



Tax Policy Center
Urban Institute and Brookings Institution

An Updated Analysis is available
http://www.taxpolicycenter.org/taxtopics/presidential_candidates.cfm

**A Preliminary Analysis of the 2008
Presidential Candidates' Tax Plans**
Summary

Tax and fiscal policy will loom large in the next president's domestic policy agenda. The scheduled expiration of most of the Bush tax cuts in 2011, the expanding impact of the alternative minimum tax (AMT), and large projected increases in spending on Social Security, Medicare, and Medicaid will all demand attention early in the new administration. Both presidential candidates have proposed major changes to the nation's tax laws that would reduce federal revenues and shift in markedly different ways the burden of taxes among households. This paper analyzes the proposals as we understand them based on speeches, campaign websites, and conversations with campaign staff. In some cases, our description is at variance with candidates' public statements (notably in the case of the AMT), but our description is consistent with what we have been able to learn from the campaigns. This analysis excludes the effect of the candidates' health proposals, but that will be included in a future report.

The candidates' tax plans head in sharply different directions. Senator McCain would permanently extend the 2001 and 2003 tax cuts, increase deductions for taxpayers supporting dependents, reduce the corporate income tax rate, and allow immediate deductions for the cost of certain short-lived capital equipment (summary table 1). Senator Obama would also make most provisions of the recent tax cuts permanent, but only for taxpayers with incomes under \$250,000. He would also raise the maximum rate on capital gains and provide new or expanded targeted tax breaks for workers, retirees, homeowners, savers, students, and new farmers. Both candidates would retain the AMT but continue the "patch" that has protected most individuals and families from the tax in recent years. Both candidates would also increase the estate tax exemption and reduce the estate tax rate compared with scheduled values after 2010, but Senator McCain would cut the tax rate and increase the exemption much more than Senator Obama. Finally, both candidates promise to recoup at least some of their tax cuts by broadening the tax base and

reducing corporate loopholes, although again, their specific proposals differ substantially from each other and both claim revenues from unspecified loophole closers.

Summary Table 1
Summary of the Major Provisions of the McCain and Obama Tax Plans

	John McCain	Barack Obama
2001/2003 Tax Cuts	Make permanent all provisions other than estate tax repeal	Make permanent select provisions, including child credit expansions; 10, 15, 25, and 28 percent rates; changes to tax implications of marriage
Estate Tax	Make permanent estate tax with \$5 million exemption and 15 percent rate	Make permanent estate tax with \$3.5 million exemption and 45 percent rate
AMT	Extend and index 2007 AMT patch, further increase exemption by 5 percent in excess of inflation after 2013 (temporarily)	Extend and index 2007 AMT patch
New Tax Cuts	<p>Increase the dependent exemption by two-thirds (phased in)</p> <p>Reduce the maximum corporate income tax rate from 35 percent to 25 percent (phased in)</p> <p>Allow first-year deduction of 3- and 5-year equipment, deny interest deduction (expires)</p> <p>Convert R&D credit to 10 percent of wages incurred for R&D, make permanent</p> <p>Suspend federal gas tax for summer 2008</p>	<p>Refundable "Making Work Pay Credit" of 6.2 percent of up to a maximum of \$8,100 of earnings</p> <p>Refundable "Universal Mortgage Credit" of 10 percent percent of mortgage interest for nonitemizers</p> <p>Eliminate income tax for seniors making less than \$50,000 per year</p> <p>Extend childless EITC phase-in range, increase phase-out threshold</p> <p>Increase EITC phase-in rate to 45 percent for families with three or more children</p> <p>Increase to \$5,000 the add-on to EITC phase-out threshold for married filers</p> <p>Make CDCTC refundable and increase maximum credit rate to 50 percent.</p> <p>Make saver's credit refundable and change formula to 50 percent match up to \$1,000 of contributions</p> <p>Make permanent R&D credit and renewable energy production tax credit</p> <p>Mandate automatic 401(k)s and automatic IRAs</p> <p>Increase Hope credit: 100% match rate on up to \$4,000</p>
Health	Replace exclusion from income for employer sponsored insurance with refundable credit of \$2,500 for individuals and \$5,000 for families	Income-related subsidies for health insurance
Tax Increases	<p>Repeal domestic production activities deduction</p> <p>Eliminate oil and gas loopholes</p> <p>Unspecified corporate base broadeners</p>	<p>Increase maximum capital gains rate to 25 percent</p> <p>Tax carried interest as ordinary income</p> <p>Eliminate oil and gas loopholes</p> <p>Tax publicly traded financial parts. as C corps.</p> <p>Codify economic substance doctrine</p> <p>Reallocate multinational tax deductions</p> <p>Require information reporting of basis for gains</p>
Simplification	Create optional alternative tax with two rates and larger standard deduction and personal exemption	Provide taxpayers with simple returns the option of pre-filled tax forms to verify and sign.

