost of business property. While complex, the phaseouts are designed to limit the benefits of the deduction that go to highly compensated labor, rather than true business income.

This option repeals the pass-through deduction. Eliminating the pass-through deduction would raise the cost of capital in the noncorporate sector, thus reducing incentives to invest. Reduced capital investment would lower the capital stock, wages, and economic output.

On a conventional basis, this option would decrease the primary deficit by $835.7 billion over the budget window. Long-run GDP would fall by 0.5 percent, while long-run GNP would fall by 0.3 percent. On a dynamic basis, the primary deficit would decrease by $505.9 billion from 2027 through 2036, $329.8 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 173.4 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.4 percent. The top quintile of taxpayers would experience a 0.5 percent decrease, whereas the bottom quintile would experience a 0.1 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.8 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$835.7B	-$505.9B
Total Deficit Change	-$1,007.4B	-$624.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	118.7%	120.0%
CY 2056	175.9%	168.9%	173.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-0.2%	-0.3%	-0.4%	-0.5%	-0.5%	-0.6%	-0.5%	-0.4%	-0.2%	**-0.4%**
Conventional, 2036	-0.1%	-0.2%	-0.3%	-0.4%	-0.5%	-0.5%	-0.6%	-0.4%	-0.4%	-0.2%	**-0.4%**
Dynamic, Long-Run	-0.5%	-0.6%	-0.7%	-0.8%	-0.9%	-0.9%	-1.0%	-0.9%	-0.9%	-0.7%	**-0.8%**

59. Reform the Section 199A Pass-Through Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.3%	**-0.1%**	**-0.5%**	**-0.2%**	**-80K**

The Tax Cuts and Jobs Act of 2017 introduced the Section 199A pass-through deduction, and the One Big Beautiful Bill Act extended it permanently. It provides a 20 percent deduction for qualified business income earned by pass-through business owners. For single filers earning above $201,775 (joint filers above $403,500; both inflation-adjusted), the deduction is subject to limitations. If income is derived from certain types of service businesses, the deduction phases out and is disallowed. For others, the deduction is limited based on the amount of wages paid and the original cost of business property. While complex, the phaseouts are designed to limit the benefits of the deduction that go to highly compensated labor, rather than true business income.

This option replaces the several limitations on the pass-through deduction with a single limitation based on the adjusted MACRS property basis for the business, allowing businesses to take a deduction equal to 20 percent of their adjusted basis. This option would reduce the benefit of the pass-through deduction, effectively raising marginal tax rates on pass-through business income.

On a conventional basis, this option would decrease the primary deficit by $524.5 billion over the budget window. Long-run GDP would fall by 0.3 percent, while long-run GNP would fall by 0.1 percent. On a dynamic basis, the primary deficit would decrease by $358.2 billion from 2027 through 2036, $166.3 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 173.8 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.3 percent. The top quintile of taxpayers would experience a 0.3 percent decrease, whereas the bottom quintile would experience a 0.1 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.5 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$524.5B	-$358.2B
Total Deficit Change	-$628.1B	-$436.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.5%	120.1%
CY 2056	175.9%	171.3%	173.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-0.1%	-0.2%	-0.3%	-0.2%	-0.4%	-0.5%	-0.2%	+0.2%	+0.4%	**-0.2%**
Conventional, 2036	-0.1%	-0.2%	-0.3%	-0.4%	-0.3%	-0.5%	-0.5%	-0.2%	0.0%	+0.2%	**-0.3%**
Dynamic, Long-Run	-0.3%	-0.4%	-0.5%	-0.6%	-0.5%	-0.7%	-0.7%	-0.5%	-0.3%	-0.1%	**-0.5%**

60. Integrate the Corporate and Individual Tax Systems Through a Dividend Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.7%	**+0.4%**	**+1.2%**	**+0.5%**	**+167K**

The US tax code taxes business income differently depending on business structure and financing method. Noncorporate business profits (sole proprietorships, partnerships, S corporations) are passed through to individual owners' tax returns and taxed through the individual income tax. C corporations face taxation at both the entity and shareholder levels. Equity-financed income is taxed twice (when earned, then again when distributed as dividends), while debt-financed income faces a lighter burden because interest payments are partially deductible. These disparities distort business decisions, encouraging excess borrowing and influencing choices about organizational form.

This option reforms the taxation of business profits by allowing corporations to deduct the dividends they pay to their shareholders from corporate taxable income. This results in one layer of tax on corporate profits distributed to shareholders, which would face the same individual-level taxes as under current law, resulting in treatment like the one layer of tax that applies to pass-through profits at the individual level. By reducing the cost of capital, this reform would spur additional capital investment and increase output.

On a conventional basis, this option would increase the primary deficit by $2,010.0 billion over the budget window. Long-run GDP would rise by 0.7 percent, and long-run GNP by 0.4 percent. On a dynamic basis, the primary deficit would increase by $1,590.5 billion from 2027 through 2036, $419.5 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 186.7 percent by 2056.

On average, taxpayers would see increases in their after-tax incomes in 2036 of 1.0 percent. The top quintile of taxpayers would experience a 1.1 percent increase, whereas the bottom quintile would experience a 0.8 percent increase. On a long-run dynamic basis, taxpayers would see a 1.5 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$2,010.0B	+$1,590.5B
Total Deficit Change	+$2,425.5B	+$1,939.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	125.9%	124.2%
CY 2056	175.9%	192.5%	186.7%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.7%	+0.5%	+0.5%	+0.5%	+1.3%	+0.5%	+0.7%	+1.0%	+2.2%	+3.4%	**+1.0%**
Conventional, 2036	+0.8%	+0.7%	+0.7%	+0.7%	+1.1%	+0.7%	+0.8%	+1.0%	+1.5%	+2.1%	**+1.0%**
Dynamic, Long-Run	+1.4%	+1.2%	+1.3%	+1.2%	+1.6%	+1.3%	+1.4%	+1.6%	+2.0%	+2.5%	**+1.5%**

Business Income Taxes: International

International corporate tax policy is a wide-ranging subject, as it interacts with both US domestic corporate income tax policy and the corporate tax policies of many other countries.

In a globalized economy, determining the "right" taxable income for a multinational company in a particular country is complicated. How do you apportion the profits of a US company's activities in a foreign country? How about a foreign company's profits in the US?

The primary revenue-raising goal of US international tax policy is to protect the US tax base by reducing profit shifting to low-tax countries. But the need to stop profit shifting should not be used as a justification to unduly tax legitimate cross-border investment. Policymakers must minimize damaging impacts on valuable cross-border investments, both inbound and outbound, and avoid overly complex provisions that can lead to unintended behavior and create high compliance costs.

International corporate income tax rules can often be divided into three types. Source-based or territorial taxes count profits where goods and services are produced. Residence-based or worldwide taxes count profits according to a multinational enterprise's home country. Destination-based taxes count profits where goods and services are sold. In practice, international tax systems, including the US's, usually end up having a mix of characteristics from the different types.

Due to considerable uncertainty, all Tax Foundation's international options are modeled without dynamic effects; reduced taxation on investment is generally efficient, but preferential regimes are generally not. Even the conventional estimates are subject to considerable uncertainty. International corporate income data is generally less available and less reliable than domestic corporate or individual income data. Furthermore, international businesses have many more potential behavioral responses—the activities can vary across time, legal structure, and place—than domestic firms or individuals.

This subchapter considers some possible reforms to the US's international business tax code.

61. Expand Research and Development Expensing to Include Foreign-Sited Research

The One Big Beautiful Bill Act permanently restored full expensing for domestic research and development (R&D) investment after the Tax Cuts and Jobs Act of 2017 required five-year amortization beginning in 2022. Foreign R&D investment by American companies must still be amortized over 15 years. This status quo disadvantages US multinationals, which ultimately harms domestic employees.

