TAX FOUNDATION
Since 1937

FISCAL FACT
No. 698
Mar. 2020

Analysis of Democratic Presidential Candidate Individual Income Tax Proposals

Erica York
Economist

Garrett Watson
Senior Policy Analyst

Key Findings

- The major 2020 Democratic presidential candidates have each proposed changes to the individual income tax, one of the largest sources of federal revenue. These proposals range from raising the top marginal income tax rate to 39.6 percent, imposing surtaxes on labor and investment income, and repealing provisions of the Tax Cuts and Jobs Act (TCJA).

- Former Vice President Joe Biden's proposal would reverse the TCJA top marginal rate cut from 37 percent back up to 39.6 percent. This change would not have a long-run effect because this tax cut is already scheduled to expire after 2025, and as such, Biden's proposal is not a change to long-run policy.

- Senator Bernie Sanders (I-VT) proposes a new top marginal rate of 52 percent on incomes above $10 million, a 4 percent tax on all households, and repeal of the Section 199A pass-through deduction. This would change long-run policy and would reduce after-tax incomes of taxpayers, lowering the return to labor and increasing the cost of capital for pass-through businesses. This reduces economic output, wages, and employment in the long run.

	Biden	Sanders
Plan Details	Raise 37% tax bracket rate to 39.6%	Impose a 52% tax rate on incomes over $10 million, impose a 4% income-based premium on all income, repeal the Section 199A pass-through deduction
Conventional Revenue, 2020-2029 (Billions of Dollars)	$109.0	$3,168.4
Dynamic Revenue, 2020-2029 (Billions of Dollars)	$84.0	$2,169.5
Gross Domestic Product (GDP)	0%	-2.04%
Capital Stock	0%	-2.54%
Full-time Equivalent Jobs	0	-1,532,000

Source: Tax Foundation General Equilibrium Model, November 2019

Editor, Rachel Shuster
Designer, Dan Carvajal

Tax Foundation
1325 G Street, NW, Suite 950
Washington, DC 20005

202.464.6200

taxfoundation.org

Introduction

Changes to individual income tax rates and the individual income tax base are a major component of the major Democratic presidential candidate tax plans. Much of the tax policy debates have centered on repealing elements of the Tax Cuts and Jobs Act (TCJA) of 2017, including reverting the top marginal income tax rate to its pre-TCJA level.

The major Democratic presidential candidates have also proposed additional income taxes to increase federal revenue and support additional spending priorities. For example, Sen. Bernie Sanders (I-VT) would impose a 4 percent income tax across all income levels to help pay for his Medicare for All proposal.

Given the large role the individual income tax plays in federal revenue and economic decision-making, it is important to understand the economic and revenue effects of these proposals. This paper reviews individual income tax proposals from the two major Democratic candidates, with detailed plans for changing taxes on individual income. Using the Tax Foundation General Equilibrium Model, we estimate the economic, revenue, and distributional effects of each tax policy proposal.

Note that we also include the plan of a former candidate, former New York City Mayor Michael Bloomberg, as it represents policy options that might be considered going forward.

Structure of the Individual Income Tax

The individual income tax is the largest source of revenue for the federal government, comprising about 49.6 percent of federal revenue and about 8.1 percent of Gross Domestic Product (GDP) in fiscal year (FY) 2019.[1] About 76 percent of individuals' gross income comes from salaries and wages, while a smaller portion comes from business income taxed on individual tax returns.[2]

The individual income tax is a graduated rate system and a progressive source of revenue, starting at a marginal tax rate 10 percent for taxable income between $0 and $19,750 (filing jointly) and rising to a top marginal tax rate of 37 percent for income above $622,050 (filing jointly). These income tax rates were lowered through the TCJA of 2017, which reduced marginal tax rates across the income spectrum.[3]

1 Congressional Budget Office, "The Budget and Economic Outlook: 2020 to 2030," Jan. 28, 2020, 7, https://cbo.gov/publication/56020.

2 Congressional Research Service, "Overview of the Federal Tax System in 2019," Nov. 20, 2019, 1-2, https://fas.org/sgp/crs/misc/R45145.pdf.

3 Scott Eastman, "The TCJA Lowered Taxes for Individuals Throughout Income Groups," Tax Foundation, Mar. 26, 2019, https://taxfoundation.org/tcja-lowered-taxes-individuals-throughout-income-groups/.

TABLE 1.