Effect of Revenues and the Debt

Both candidates have stressed fiscal responsibility, but their specific non-health tax proposals would reduce tax revenues by \$3.6 trillion (McCain) and \$2.7 trillion (Obama) over the next 10 years compared with current law (summary table 2). Including interest, the tax cuts would increase the national debt by \$4.3 trillion (McCain) or \$3.3 trillion (Obama) by the end of 2018.

The campaigns point out that the net effect of their plans on the budget could be much smaller, but it could also be larger. On the one hand, McCain and Obama both say that they will reduce spending by eliminating earmarks and improving government efficiency. Obama says that he will save money by ending the war in Iraq (although it should be noted that most of the cost of the war is not in the baseline). McCain counters that Senator Obama's health proposals could be very expensive.

On the other hand, there is a lot of uncertainty about the true cost of the candidates' tax proposals. Phase-ins and sunsets (scheduled expiration dates) mask the true cost of McCain's policies: if his policies were immediately and permanently in place, the ten-year cost would jump more than 10 percent to \$4.0 trillion. And both candidates may be overoptimistic in their revenue targets for closing tax loopholes—Obama probably more than McCain.

The candidates argue that their proposals should be scored against a “current policy” baseline instead of current law. That alternative baseline assumes permanent extension of both the 2001 and 2003 tax cuts and the AMT patch, which together would cut projected tax revenue over the next decade by \$3 trillion. Against such a baseline, Senator Obama's proposals would raise \$300 billion and Senator McCain's proposals would lose \$600 billion (assuming they phase in and out as scheduled).

Summary Table 2
Revenue Effect of Candidates' Tax Plans
Impact on Tax Revenue, 2009-2018

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total 2009-2018
Change in Tax Revenue Against Current Law (billions of dollars)											
McCain	-42	-119	-248	-373	-386	-394	-450	-492	-532	-573	-3,610
Obama	-14	-83	-187	-290	-311	-329	-347	-368	-390	-414	-2,733
Change in Tax Revenue Against Current Policy (billions of dollars)											
McCain	-19	-58	-35	-56	-48	-34	-68	-86	-99	-112	-615
Obama	9	-22	26	28	27	31	34	38	43	47	262
Revenues Collected (percent of GDP)											
McCain	18.6	17.9	17.9	17.9	17.8	17.9	17.7	17.7	17.7	17.8	17.9
Obama	18.8	18.2	18.3	18.4	18.2	18.2	18.3	18.3	18.4	18.5	18.4
Baseline Revenues (percent of GDP)											
Current Law	18.9	18.7	19.4	20.0	19.9	20.0	20.0	20.1	20.2	20.3	19.8
Current Policy	18.8	18.3	18.1	18.2	18.0	18.1	18.1	18.1	18.2	18.3	18.2

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0308-5), various JCT scores, the fiscal year 2009 Treasury blue book, and CBO's most recent budget projections.