This option extends R&D expensing to foreign-sited R&D. Extending expensing to foreign-sited R&D would indirectly benefit domestic workers, because when American companies expand abroad, it also makes their domestic workforces more productive on the margin. The estimates below do not capture such benefits, and so this option has no measured economic impacts.

On a conventional basis, this option would increase the primary deficit by $41.9 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.1 percent by 2056.

On average, in 2036, taxpayers would see small increases in their after-tax incomes on both a conventional and dynamic basis.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$41.9B	+$41.9B
Total Deficit Change	+$55.6B	+$55.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.9%	120.9%
CY 2056	175.9%	176.1%	176.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+<0.05%	+0.1%	+0.1%	+0.2%	+0.3%	**+0.1%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	**+<0.05%**
Dynamic, Long-Run	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	**+<0.05%**

62. Restore the 10 Percent Qualified Business Asset Investment Carveout for Net Controlled Foreign Corporation Tested Income and Foreign-Derived Deduction Eligible Income

Prior to the One Big Beautiful Bill Act (OBBBA), both the global intangible low-taxed income (GILTI) and foreign-derived intangible income (FDII) regimes included a qualified business asset investment (QBAI) carveout. QBAI helped divide American corporations' international earnings into tangible income (coming from capital and labor) and intangible income (coming from trademarks, ideas, or intellectual property). It did so by deducting 10 percent of the value of tangible assets (such as buildings or machinery) from the GILTI and FDII tax bases, leaving a proxy for intangible income subject to the preferential rates.

The OBBBA removed QBAI from both calculations. Removing QBAI increased the tax burden for American companies with tangible operations abroad and reduced it for American companies that export and have tangible operations in the US. To reflect these changes, the new law renamed GILTI to "net CFC-tested income" (NCTI) and FDII to "foreign-derived deduction eligible income" (FDDEI).

This option restores the 10 percent QBAI carveout in both regimes. GILTI (NCTI) and FDII (FDDEI) work in opposite directions, so QBAI restoration has different effects on each. For GILTI, restoration is a tax cut: a substance carveout designed to focus the regime on intangible income held abroad. For FDII, restoration is a tax hike: it focuses the preferential rate on intangible income only, making FDII more like a patent box and less like an export subsidy.

Because the FDII tax hike has the greater direct domestic impact, restoring QBAI would on net reduce the deficit. As with other international options, the economic implications are complex and not captured in our model.

On a conventional basis, this option would decrease the primary deficit by $28.6 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower, reaching 175.7 percent by 2056.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$28.6B	-$28.6B
Total Deficit Change	-$34.4B	-$34.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.7%	120.7%
CY 2056	175.9%	175.7%	175.7%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	**-<0.05%**
Conventional, 2036	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**-<0.05%**
Dynamic, Long-Run	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**-<0.05%**

63. Increase the Foreign-Derived Deduction Eligible Income Exclusion to 50 Percent

Foreign-derived deduction eligible income (FDDEI) was originally a measure designed to encourage corporations to locate their intangible assets, and thus more international income, within the US. However, recent changes to FDDEI in the One Big Beautiful Bill Act have made it resemble an export subsidy by extending its benefits to export income from more "tangible" assets. It allows companies to exclude 33 percent of their deduction-eligible income, corresponding to a 14 percent effective tax rate on eligible export income.

This option increases the FDDEI exclusion rate from 33 percent to 50 percent, while leaving the 21 percent corporate rate unchanged, corresponding to a 10.5 percent effective US tax rate on eligible FDDEI income. The more competitive tax rate on FDDEI would help attract more mobile intangible income to the US, and encourage more tangible investment as well, but it may distort business investment decisions toward deduction-eligible income rather than the best economic use.

Tax Foundation modeling reflects only a partial profit-shifting response to a reduced FDDEI rate, but not dynamic effects. As with other international options, the economic implications are complex and not captured in our model.

On a conventional basis, this option would increase the primary deficit by $69.0 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.5 percent by 2056.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$69.0B	+$69.0B
Total Deficit Change	+$83.4B	+$83.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.0%	121.0%
CY 2056	175.9%	176.5%	176.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+0.1%	**+<0.05%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+0.1%	**+<0.05%**
Dynamic, Long-Run	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+0.1%	**+<0.05%**

64. Eliminate the Foreign-Derived Deduction Eligible Income Exclusion

Foreign-derived deduction eligible income (FDDEI) was originally a measure designed to encourage corporations to locate their intangible assets, and thus more international income, within the US. However, recent changes to FDDEI in the One Big Beautiful Bill Act have made it resemble an export subsidy by extending its benefits to export income from more "tangible" assets. It allows companies to exclude 33 percent of their deduction-eligible income, corresponding to a 14 percent effective tax rate on eligible export income.

This option eliminates the FDDEI provision. As modeled here, none of the eligible FDDEI base would be excluded from the corporate income tax base. The higher rate on export income would discourage mobile intangible income from being located in the US. However, it would equalize rates between domestic and export income, which would remove a distortion that favors exports over domestic production. As with other international options, the economic implications are complex and not captured in our model.

On a conventional basis, this option would decrease the primary deficit by $166.6 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.6 percent by 2056.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$166.6B	-$166.6B
Total Deficit Change	-$200.4B	-$200.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.4%	120.4%
CY 2056	175.9%	174.6%	174.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-0.1%	-0.1%	-0.2%	-0.3%	**-0.1%**
Conventional, 2036	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.2%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**

65. Eliminate the Base Erosion and Anti-Abuse Tax

The base erosion and anti-abuse tax (BEAT) is a corporate alternative minimum tax that disallows certain deductible payments to related foreign parties. It functions in part as a valid base erosion measure, but also as a corporate income tax and as a tariff-like barrier on the international activities for which deductions are denied. The mix of these elements is genuinely unknown, but at least some are distortionary and damaging to growth. Even BEAT's overall revenue effect is uncertain because behavior and reported information under one minimum tax regime may not remain the same under another, making counterfactuals challenging to establish. Though BEAT raises little revenue directly, it likely raises considerable revenue indirectly through companies paying more under the ordinary corporate income tax system.

This option repeals BEAT. This would make the US tax base more vulnerable to certain kinds of profit shifting but also remove the tariff-like barrier on legitimate international activity, boosting productivity and potentially even investment. As with other international options, the economic implications are complex and not captured in our model.

On a conventional basis, this option would increase the primary deficit by $257.2 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.9 percent by 2056.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$257.2B	+$257.2B
Total Deficit Change	+$313.2B	+$313.2B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.5%	121.5%
CY 2056	175.9%	177.9%	177.9%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+0.1%	+0.1%	+0.1%	+0.2%	+0.1%	+0.1%	+0.1%	+0.3%	+0.5%	**+0.1%**
Conventional, 2036	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.2%	+0.2%	**+0.1%**
Dynamic, Long-Run	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.2%	+0.2%	**+0.1%**

66. Eliminate the Net Controlled Foreign Corporation Tested Income Foreign Tax Credit Haircut

Net CFC-tested income (NCTI) is the system for taxing international earnings of US companies. It is a hybrid between a territorial and worldwide system, requiring a US shareholder of one or more controlled foreign corporations (CFCs) to partially include in current income a pro rata share of each CFC's tested income, net of tested losses, regardless of whether the earnings are distributed.

This option removes the NCTI foreign tax credit haircut by increasing allowed creditability from 90 percent to 100 percent. It leaves the NCTI inclusion rate and other settings unchanged relative to current law.