Individual Income Tax Brackets and Rates Under Current Law, Tax Year 2020

Rate	For Single Individuals, Taxable Income Over	For Married Individuals Filing Joint Returns, Taxable Income Over	For Heads of Households, Taxable Income Over
10%	$0	$0	$0
12%	$9,875	$19,750	$14,100
22%	$40,125	$80,250	$53,700
24%	$85,525	$171,050	$85,500
32%	$163,300	$326,600	$163,300
35%	$207,350	$414,700	$207,350
37%	$518,400	$622,050	$518,400

Source: Internal Revenue Service

Taxpayers may take "above-the-line" deductions when calculating their adjusted gross income (AGI), which includes teacher expenses, tuition and fees, and others, subject to certain qualifications and limitations. The individual income tax provides taxpayers the option to itemize their deductions when calculating their taxable income or use the standard deduction of $24,800 in tax year 2020 (filing jointly) in lieu of itemized deductions.

The individual income tax also includes other adjustments, such as the Section 199A pass-through deduction. Enacted as part of the TCJA, the pass-through deduction permits a 20 percent deduction for qualified pass-through business income, lowering the effective tax rate that pass-through business income faces for the individual income tax.[4]

Former Vice President Biden's Proposal

Biden has proposed raising the top individual income tax rate from 37 percent to 39.6 percent, reverting the top rate to its level before the TCJA. Under current law, the top marginal income tax rate is set to rise to 39.6 percent from 37 percent after December 31, 2025. Biden's proposal simply changes the expiration date of the reduction in the top marginal tax rate.

This proposed change would raise individual income tax rates for taxpayers at the top bracket for tax years 2020 through 2025, after which the proposal would match the tax rate already scheduled to take effect under current law for tax years 2026 through 2029.

4 See generally, Scott Greenberg, "Reforming the Pass-Through Deduction," Tax Foundation, June 21, 2018, https://taxfoundation.org/reforming-pass-through-deduction-199a/.

Economic Effect

According to the Tax Foundation General Equilibrium Model, this proposal would not change economic output (GDP) in the long run. This is because the long-run top marginal tax rate is the same as Biden's proposed rate of 39.6 percent, producing no change in long-run economic output. Put another way, the level of long-run economic output remains the same, despite a shift in the timing of output growth between now and the long run due to the lower tax rate under current law.[5]

TABLE 2.

Economic Effect of Biden's Individual Income Tax Proposal

Gross Domestic Product (GDP)	0.0%
Capital Stock	0.0%
Full-time Equivalent Jobs	0

Source: Tax Foundation General Equilibrium Model, November 2019.

We also estimate that this proposed change would have no effect on the capital stock or the number of full-time equivalent jobs. Similarly, there is no long-run change in after-tax incomes from a distributional perspective.

Revenue Effect

We estimate the Biden proposal would raise $109 billion between 2020 and 2029 on a conventional basis. The proposal raises about $16 and $20 billion per year between 2020 and 2025, then doesn't raise revenue from 2026 to 2029. This is because under current law, the top marginal tax rate is set to rise from 37 percent to 39.6 percent in 2026, yielding no additional revenue from the policy change.

TABLE 3.

Revenue Effect of Biden's Individual Income Tax Proposal (Billions of Dollars)

Year	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2020-2029
Conventional	$16.0	$17.0	$18.0	$19.0	$19.0	$20.0	$0.0	$0.0	$0.0	$0.0	$109.0
Dynamic	$13.0	$13.0	$14.0	$14.0	$15.0	$15.0	$0.0	$0.0	$0.0	$0.0	$84.0

Source: Tax Foundation General Equilibrium Model, November 2019. Values may not add to total due to rounding.

On a dynamic basis, the proposal would raise about $84 billion between 2020 and 2029. Revenue collections are smaller on a dynamic basis due to lower output as a result of the tax between 2020 and 2025.

5 For more on the long-run economic effects of provisions within the TCJA, see "Preliminary Details and Analysis of the Tax Cuts and Jobs Act," Tax Foundation, Dec. 18, 2017, https://taxfoundation.org/final-tax-cuts-and-jobs-act-details-analysis/.

Sen. Sanders' Proposal

Sanders has proposed a new top marginal rate of 52 percent on incomes above $10 million (we assume $5 million for single filers and adjust both amounts for inflation) and a 4 percent income-based premium on households. These two changes would result in a top marginal tax rate of 56 percent on incomes above $10 million.

Sanders has also proposed repealing the Section 199A pass-through deduction, which provides a 20 percent deduction for qualified pass-through business income.[6]

Note that when the individual income tax cuts that were included in the TCJA expire after 2025, Sanders' 4 percent income-based premium would apply to higher marginal tax rates than at the beginning of the budget window, when the TCJA tax cuts are still in effect.