For more detailed tables, see
<http://www.taxpolicycenter.org/numbers/displayatab.cfm?template=simulation&SimID=266>

Effect on Distribution of Tax Burdens

The Obama and McCain tax plans would have radically different effects on the distribution of tax burdens. The Obama tax plan would make the tax system significantly more progressive by providing large tax breaks to those at the bottom of the income scale and raising taxes significantly on upper-income earners. His proposals would raise after-tax incomes (cut taxes) in 2009 for those in the bottom quintile by more than 5.5 percent and raise them by somewhat less for those in the next three quintiles, while reducing after-tax income (increasing taxes) by an average of 2.0 percent for those in the top quintile and nearly 9 percent for those in the top 1 percent (summary table 3). In marked contrast, the McCain tax plan would make the tax system more regressive—even compared with a system in which the 2001–06 tax cuts are made permanent—because it would give huge tax cuts to households at the very top of the income distribution but little tax relief to those at the bottom of the income scale. McCain’s tax proposals would raise after-tax income for households in the lowest income quintile by only 0.2 percent in 2009, while raising after-tax incomes for households in the top quintile by 3.0 percent on average.

Summary Table 3
Effects of Candidates' Tax Proposals on After-Tax Income, 2009 and 2012
Percentage Change in After-Tax Income by Cash Income Percentile

Cash Income Percentile	McCain Tax Proposals		Obama Tax Proposals	
	2009	2012	2009	2012
Lowest Quintile	0.2	0.9	5.5	6.2
Second Quintile	0.5	2.8	3.6	5.9
Middle Quintile	0.7	3.1	2.4	4.6
Fourth Quintile	1.4	4.1	1.8	4.4
Top Quintile	3.0	6.4	-2.0	1.5
All	2.0	4.9	0.3	3.2
Addendum				
80-90	2.5	4.8	2.1	4.4
90-95	3.0	4.8	1.9	3.8
95-99	3.1	5.3	0.0	2.3
Top 1 Percent	3.4	9.5	-8.7	-2.9
Top 0.1 Percent	4.4	11.6	-11.5	-5.1

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0308-5).

For more detailed tables, see

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Effects on the Economy

The two candidates' proposals to change the tax code would affect economic activity differently in several important ways. Senator McCain proposes lower top marginal rates (35 percent on individual income and 25 percent on corporate income) than Senator Obama (39.6 and 35 percent, respectively). Those lower tax rates could improve economic efficiency and increase domestic investment, but, absent offsetting cuts in spending, would create larger future deficits that would reduce and possibly fully offset any positive effect. In contrast, Senator Obama proposes new payroll tax credits and an expanded EITC for childless workers that could encourage more low-income people, especially those without children, to work. However, his plan would also reduce taxes for many seniors (an already favored group) and subsidize borrowing for housing (which already gets favorable tax treatment); alternative revenue cuts could be more effective in encouraging work, saving, and a productive allocation of capital investment. And, as with Senator McCain's plan, Senator Obama's tax proposals would raise deficits, relative to current law.

Proposals Not Studied

Both candidates have proposed other initiatives but with too little detail for us to analyze them. For example, Senator McCain would replace the current exclusion of employer-paid health insurance premiums with a limited refundable credit for anyone who obtains qualified health insurance and would also expand the availability of health savings accounts. Senator Obama has proposed to expand health insurance coverage following the Massachusetts model with a portable national insurance plan, mandatory coverage for children, required contributions from employers who do not help their employees get health coverage, and other features.

Obama has repeatedly talked of raising payroll taxes to pay for Social Security but his campaign insists that there is no concrete proposal that we could model. McCain has called for repeal of the AMT but his campaign says he would only phase out the tax and the plan they offer would only phase it down and not out. And McCain has proposed giving taxpayers the option of electing a simpler tax with virtually no deductions or exemptions and just two rates—and which would neither gain nor lose revenue—but has provided none of the detail needed to model such a plan. We plan to examine health care and the non-proposals in our next analysis of the candidates' plans. (If the candidates do not clarify the proposals, we will speculate about what the candidates might mean and how that could affect our conclusions.)