As with other international options, the economic implications are complex and not captured in our model. In this case especially, international tax policy effects are heavily dependent on the policy responses that this change evokes in other countries; while foreign tax crediting is a direct tax cut, it indirectly incentivizes, at the margin, increases in the creditable taxes. Tax Foundation modeling does not include assumptions on how or when such a response might happen.

On a conventional basis, this option would increase the primary deficit by $43.1 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.3 percent by 2056.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$43.1B	+$43.2B
Total Deficit Change	+$52.3B	+$52.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.9%	120.9%
CY 2056	175.9%	176.3%	176.3%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+0.1%	**+<0.05%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	**+<0.05%**
Dynamic, Long-Run	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+<0.05%	**+<0.05%**

67. Adopt a Clean 15 Percent Net Controlled Foreign Corporation Tested Income Rate with Full Foreign Tax Credit Crediting

Net CFC-tested income (NCTI) is the system for taxing international earnings of US companies. It is a hybrid between a territorial and worldwide system, requiring a US shareholder of one or more controlled foreign corporations (CFCs) to partially include in current income a pro rata share of each CFC's tested income, net of tested losses, regardless of whether the earnings are distributed.

This option makes two changes to NCTI to bring it more in line with typical international practices: setting the NCTI inclusion to 5/7 and allowing full foreign tax crediting. In combination with a 21 percent domestic rate, those settings produce a clean 15 percent effective US rate on NCTI with no foreign tax credit haircut, rather than the 12.6 percent to 14 percent effective range seen under current law, which varies based on foreign tax rate.

NCTI has no direct effects on the US economy, but likely some indirect economic effects, plus some longer-run elasticities of taxable income worthy of consideration. Operations by a US company in a foreign jurisdiction are often complementary to operations in the US. An increased tax burden on international investment may result in smaller operations abroad, and less investment in the US to support them. An increased NCTI rate would also make US companies less competitive in international mergers and acquisitions, ultimately eroding some of the NCTI base. As with other international options, the economic implications are complex and not captured in our model.

On a conventional basis, this option would decrease the primary deficit by $104.5 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 175.1 percent by 2056.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$104.5B	-$104.5B
Total Deficit Change	-$126.6B	-$126.6B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.5%	120.5%
CY 2056	175.9%	175.1%	175.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-<0.05%	-0.1%	-0.1%	-0.2%	**-0.1%**
Conventional, 2036	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-<0.05%	-0.1%	-0.1%	-0.1%	**-0.1%**
Dynamic, Long-Run	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-<0.05%	-0.1%	-0.1%	-0.1%	**-0.1%**

68. Reduce the Net Controlled Foreign Corporation Tested Income Inclusion Rate to 50 Percent

Net CFC-tested income (NCTI) is the system for taxing international earnings of US companies. It is a hybrid between a territorial and worldwide system, requiring a US shareholder of one or more controlled foreign corporations (CFCs) to partially include in current income a pro rata share of each CFC's tested income, net of tested losses, regardless of whether the earnings are distributed.

This option lowers the share of NCTI included in the US corporate tax base from 60 percent to 50 percent. In broad terms, it reduces the residual US tax burden on covered foreign earnings relative to current law. Under this option, NCTI would be taxed in a 10.5 percent to 11.67 percent range, depending on foreign tax rates, rather than the 12.6 percent to 14 percent range seen under current law.

NCTI has no direct effects on the US economy, but likely some indirect economic effects, plus some longer-run elasticities of taxable income worthy of consideration. Operations by a US company in a foreign jurisdiction are often complementary to operations in the US. A reduced tax burden on international investment may support larger operations abroad, and greater investment in the US to support them. A reduced NCTI rate would also make US companies more competitive in international mergers and acquisitions, ultimately bringing more income into the NCTI base. As with other international options, the economic implications are complex and not captured in our model.

On a conventional basis, this option would increase the primary deficit by $124.0 billion over the budget window. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 176.9 percent by 2056.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$124.0B	+$124.0B
Total Deficit Change	+$150.3B	+$150.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.1%	121.1%
CY 2056	175.9%	176.9%	176.9%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+<0.05%	+<0.05%	+0.1%	+0.1%	+0.2%	**+0.1%**
Conventional, 2036	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+<0.05%	+0.1%	+0.1%	+0.1%	+0.1%	**+0.1%**
Dynamic, Long-Run	+<0.05%	+<0.05%	+<0.05%	+<0.05%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	+0.1%	**+0.1%**

Business Income Taxes: Other

Business tax reform comes in many forms. One of the most common mantras of tax reform is to "lower the rates and broaden the base." While generally a good framing, the phrase has sometimes been misapplied, particularly in relation to reforms that would prevent firms from fully deducting capital investments. The corporate tax base is corporate profits, and corporate profits are revenues minus costs.

Sound corporate tax base-broadening involves removing preferences that tax certain corporate profits at lower rates than the ordinary one. Unsound corporate tax base-broadening involves changing the definition of profits by preventing companies from deducting costs.

This subchapter includes major structural reforms, including replacing the corporate income tax (which mostly falls on investment) with either a value-added tax (which does not fall on investment) or with a destination-based cash flow tax (DBCFT) and changing other major aspects of the corporate tax base, such as the treatment of interest expense. It also considers eliminating the Inflation Reduction Act's corporate alternative minimum tax (CAMT) on book income.

Finally, it includes several incremental base-broadeners, ranging from eliminating non-neutral preferences for narrow types of economic activity—like credit unions, the production of certain biofuels, and low-income housing—to less-sound incremental expansions of the tax base, such as further limiting the deductibility of high-level employee compensation.

69. Eliminate the Deductibility of Business Interest and Exempt Interest Income from Taxation

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-1.6%	**-0.9%**	**-3.4%**	**-1.3%**	**-427K**

The US tax code treats debt and equity financing differently, generally favoring debt as businesses can deduct their interest payments to debtholders (subject to a limitation) but not their dividend payments to stockholders. Beginning in 2018, the Tax Cuts and Jobs Act introduced a new limit on the deduction for business interest paid of 30 percent of EBITDA (earnings before interest, taxes, depreciation, and amortization), intended to reduce the tax code's bias for debt over equity. At the individual level, interest income received is taxable, and at higher rates than dividends, but in practice, a large share of business debt is held by tax-exempt entities or foreigners. The result is a relatively large gap in the income tax and a preference for debt over equity financing.

This option reverses the status quo. Rather than partially limiting interest deduction and partially taxing interest income, it would make interest paid by businesses non-deductible and interest income received non-taxable. By effectively ignoring interest paid and received, the tax system would no longer favor debt financing and would be much simpler. Flipping the treatment of interest would, however, increase the cost of capital by removing the current subsidy for debt financing, reducing capital investment and economic output.

On a conventional basis, this option would decrease the primary deficit by $581.3 billion over the budget window. Long-run GDP would fall by 1.6 percent, and long-run GNP would fall by 0.9 percent. On a dynamic basis, the primary deficit would increase by $364.3 billion from 2027 through 2036, $945.6 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 182.7 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.5 percent. The top quintile of taxpayers would experience a 0.6 percent decrease, whereas the bottom quintile would experience a 0.4 percent decrease. On a long-run dynamic basis, taxpayers would see a 1.8 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$581.3B	+$364.3B
Total Deficit Change	-$665.5B	+$428.1B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.4%	123.3%
CY 2056	175.9%	168.5%	182.7%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-0.1%	-0.1%	-0.2%	-0.1%	**-0.1%**
Conventional, 2036	-0.4%	-0.3%	-0.3%	-0.3%	-0.6%	-0.3%	-0.5%	-0.7%	-1.2%	-0.3%	**-0.5%**
Dynamic, Long-Run	-1.8%	-1.6%	-1.6%	-1.6%	-2.0%	-1.7%	-1.9%	-2.1%	-2.7%	-1.7%	**-1.8%**

70. Replace the Corporate Income Tax with a 5 Percent Value-Added Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.2%	**+0.4%**	**+1.6%**	**+1.3%**	**-883K**

This option repeals the current corporate income tax, with its attendant complexities in defining domestic and foreign income, and replaces it with a 5 percent value-added tax (VAT), which is a broad-based tax on consumption. The corporate income tax raises the cost of capital, discouraging investment, wages, and economic output. Replacing it with a VAT, which allows businesses to immediately deduct the cost of their investments, would reduce the cost of capital, increase investment, and expand economic output. It would also increase the tax burden on labor, leading to a reduction in hours worked.