Economic Effect

According to the Tax Foundation General Equilibrium Model, Sanders' proposal would reduce economic output (GDP) by 2.04 percent. The capital stock would fall by 2.54 percent, wages by 0.41 percent, and employment by more than 1.5 million full-time equivalent jobs. These changes are driven by the new top marginal rate and the 4 percent tax. The Section 199A pass-through deduction is set to expire at the end of 2025 and changing the expiration date does not produce long-run economic effects.

TABLE 4.

Economic Effect of Sanders' Individual Income Tax Proposal

Gross Domestic Product	-2.04%
Capital Stock	-2.54%
Wage Rate	-0.41%
Full-time Equivalent Jobs	-1,532,000

Source: Tax Foundation General Equilibrium Model, November 2019

Revenue Effect

We estimate that Sanders' proposal would raise nearly $3.2 trillion between 2020 and 2029. In years 2020 to 2025, repeal of the Section 199A pass-through deduction raises revenue, but in years 2026 to 2029, the provision is already scheduled to expire under current law, so the change does not raise revenue after 2025. Revenue raised after 2025 comes from the higher top marginal rate and the 4 percent tax. Due to the expiration of the TCJA tax cuts after 2025, Sanders' income tax increases apply to higher marginal tax rates at the end of the budget window than at the beginning.

On a dynamic basis, we estimate the Sanders' proposal would raise about 30 percent less revenue than on a conventional basis. Revenue collections would total approximately $2.2 trillion from 2020 to 2029, as output would be lower as a result of the tax increases.

6 Sanders also states that he would require large pass-through businesses to be subject to corporate taxes. We do not include this change in our analysis.

TABLE 5.

Revenue Effect of Sanders' Individual Income Tax Proposal (Billions of Dollars)

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2020 - 2029
Conventional	$366.2	$366.9	$366.4	$364.5	$362.2	$359.2	$248.2	$246.5	$245.0	$243.5	$3,168.4
Dynamic	$272.7	$268.9	$266.2	$261.0	$255.5	$249.7	$152.6	$150.6	$147.4	$144.9	$2,169.5

Source: Tax Foundation General Equilibrium Model, November 2019

Distributional Effect

The combined effect of the proposals would increase the progressivity of the tax code, primarily due to the new top marginal rate on high-income earners. Overall, Sanders' proposal would reduce after-tax income of all taxpayers by 2.65 percent, on average.

On a conventional basis, after-tax incomes of the middle quintile would fall by 1.53 percent and the top 1 percent would fall by 6.65 percent.

TABLE 6.

Conventional Distributional Effect of Sanders' Individual Income Tax Proposal (Percent-Change in After-Tax Income)

Income Group	Conventional
0% to 20%	-0.05%
20% to 40%	-0.48%
40% to 60%	-1.53%
60% to 80%	-1.79%
80% to 90%	-2.32%
90% to 95%	-2.26%
95% to 99%	-1.76%
99% to 100%	-6.65%
Total	-2.65%

Source: Tax Foundation General Equilibrium Model, November 2019.

Additional Analysis

While former Mayor Bloomberg is no longer running in the Democratic presidential primaries, we have included an analysis of his proposal as it represents other ideas that might someday return to public discussion. Bloomberg proposed raising the top individual income tax rate from 37 percent to 39.6 percent and repealing the Section 199A pass-through deduction. Both these TCJA provisions are scheduled to expire after December 31, 2025, under current law.

Additionally, his plan would assess a 5 percent surtax on income earned above $5 million.[7] This surtax would be applied on both labor and investment income, raise the top marginal income tax rate to 44.6

7 Erica York, "Overview of Democratic Presidential Candidate Michael Bloomberg's Tax Plan," Tax Foundation, Feb. 7, 2020, https://taxfoundation.org/michael-bloomberg-tax-plan/.

percent on wage income, and raise the top tax rate on investment income to 28.8 percent, including the 3.8 percent Net Investment Income Tax (NIIT) under the current law treatment of qualified capital gains and dividends.

Economic Effect

According to the Tax Foundation General Equilibrium Model, this proposal would reduce economic output (GDP) by 0.59 percent in the long run. We estimate that wealth owned by Americans in the United States would be 1.4 percent smaller. The proposal would lead to about 204,000 fewer full-time equivalent jobs.

TABLE 7.

Economic Effect of Bloomberg's Individual Income Tax Proposal

Gross Domestic Product (GDP)	-0.59%
Gross National Product (GNP)	-0.67%
Capital Stock	-1.0%
Wealth	-1.4%
Full-time Equivalent Jobs	-204,000

Source: Tax Foundation General Equilibrium Model, November 2019.