This option raises substantial revenue because the VAT has a broader base than the corporate income tax, covering approximately 72 percent of US GDP. Exempting sectors of the economy from the VAT would reduce its revenue-raising potential.

Replacing the corporate income tax with a VAT would be regressive. Over the long term, some of the reduction in after-tax income would be offset by the increase in economic output, but because this swap raises substantial revenue, most taxpayers would still see reductions in after-tax income. Imposing the VAT at a lower rate would raise less revenue, creating a smaller decrease in after-tax incomes and a larger growth effect from this option.

On a conventional basis, this option would decrease the primary deficit by $4,013.5 billion over the budget window. Long-run GDP would rise by 0.2 percent, while long-run GNP would rise by 0.4 percent. On a dynamic basis, the primary deficit would decrease by $3,753.6 billion from 2027 through 2036, $259.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 144.4 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 2.0 percent. The top quintile of taxpayers would experience a 1.6 percent decrease, whereas the bottom quintile would experience a 2.4 percent decrease. On a long-run dynamic basis, taxpayers would see a 1.9 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$4,013.5B	-$3,753.6B
Total Deficit Change	-$4,831.3B	-$4,471.0B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	110.5%	111.2%
CY 2056	175.9%	144.7%	144.4%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-2.7%	-2.9%	-3.3%	-3.3%	-1.3%	-3.3%	-2.9%	-2.0%	+1.0%	+4.4%	**-2.1%**
Conventional, 2036	-2.4%	-2.4%	-2.7%	-2.7%	-1.6%	-2.6%	-2.5%	-1.9%	-0.4%	+1.7%	**-2.0%**
Dynamic, Long-Run	-2.2%	-2.2%	-2.5%	-2.4%	-1.5%	-2.4%	-2.3%	-1.7%	-0.4%	+1.5%	**-1.9%**

71. Replace the Corporate Income Tax with a Destination-Based Cash Flow Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+1.4%	**+1.4%**	**+2.6%**	**+1.3%**	**+463K**

The US corporate income tax is a source-based, or "territorial," system, taxing corporate profits where goods and services are produced. The One Big Beautiful Bill Act increased the amount of capital investment that can be deducted immediately, but some portions remain deducted gradually over time. Interest payments are partially deductible, while returns to equity are not, creating a bias toward debt financing. The business tax system also involves complex provisions to address cross-border taxation.

This option replaces the current corporate income tax and individual income taxes on non-corporate businesses with a destination-based cash flow tax. It provides full and immediate expensing for all business investment, flips the treatment of interest so that interest paid is not deductible and interest received is not taxable, removes foreign income from the tax base, removes general business tax credits, removes the Section 199A pass-through deduction, and is border adjusted. The border adjustment, which exempts exports and taxes imports, ensures the tax applies where goods and services are consumed rather than where they are produced.

The resulting measure of profit faces a flat 21 percent tax on all business cash flow. Taxing cash flow and providing full and immediate deductibility for business investment would significantly reduce the cost of capital and incentivize new domestic investment. It would render complex profit-shifting rules unnecessary.

On a conventional basis, this option would decrease the primary deficit by $2,334.7 billion over the budget window. Long-run GDP would rise by 1.4 percent, while long-run GNP would also rise by 1.4 percent. On a dynamic basis, the primary deficit would decrease by $3,276.6 billion from 2027 through 2036, $935.9 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 150.6 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 1.4 percent. The top quintile of taxpayers would experience a 1.2 percent decrease, whereas the bottom quintile would experience a 5.4 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.5 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$2,334.7B	-$3,276.6B
Total Deficit Change	-$2,819.4B	-$3,912.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	114.8%	112.5%
CY 2056	175.9%	160.7%	150.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-5.4%	-2.5%	-1.5%	-1.1%	-1.2%	-1.1%	-1.3%	-1.1%	-1.2%	-2.2%	**-1.4%**
Conventional, 2036	-6.3%	-3.7%	-2.3%	-1.8%	-0.7%	-1.6%	-1.6%	-0.9%	+0.8%	+1.8%	**-1.6%**
Dynamic, Long-Run	-5.4%	-2.9%	-1.3%	-0.8%	+0.4%	-0.6%	-0.5%	+0.2%	+1.9%	+2.9%	**-0.5%**

72. Expand the Limit on the Deductibility of Executive Compensation

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.1%	**-0.1%**	**-0.1%**	**0.0%**	**-163K**

Under current law, public companies face the Section 162(m) limitation, which disallows deductions for compensation in excess of $1 million for covered employees, including the CEO and other C-suite officials.

This option expands the 162(m) limitation to compensation in excess of $1 million for any employee. In practice, the limitation raises the marginal tax rate on (highly compensated) labor, thus reducing labor supply. Notably, the $1 million threshold is not indexed for inflation, meaning over time the limitation would become more economically significant.

On a conventional basis, this option would decrease the primary deficit by $377.5 billion over the budget window. Long-run GDP and GNP would fall by 0.1 percent. On a dynamic basis, the primary deficit would decrease by $254.2 billion from 2027 through 2036, $123.3 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.0 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.3 percent decrease, whereas the bottom quintile would experience no change. On a long-run dynamic basis, taxpayers would see a 0.3 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$377.5B	-$254.2B
Total Deficit Change	-$450.6B	-$303.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	119.8%	120.3%
CY 2056	175.9%	172.7%	174.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.2%	0.0%	0.0%	-<0.05%	-0.6%	-1.2%	**-0.1%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-0.3%	0.0%	0.0%	-<0.05%	-0.9%	-1.6%	**-0.2%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.1%	-0.4%	-0.1%	-0.1%	-0.1%	-1.1%	-1.7%	**-0.3%**

73. Cap the Business State and Local Tax Deduction

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-1.3%	**-1.0%**	**-2.5%**	**-1.0%**	**-370K**

The Tax Cuts and Jobs Act of 2017 introduced a limitation on the individual itemized deduction for state and local taxes (SALT) paid. The limitation applies to all individual taxpayers, including owners of pass-through businesses; however, business-level taxes paid still remain deductible. Businesses pay several different state and local taxes, including income, property, sales, and excise taxes. The deduction for business taxes paid under current law reduces effective statutory tax rates on business income, and has created an opportunity for pass-through entity tax (PTET) workarounds for taxpayers to avoid the individual-level SALT cap.

This option disallows business-level deductions for income and property taxes paid by corporate and non-corporate businesses and ends the current PTET workaround regime. Disallowing business deductions for state and local income and property taxes paid would increase marginal tax rates on business income and reduce incentives to invest, lowering long-run economic output.

On a conventional basis, this option would decrease the primary deficit by $934.9 billion over the budget window. Long-run GDP would fall by 1.3 percent, and long-run GNP by 1.0 percent. On a dynamic basis, the primary deficit would decrease by $188.0 billion from 2027 through 2036, $746.9 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 178.1 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.3 percent. The top quintile of taxpayers would experience a 0.4 percent decrease, while the bottom quintile would experience a 0.3 percent decrease. On a long-run dynamic basis, taxpayers would see a 1.3 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$934.9B	-$188.0B
Total Deficit Change	-$1,128.2B	-$256.3B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	118.4%	120.3%
CY 2056	175.9%	168.3%	178.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.4%	-0.2%	-0.2%	-0.1%	-0.5%	-0.2%	-0.2%	-0.4%	-1.3%	-0.4%	**-0.4%**
Conventional, 2036	-0.3%	-0.2%	-0.2%	-0.2%	-0.4%	-0.2%	-0.3%	-0.4%	-0.8%	-0.4%	**-0.3%**
Dynamic, Long-Run	-1.4%	-1.1%	-1.2%	-1.2%	-1.5%	-1.3%	-1.3%	-1.5%	-1.9%	-1.5%	**-1.3%**

74. Repeal the Corporate Alternative Minimum Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-0.1%	-0.2%	-<0.05%	-14K

The Inflation Reduction Act of 2022 introduced a new 15 percent corporate alternative minimum tax (CAMT) for corporations earning over $1 billion in profits. The original motivation for CAMT was to address discrepancies between book income (calculated for financial statements) and taxable income (calculated for tax returns) by levying a minimum tax on book income.

Book income and taxable income are intended to measure different things and have different rules for legitimate reasons. Taxable income may be lower than book income in a given year because a company has made a lot of investments, which are often deducted faster for tax purposes than they are under book income rules. Placing a tax based on book income would put a disproportionate tax burden on investment. Due to several problems with basing a tax on financial statement income, such as investment incentives, CAMT features several modifications to arrive at adjusted financial statement income, requiring a complex set of calculations.

This option repeals CAMT. Repealing CAMT would lower marginal tax rates for some firms, as they faced a lower, 15 percent rate under the CAMT regime compared to the 21 percent statutory corporate tax rate. As a result, repealing the minimum tax would have a negative, but small, impact on long-run output. Notably, the economic effects of repealing CAMT do not include compliance cost savings, which would be significant.

On a conventional basis, this option would increase the primary deficit by $360.9 billion over the budget window. Long-run GDP would decline slightly, and long-run GNP would fall by 0.1 percent. On a dynamic basis, the primary deficit would increase by $394.5 billion from 2027 through 2036, $33.6 billion more than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 179.6 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.2 percent. The top quintile of taxpayers would experience a 0.2 percent increase, while the bottom quintile would experience a 0.1 percent increase. On a long-run dynamic basis, taxpayers would see a 0.1 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$360.9B	+$394.5B
Total Deficit Change	+$435.0B	+$474.1B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.7%	121.9%
CY 2056	175.9%	179.2%	179.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.1%	+0.1%	+0.1%	+0.1%	+0.2%	+0.1%	+0.1%	+0.2%	+0.4%	+0.7%	**+0.2%**
Conventional, 2036	+0.1%	+0.1%	+0.1%	+0.1%	+0.2%	+0.1%	+0.2%	+0.2%	+0.3%	+0.4%	**+0.2%**
Dynamic, Long-Run	+0.1%	+0.1%	+0.1%	+0.1%	+0.2%	+0.1%	+0.1%	+0.2%	+0.2%	+0.3%	**+0.1%**

75. Reform Green Energy Tax Credits

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**+<0.05%**	**0.0%**	**0.0%**	**0**

The Inflation Reduction Act of 2022 introduced or expanded numerous tax credits for green energy technology. The One Big Beautiful Bill Act repealed many of the individual-side tax credits and imposed limits or sharper phaseouts for many of the business-side credits.

This option further rolls back some of the remaining tax credits, all of which are scheduled to be temporary under current law. It repeals the clean fuel production credit and the carbon sequestration credit. It halves the clean electricity investment tax credit (from 30 to 15 percent), clean electricity production credit, and zero-emission nuclear electricity production credit. It also, where applicable, eliminates the prevailing wage and apprenticeship requirements and location-related bonuses.

Because the credits are temporary, repealing them does not raise the cost of capital in the long run, and so does not alter long-run investment incentives or output. The revenue raised from repeal reduces the budget deficit and federal government borrowing, which reduces interest payments to foreigners and raises American incomes as measured by GNP.

On a conventional basis, this option would decrease the primary deficit by $123.7 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would rise slightly. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 175.1 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of less than 0.05 percent.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$123.7B	-$123.7B
Total Deficit Change	-$153.7B	-$153.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.5%	120.5%
CY 2056	175.9%	175.1%	175.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-0.1%	-0.1%	-0.2%	-0.3%	**-0.1%**
Conventional, 2036	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-0.1%	**-<0.05%**
Dynamic, Long-Run	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-0.1%	**-<0.05%**

76. Repeal the Low-Income Housing Tax Credit and the New Markets Tax Credit

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	+<0.05%	-<0.05%	-<0.05%	-4K

The low-income housing tax credit provides a credit for developers investing in designated affordable housing. It has two tracks: one is awarded non-competitively, and the other is allocated by state housing finance authorities. The low-income housing tax credit has come under scrutiny for high costs per housing unit developed when compared to conventional market-rate housing. The new markets tax credit provides credits for investment in distressed communities and is allocated competitively by the Treasury Department.

This option repeals the low-income housing tax credit and the new markets tax credit. Repealing the two credits would broaden the tax base, and in some cases, slightly increase the cost of capital, thus slightly reducing investment.

On a conventional basis, this option would decrease the primary deficit by $210.5 billion over the budget window. Long-run GDP would fall slightly, while long-run GNP would rise slightly. On a dynamic basis, the primary deficit would decrease by $202.7 billion from 2027 through 2036, $7.8 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.2 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, and the bottom quintile would also experience a 0.1 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$210.5B	-$202.7B
Total Deficit Change	-$252.6B	-$243.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.3%	120.3%
CY 2056	175.9%	174.1%	174.2%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-0.1%	-<0.05%	-<0.05%	-0.1%	-0.2%	-0.3%	**-0.1%**
Conventional, 2036	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.2%	-0.2%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.2%	-0.2%	**-0.1%**

77. Repeal the Tax Exemption for Credit Unions

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	**0.0%**	**-<0.05%**	**-<0.05%**	**-2K**

Credit unions are tax-exempt nonprofit financial institutions. While originally founded as community organizations meant to serve particular, often disadvantaged households and communities, credit unions today are less distinguishable from conventional banks. The number of credit unions has declined, but the remaining credit unions are larger, and the population of credit union customers is similar in terms of economic background to the population of bank customers.

This option repeals the tax exemption for credit unions. This change would broaden the corporate tax base. At the same time, it would slightly increase the cost of capital, thus slightly reducing investment.

On a conventional basis, this option would decrease the primary deficit by $31.7 billion over the budget window. Long-run GDP would fall by less than 0.05 percent, while long-run GNP would be unchanged, as the effects of the smaller deficits offset the effects of reduced investment on American incomes. On a dynamic basis, the primary deficit would decrease by $29.2 billion from 2027 through 2036, $2.5 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 175.7 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of less than 0.05 percent. The top quintile of taxpayers would experience a less than 0.05 percent decrease, whereas the bottom quintile would see no change. On a long-run dynamic basis, taxpayers would see a less than 0.05 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$31.7B	-$29.2B
Total Deficit Change	-$38.2B	-$35.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.7%	120.7%
CY 2056	175.9%	175.7%	175.7%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**-<0.05%**
Conventional, 2036	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**-<0.05%**
Dynamic, Long-Run	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	-<0.05%	**-<0.05%**

Excise Taxes and Customs Duties

Excise taxes are imposed on specific types or categories of goods, unlike broad-based consumption taxes, such as sales taxes and value-added taxes. A century ago, almost half of all federal revenue came from excise taxes on products such as distilled spirits and tobacco; customs duties on imported goods also played a larger role in early US history compared to today.