The long-run economic effect of this proposal is driven by the 5 percent surtax on labor and investment income over $10 million. The Section 199A pass-through deduction and the 37 percent top marginal income tax rate are set to expire at the end of 2025, and changing the expiration date does not produce long-run economic effects. By contrast, a new 5 percent surtax on labor and investment income over $5 million for those married filing jointly ($2.5 million for single filers) would reduce the return to labor, lowering hours worked and economic output.

The 5 percent surtax on investment income would reduce investment by Americans domestically, though this reduction would be mostly offset by greater investment from abroad. The difference between GDP (0.59 percent decrease) and GNP (0.67 percent decrease) shows the increase in the level of foreign investment that offsets a decline in domestic investment.

Pass-through businesses would still experience a negative long-run effect, however, because they are not as open to foreign investment as C corporations. This is what produces a lower level of long-run GDP in combination with a decrease in hours worked. Wealth owned by Americans would also fall, as the 5 percent tax on investment increases the incentive to consume on the margin.

Revenue Effect

We estimate the Bloomberg proposal would raise about $402.6 billion between 2020 and 2029 on a conventional basis. Most of the revenue comes from the repeal of the Section 199A pass-through deduction and raising the (current) top marginal tax rate to 39.6 percent in years 2020 to 2025. After 2025, the top marginal rate is set to increase and the Section 199A deduction is set to expire under current law.

Revenue raised after 2025 comes from the 5 percent surtax on labor and investment income over $5 million. Additionally, the increase in the tax rate on investment income reduces capital gains realizations as taxpayers attempt to avoid the tax, reducing expected revenue.

TABLE 8.

Revenue Effect of Bloomberg's Individual Income Tax Proposal (Billions of Dollars)

Year	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2020-2029
Conventional	$63.9	$63.8	$63.6	$63.1	$62.2	$61.3	$5.9	$6.1	$6.3	$6.6	$402.6
Dynamic	$50.0	$42.8	$39.1	$38.5	$34.0	$26.0	-$25.3	-$24.9	-$21.2	-$18.1	$140.9

Source: Tax Foundation General Equilibrium Model, November 2019. Values may not add to total due to rounding.

On a dynamic basis, the proposal would raise about $140.9 billion between 2020 and 2029. Revenue collections are smaller on a dynamic basis due to lower individual income tax and payroll tax revenue resulting from a smaller economy. From 2026 to 2029, revenue collections turn negative when combining lower income and payroll tax revenue, a decrease in capital gains realizations, and expiring tax provisions related to TCJA.

Distributional Effect

The Tax Foundation General Equilibrium Model estimates that taxpayers would experience a 0.06 percent fall in after-tax income on average. Bloomberg's proposal would make the tax code more progressive. Taxpayers below the 95th percentile would see no change in after-tax income on a conventional basis, while taxpayers above the 99th percentile would experience a 0.87 percent decrease in after-tax income.

TABLE 9.

Conventional Distributional Effect of Bloomberg's Proposal (Percent Change in After-Tax Income)

Income Group	Conventional
0% to 20%	0%
20% to 40%	0%
40% to 60%	0%
60% to 80%	0%
80% to 90%	0%
90% to 95%	0%
95% to 99%	-0.01%
99% to 100%	-0.87%
Total	-0.06%

Source: Tax Foundation General Equilibrium Model, November 2019.

Modeling Notes and Policy Assumptions

We use the Tax Foundation General Equilibrium Tax Model to estimate the impact of tax policies.[8] The model can produce both conventional and dynamic revenue estimates of tax policy. Conventional estimates hold the size of the economy constant and attempt to estimate potential behavioral effects of tax policy. Dynamic revenue estimates consider both behavioral and macroeconomic effects of tax policy on revenue.

The model can also produce estimates of how policies impact measures of economic performance such as GDP, wages, employment, the capital stock, investment, consumption, saving, and the trade deficit. Lastly, it can produce estimates of how different tax policy impacts the distribution of the federal tax burden.

This analysis is based on details released by each presidential candidate and their advisors. Ultimately, the impact of each proposal depends on its final details and whether it is applied in combination with other policies that may create interaction effects.

Revenue estimates were calculated by estimating the percentage change in federal revenue by revenue source (such as income tax revenue and payroll tax revenue) and applying this change over the latest CBO baseline projections over the 2020-2029 budget window.

8 Stephen J. Entin, Huaqun Li, and Kyle Pomerleau, "Overview of the Tax Foundation's General Equilibrium Model," Tax Foundation, April 2018 Update, https://files.taxfoundation.org/20180419195810/TaxFoundaton_General-Equilibrium-Model-Overview1.pdf.