Today, excise taxes account for only two percent of federal revenue. In 2024, the gasoline tax was the largest ($26 billion), followed by air travel ($13 billion), alcohol ($11 billion), and tobacco ($9 billion). Similarly, customs duties have consistently comprised two percent or less of federal revenue in recent decades, though new tariffs introduced in 2025 caused a spike from $77 billion in 2024 to $195 billion in 2025 (but much of that is due to be refunded after certain tariffs were ruled illegal).

Excise taxes fall into two categories: a user-pays model, where taxes fund a related program (such as gasoline and truck taxes dedicated to the Highway Trust Fund), or a tax on socially harmful activity. The latter can be justified when an activity imposes costs on others not reflected in the market price, though such costs are difficult to measure and translate into an optimal tax rate. The more successful these taxes are at discouraging behavior, the less revenue they raise. Tariffs lack both justifications and instead are aimed at reducing foreign competition and raising revenue.

Economically, excise taxes and tariffs primarily burden labor. They create a wedge between the prices consumers pay and the prices producers receive, reducing income available to compensate workers and business owners, without directly affecting the after-tax return on new investment. Consider an individual who earns $1 after-tax: they can consume it today or save it and earn a 5 percent return, purchasing $1.05 in goods next year. An excise tax does not change this trade-off. As a result, the burden falls primarily on labor income, reducing real after-tax wages, hours worked, and output. The exception is when taxes apply to capital goods or inputs, which can also affect investment.

This chapter considers several excise tax and tariff options. For excise taxes, we consider changes to areas where the US already has federal excise taxes, such as transportation as well as the possibility of a tax on greenhouse gas emissions. We also look at several major tariff proposals.

78. Increase the Federal Gasoline Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-<0.05%	-<0.05%	0.0%	-29K

The federal gas tax and diesel tax have been set at 18.4 cents per gallon and 24.4 cents per gallon since 1993, without any inflation adjustments, reducing the real, inflation-adjusted value of the relevant tax rates. In theory, revenues from road transportation taxes should cover highway costs, aligning with the user-fee model of excise taxes, but highway outlays have exceeded road transportation tax revenue for several years.

This option would raise the gas tax from 18.4 cents per gallon to 28 cents per gallon and the diesel tax from 24.4 cents per gallon to 40 cents per gallon in 2027, adjusting them for inflation moving forward. This option would close the gap between highway spending and road transportation revenue. Like other excise taxes, increasing the gas and diesel tax would reduce real, after-tax wages, hours worked, and economic output.

On a conventional basis, this option would decrease the primary deficit by $210.5 billion over the budget window. Long-run GDP and GNP would fall by less than 0.05 percent. On a dynamic basis, the primary deficit would decrease by $176.9 billion from 2027 through 2036, $33.6 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.5 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, as would bottom quintile. On a long-run dynamic basis, taxpayers would see a 0.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$210.5B	-$176.9B
Total Deficit Change	-$252.5B	-$212.0B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.3%	120.4%
CY 2056	175.9%	174.2%	174.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**
Conventional, 2036	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**

79. Introduce a Vehicle Miles Traveled Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-<0.05%	-<0.05%	-<0.05%	0.0%	-22K

Existing transportation taxes poorly approximate the costs different cars impose on roads. Electric vehicles do not pay the gas tax, while freight traffic is substantially underpriced relative to the wear and tear it creates.

This option would repeal all federal taxes associated with the Highway Trust Fund (gas and diesel taxes, highway use fee, truck sales, and tire taxes) and replaces them with a tax on each mile driven that varies by vehicle weight per axle to approximate maintenance costs imposed, adjusted for inflation. This would better align with a user-pays model. Under this option, the average passenger vehicle would pay approximately 0.9 cents per mile, while the average freight vehicle would pay approximately 10.6 cents per mile. This option would close the gap between highway spending and road transportation revenue. Like other excise taxes, a vehicle miles traveled tax would reduce real, after-tax wages, hours worked, and output.

On a conventional basis, this option would decrease the primary deficit by $157.1 billion over the budget window. Long-run GDP and GNP would fall by less than 0.05 percent. On a dynamic basis, the primary deficit would decrease by $133.7 billion from 2027 through 2036, $23.4 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.8 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.1 percent. The top quintile of taxpayers would experience a 0.1 percent decrease, as would the bottom quintile. On a long-run dynamic basis, taxpayers would see a 0.1 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$157.1B	-$133.7B
Total Deficit Change	-$187.7B	-$159.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.4%	120.5%
CY 2056	175.9%	173.7%	174.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**
Conventional, 2036	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**
Dynamic, Long-Run	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	**-0.1%**

80. Introduce a Carbon Tax at $25 per Ton

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.2%	**-0.1%**	**-0.2%**	**0.0%**	**-194K**

Among economists, a tax on greenhouse gas emissions like CO2 is viewed as an ideal policy solution to address climate change, although identifying the optimal rate is subject to uncertainty.

This option imposes a tax on US greenhouse gas emissions (carbon dioxide, methane, nitrous oxide, and fluorinated gases), including both energy-related and non-energy-related emissions. The tax is border-adjusted, so it exempts emissions from producing exports, while including emissions from purchasing imports.

The tax rate starts at $25 per ton of CO2 equivalent greenhouse gas emissions and rises by inflation plus 1 percent per year. We assume high noncompliance rates for areas where emissions may be difficult to measure, such as methane emissions from agriculture. Like other excise taxes, a carbon tax would primarily burden labor, reducing real, after-tax wages, hours worked, and economic output. These estimates only capture the effect of a carbon tax reducing after-tax returns to labor and do not account for environmental or other benefits, nor compliance or other costs.

On a conventional basis, this option would decrease the primary deficit by $1,099.6 billion over the budget window. Long-run GDP would fall by 0.2 percent, while long-run GNP would fall by 0.1 percent. On a dynamic basis, the primary deficit would decrease by $910.5 billion from 2027 through 2036, $189.1 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 172.8 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 0.5 percent. The top quintile of taxpayers and the bottom quintile of taxpayers would each experience a 0.5 percent decrease. On a long-run dynamic basis, taxpayers would see a 0.6 percent decrease on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,099.6B	-$910.5B
Total Deficit Change	-$1,339.4B	-$1,108.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	118.0%	118.7%
CY 2056	175.9%	171.0%	172.8%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-0.6%	-0.6%	-0.7%	-0.6%	-0.6%	-0.7%	-0.7%	-0.6%	-0.6%	-0.5%	**-0.6%**
Conventional, 2036	-0.5%	-0.5%	-0.5%	-0.5%	-0.5%	-0.5%	-0.5%	-0.5%	-0.4%	-0.4%	**-0.5%**
Dynamic, Long-Run	-0.6%	-0.6%	-0.7%	-0.6%	-0.6%	-0.7%	-0.7%	-0.6%	-0.6%	-0.5%	**-0.6%**

81. Introduce a 10 Percent Universal Tariff

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
-0.4%	**-0.2%**	**-0.3%**	**0.0%**	**-395K**

Tariffs are taxes imposed on imported goods. As tariffs increase the price of foreign-produced goods, they incentivize buyers to switch to domestically produced goods and provide domestic producers room to increase their prices. Tariffs benefit domestic producers who receive higher prices and sales, but tariffs impose costs on foreign producers as well as other businesses and workers in the domestic economy.

This option applies a 10 percent universal tariff to all US goods imports in addition to sector- and country-specific Section 232 and Section 301 tariffs in effect as of April 2026. A universal tariff would affect both consumer goods and capital goods. In 2025, the United States imported $3.3 trillion of general merchandise goods, more than half of which were industrial materials or capital goods like machinery.

In addition to burdening labor like other excise taxes, applying tariffs to capital goods would increase the cost of capital, reducing overall incentives to invest in the United States and shrinking the capital stock, productivity, wages, and output. These estimates only capture the effect of tariffs reducing after-tax returns to labor, likely understating the economic effect on investment and the capital stock. Tariffs may also invite foreign retaliation, whether tariff or non-tariff barriers on US exports, which further reduce US output but generate no additional revenue for the US Treasury. These estimates assume no foreign retaliation.

On a conventional basis, this option would decrease the primary deficit by $1,996.2 billion over the budget window. Long-run GDP would fall by 0.4 percent, while long-run GNP would fall by 0.2 percent. On a dynamic basis, the primary deficit would decrease by $1,522.6 billion from 2027 through 2036, $473.6 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 164.5 percent by 2056.

On average, in 2036, taxpayers would see decreases in their after-tax incomes of 1.0 percent on a conventional basis, rising to 1.3 percent in the long run on a dynamic basis. The top 1 percent of taxpayers would see a slightly smaller decrease.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,996.2B	-$1,522.6B
Total Deficit Change	-$2,404.5B	-$1,833.5B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	115.7%	117.4%
CY 2056	175.9%	159.9%	164.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	-1.0%	-0.9%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-0.9%	-0.7%	**-1.0%**
Conventional, 2036	-1.0%	-0.9%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-1.0%	-0.9%	-0.8%	**-1.0%**
Dynamic, Long-Run	-1.3%	-1.2%	-1.3%	-1.3%	-1.3%	-1.4%	-1.4%	-1.3%	-1.3%	-1.1%	**-1.3%**

82. Repeal All Tariffs Imposed Since 2017

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
+0.3%	**+0.1%**	**+0.3%**	**0.0%**	**+302K**

Tariffs are taxes imposed on imported goods. They are legally paid by the importer of record, and economically, the burden may be shared across foreign exporters, importers, other business owners, or workers. Prior to 2025, tariffs comprised less than 2 percent of federal tax revenues; throughout 2025, that share has climbed to nearly 5 percent of federal revenues as sector-specific, country-specific, and broad-based tariffs have been imposed under various authorities.

The effective tariff rate, a measure of customs duties revenues as a share of goods imports, rose from 1.4 percent in 2017 to 2.7 percent in 2019 and 7.7 percent in 2025. It will likely be lower in 2026 after the *Learning Resources *Supreme Court decision struck down the majority of the new tariffs imposed under emergency authorities.

This option would revert US tariff policy back to 2017 levels, removing all sector-specific, country-specific, and broad-based tariffs that have been imposed under Section 232, Section 301, and Section 122 authorities. Removing tariffs would reduce the tax wedge they impose, increasing returns to labor. Removing tariffs on capital goods and inputs would lower the cost of capital, increasing incentives to invest. These estimates only capture the effect of tariffs reducing after-tax returns to labor, likely understating the economic effect on investment and the capital stock. Removing tariffs may also reduce foreign retaliation, whether tariff or non-tariff barriers on US exports, which would further boost US output. These estimates assume no changes in foreign retaliation.

On a conventional basis, this option would increase the primary deficit by $1,305.4 billion over the budget window. Long-run GDP would rise by 0.3 percent and long-run GNP by 0.1 percent. On a dynamic basis, the primary deficit would increase by $945.3 billion from 2027 through 2036, $360.1 billion less than the conventional estimate. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.7 percent by 2056.

On average, in 2036, taxpayers would see increases in their after-tax incomes of 0.7 percent. The top quintile of taxpayers would experience a 0.6 percent increase, while the bottom quintile would experience a 0.7 percent increase. On a long-run dynamic basis, taxpayers would see a 0.9 percent increase on average.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$1,305.4B	+$945.3B
Total Deficit Change	+$1,572.1B	+$1,137.9B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	124.1%	123.7%
CY 2056	175.9%	178.6%	177.9%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	+0.7%	+0.6%	+0.7%	+0.7%	+0.6%	+0.7%	+0.7%	+0.6%	+0.6%	+0.5%	**+0.7%**
Conventional, 2036	+0.7%	+0.6%	+0.7%	+0.7%	+0.6%	+0.7%	+0.7%	+0.7%	+0.6%	+0.5%	**+0.7%**
Dynamic, Long-Run	+0.9%	+0.8%	+0.9%	+0.8%	+0.8%	+0.9%	+0.9%	+0.9%	+0.8%	+0.7%	**+0.9%**

Estate and Gift Taxes

Estate and gift taxes are the smallest major source of federal revenue, raising just under $30 billion in 2025 and accounting for less than 1 percent of federal revenue.

Estate and gift taxes apply to intergenerational transfers. The estate tax falls on the value of an estate that exceeds an exemption of $15 million for single filers and $30 million for joint filers in 2026, indexed to inflation thereafter. The estate tax applies to gross property (everything that the decedent owned), including stocks, bonds, homes, business interests, art, and personal property. The value of the estate that exceeds the exemption faces a graduated set of rates that rises quickly to a top rate of 40 percent.

The estate tax encourages tax planning and avoidance and entails substantial compliance costs. To reduce avoidance, the gift tax applies to transfers made during a donor's life. The gift tax exemption is integrated with the estate tax exemption. Gifts given during a donor's life reduce the estate tax exemption. The gift tax has an additional exclusion each year ($19,000 for 2026, indexed to inflation), allowing donors to gift a certain amount each year without counting toward the exemption amount. Additionally, the generation-skipping tax applies an additional layer of tax on gifts made to recipients who are two or more generations younger than the donor to further prevent estate tax avoidance.

The presence of an estate tax encourages individuals to consume their wealth during their lifetime rather than invest it for future generations, thus marginally discouraging saving. The estate tax often represents a third or fourth layer of taxation on saving. An individual's income can be taxed when it is earned, when it yields a profit at the business level, when it is returned to the individual via dividend or realized as a capital gain, and upon the individual's death.

In part, to mitigate this double taxation, inheritors do not face income tax on inheritances they receive, and they also get to step-up the basis of assets they inherit to their fair market value so that assets are not subject to both the estate tax and the capital gains tax.

This chapter considers several options to change the estate tax, ranging from repeal to expansion, lowering rates to raising rates, and, more fundamentally, replacing the estate tax and reforming the treatment of capital gains taxes at death.

83. Eliminate the Estate and Gift Tax

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-<0.05%**	**0.0%**	**0.0%**	**0**

In 2026, the estate tax applies to estates above a $15 million exemption threshold ($30 million for joint filers) according to a rate schedule that quickly rises to 40 percent. The gift tax, meanwhile, applies to transfers made during an individual's lifetime, subject to an annual exclusion of $19,000 per recipient as of 2026. The estate and gift taxes effectively fall on saving, as they impose another layer of tax on income earned but not immediately consumed.

This option repeals the estate and gift taxes. Eliminating these taxes would increase the after-tax returns to saving. Domestic saving would rise, and more of the returns to American investment would flow to Americans. However, the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners. These two offsetting effects lead to a slight decline in GNP in the long run. These estimates do not account for the substantial reduction in compliance costs that would come from eliminating the estate and gift taxes.

On a conventional basis, this option would increase the primary deficit by $407.2 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would fall by less than 0.05 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 179.6 percent by 2056.

On average, taxpayers would see increases in their after-tax incomes of 0.2 percent, with the changes all concentrated within the top quintile.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$407.2B	+$407.2B
Total Deficit Change	+$489.4B	+$489.4B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.8%	121.8%
CY 2056	175.9%	179.6%	179.6%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	+0.3%	0.0%	0.0%	0.0%	+1.2%	+1.3%	**+0.2%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	+0.4%	0.0%	0.0%	0.0%	+1.4%	+1.5%	**+0.2%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	+0.4%	0.0%	0.0%	0.0%	+1.4%	+1.5%	**+0.2%**

84. Lower the Top Estate Tax Rate to 30 Percent

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-<0.05%**	**0.0%**	**0.0%**	**0**

In 2026, the estate tax applies to estates above a $15 million exemption threshold ($30 million for joint filers) according to a rate schedule that quickly rises to 40 percent. The estate tax effectively falls on saving, as it imposes another layer of tax on income earned but not immediately consumed.

One way to reduce the burden of the estate tax is by lowering the top marginal rate. This option reduces the top rate to 30 percent. Reducing the estate tax rate would increase the after-tax returns to saving. Domestic saving would rise, and more of the returns to American investment would flow to Americans. However, the larger budget deficit would increase federal government borrowing, and more interest payments would flow to foreigners, resulting in a slight decline in GNP. These estimates do not account for any changes to the substantial cost of complying with the estate and gift taxes.

On a conventional basis, this option would increase the primary deficit by $114.7 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would fall by less than 0.05 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be higher than baseline, reaching 177.0 percent by 2056.

On average, taxpayers would see increases in their after-tax incomes of 0.1 percent, concentrated among the top 1 percent of filers.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	+$114.7B	+$114.7B
Total Deficit Change	+$137.9B	+$137.9B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	121.1%	121.1%
CY 2056	175.9%	177.0%	177.0%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	+0.1%	0.0%	0.0%	0.0%	+0.3%	+0.4%	**+0.1%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	+0.1%	0.0%	0.0%	0.0%	+0.4%	+0.4%	**+0.1%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	+0.1%	0.0%	0.0%	0.0%	+0.4%	+0.4%	**+0.1%**

85. Return the Estate Tax to Clinton-Era Parameters

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-0.1%**	**0.0%**	**0.0%**	**0**

In 2026, the estate tax applies to estates above a $15 million ($30 million for joint filers) exemption threshold according to a rate schedule that quickly rises to 40 percent.

This option returns the estate tax to the estate tax law in effect in 2000. The estate tax per-person exemption is cut to $675,000 and no longer indexed for inflation, and the top tax rate rises to 55 percent for taxable estates and gifts. Reducing the per-person exemption and increasing the top tax rate on estates would significantly increase the scope of the estate tax, as well as the revenue it raises. It would also reduce returns to saving, encouraging consumption during a taxpayer's lifetime rather than saving.

Domestic saving would fall, and foreign investment into the US would increase, causing more of the returns to American investment to flow to foreigners. The smaller budget deficit would reduce federal government borrowing and interest payments to foreigners, offsetting some of the decline in domestic saving, but this option would still result in a decrease in GNP. These estimates do not account for the increased compliance burden that would result from this option.

On a conventional basis, this option would decrease the primary deficit by $1,106.5 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would fall by 0.1 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 166.1 percent by 2056.

On average, taxpayers would see decreases in their after-tax incomes of 0.6 percent in 2036 and the long run, concentrated within the top quintile.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$1,106.5B	-$1,106.5B
Total Deficit Change	-$1,329.7B	-$1,329.7B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	118.0%	118.0%
CY 2056	175.9%	166.1%	166.1%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.9%	-<0.05%	-0.0%	-0.2%	-1.9%	-4.8%	**-0.6%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-1.0%	-<0.05%	-0.0%	-0.2%	-2.2%	-5.7%	**-0.6%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	-1.0%	-<0.05%	-0.0%	-0.2%	-2.2%	-5.7%	**-0.6%**

86. Replace the Estate Tax with Capital Gains Taxation at Death

LONG-RUN ECONOMIC EFFECTS

Gross Domestic Product	Gross National Product	Capital Stock	Pre-Tax Wage Rate	Full-Time Equiv. Jobs
0.0%	**-0.1%**	**0.0%**	**0.0%**	**0**

The estate tax applies to estates above a $15 million ($30 million for joint filers) exemption threshold at a top rate of 40 percent. At the same time, the tax basis of property transferred to an heir at death is "stepped up" to its current market value, such that only the asset appreciation after the inheritance faces capital gains tax.

Step-up in basis ensures that when an asset is passed to an heir, the value of the asset is not subject to both the estate tax and the capital gains tax. Step-up in basis has been critiqued for discouraging taxpayers from realizing capital gains, and for benefiting high-income taxpayers, allowing some capital gains to fully escape taxation.

This option replaces the estate tax and step-up in basis treatment of capital gains at death with a tax on the transfer of capital gains at death. This would increase the overall tax burden on saving, which would reduce the incentive to save. Domestic saving would fall, and foreign investment into the US would increase, causing more of the returns to American investment to flow to foreigners. The smaller budget deficit would reduce federal government borrowing and interest payments to foreigners, with the fall in domestic saving dominating, resulting in a decline in GNP. These estimates do not account for any changes in compliance costs.

On a conventional basis, this option would decrease the primary deficit by $231.2 billion over the budget window. Long-run GDP would be unchanged, while long-run GNP would decline by 0.1 percent. Incorporating changes in interest costs, the publicly held debt-to-GDP ratio would be lower than baseline, reaching 174.5 percent by 2056.

On average, taxpayers would see decreases in their after-tax incomes of 0.1 percent in 2036 and the long run, concentrated among taxpayers in the top 1 percent.

10-YEAR CHANGE IN THE DEFICIT, 2027-2036

	Conventional	Dynamic
Primary Deficit Change	-$231.2B	-$231.2B
Total Deficit Change	-$286.8B	-$286.8B

A negative number is a decrease in the deficit

CHANGE IN THE PUBLICLY HELD DEBT-TO-GDP RATIO

	Baseline	Conventional	Dynamic
CY 2036	120.8%	120.2%	120.2%
CY 2056	175.9%	174.5%	174.5%

DISTRIBUTIONAL EFFECTS: PERCENT CHANGE IN AFTER-TAX INCOME

	0% - 20.0%	20.0% - 40.0%	40.0% - 60.0%	60.0% - 80.0%	80.0% - 100%	80.0% - 90.0%	90.0% - 95.0%	95.0% - 99.0%	99.0% - 99.9%	99.9% - 100%	Total
Conventional, 2027	0.0%	0.0%	0.0%	0.0%	-0.3%	0.0%	0.0%	-0.2%	0.0%	-1.8%	**-0.2%**
Conventional, 2036	0.0%	0.0%	0.0%	0.0%	-0.1%	0.0%	0.0%	-0.1%	+0.5%	-1.2%	**-0.1%**
Dynamic, Long-Run	0.0%	0.0%	0.0%	0.0%	-0.1%	0.0%	0.0%	-0.1%	+0.5%	-1.2%	**-0.1%**

About the Tax Foundation

The Tax Foundation is the nation's leading independent tax policy research organization. Since 1937, our research, analysis, and experts have informed smarter tax policy at the federal, state, and global levels. Our Center for Federal Tax Policy's research and outreach highlight our tax code's strengths and weaknesses and show how tax policy impacts taxpayers, the government, and the economy at large.

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The One Big Beautiful Bill Act (OBBBA) of 2025 made many expiring parts of the federal tax code permanent. But tax reform is far from over.

Over the next decade, one of the most consequential questions facing policymakers will be how tax policy can help address the United States' unsustainable fiscal trajectory. Whether the goal is to raise or reduce taxes, policymakers must consider how each change would affect not only federal revenue, but also the US economy at large.

Our team of economists has modeled more than 80 tax options, estimating their impact on the economy, federal revenue, and the distribution of the tax burden. With the analysis in this guide, policymakers can compare the trade-offs of each option and make informed choices to improve the tax code and put US fiscal policy on a more sustainable course.

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