TAX FOUNDATION Since 1937
FISCAL FACT
Sept. 2015
No. 482

Details and Analysis of Donald Trump's Tax Plan

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Key Findings

- Mr. Trump's tax plan would substantially lower individual income taxes and the corporate income tax and eliminate a number of complex features in the current tax code.
- Mr. Trump's plan would cut taxes by $11.98 trillion over the next decade on a static basis. However, the plan would end up reducing tax revenues by $10.14 trillion over the next decade when accounting for economic growth from increases in the supply of labor and capital.
- The plan would also result in increased outlays due to higher interest on the debt, creating a ten-year deficit somewhat larger than the estimates above.
- According to the Tax Foundation's Taxes and Growth Model, the plan would significantly reduce marginal tax rates and the cost of capital, which would lead to an 11 percent higher GDP over the long term provided that the tax cut could be appropriately financed.
- The plan would also lead to a 29 percent larger capital stock, 6.5 percent higher wages, and 5.3 million more full-time equivalent jobs.
- The plan would cut taxes and lead to higher after-tax incomes for taxpayers at all levels of income.

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Yesterday, Donald J. Trump released details of a tax reform plan.[1] This plan would reduce individual income tax rates, lowering the top rate from 39.6 percent to 25 percent and creating a large zero bracket. The plan would also reform the business tax code by reducing the income tax on all businesses to 15 percent and eliminate business tax expenditures, including deferral and interest deductions. In addition, the plan would eliminate the Estate Tax and the Alternative Minimum Tax.

While some aspects of the plan remain unspecified, many others are very clear, working within the existing income tax framework and lowering the rates. As such, we are able to model virtually all of the major provisions of the plan.

Our analysis finds that the plan would reduce federal revenues by $11.98 trillion over the next decade. However, it also would improve incentives to work and invest, which could increase gross domestic product (GDP) by 11 percent over the long term. This increase in GDP would translate into 6.5 percent higher wages and 5.3 million new full-time equivalent jobs. After accounting for increased incomes due to these factors, the plan would only reduce tax revenues by $10.14 trillion.[2]

Details of the Plan

Individual Income Tax Changes

- Consolidates the current seven tax brackets into four, with a top marginal income tax rate of 25 percent (Table 1).
- Taxes long-term capital gains and qualified dividends at a top marginal rate of 20 percent.
- Creates a substantial zero bracket for lower income individuals.

Table 1.
Individual Income Tax Brackets Under Donald Trump's Tax Plan

Ordinary Income	Capital Gains and Dividends	Single Filers	Married Filers	Head of Household
0%	0%	$0 to $25,000	$0 to $50,000	$0 to $37,500
10%	0%	$25,000 to $50,000	$50,000 to $100,000	$37,500 to $75,000
20%	15%	$50,000 to $150,000	$100,000 to $300,000	$75,000 to $225,000
25%	20%	$150,000 and up	$300,000 and up	$225,000 and up

1 "TAX REFORM THAT WILL MAKE AMERICA GREAT AGAIN," Sep. 28, 2015, https://www.donaldjtrump.com/positions/tax-reform.

2 For a reduction in revenues of this size, it is also likely appropriate to consider the macroeconomic effects that the Taxes and Growth model does not predict. Among these are the fiscal costs of higher interest payments, or the macroeconomic effects of the spending reductions needed to bring the budget into balance.

- Steepens the curve of the Personal Exemption Phase-out (PEP) and the Pease Limitation on itemized deductions.
- Eliminates the Alternative Minimum Tax.
- Eliminates the Net Investment Income Tax of 3.8 percent, which was passed as part of the Affordable Care Act.
- Taxes carried interest at ordinary income tax rates instead of capital gains and dividends tax rates.
- Phases out the tax exemption on life insurance interest.

Business Tax Changes

- Cuts the corporate income tax rate from the current 35 percent to 15 percent.
- Ends the deferral of income from controlled foreign subsidiaries, but preserves the foreign tax credit. It would also enact, as a transitional revenue raiser, a one-time deemed repatriation tax of 10 percent on all foreign profits currently deferred.
- Taxes pass-through businesses at the rate of 15 percent commensurate with the traditional corporations.
- Caps the deductibility of interest expenses.

Other Changes

- Eliminates the Estate Tax.

Economic Impact

According to our Taxes and Growth Model, the increased incentives to work and invest from this tax plan would increase the size of the economy by 11 percent over the long run. The plan would lead to 6.5 percent higher wages and a 29 percent larger capital stock. The larger economy is mainly the result of the significant reduction in the service price of capital due to the rate reductions for corporations and pass through businesses. In addition, the reduction of marginal tax rates on individual income would increase incentives to work and result in 5.3 million full-time equivalent jobs.

Table 2.
Economic Impact of Donald Trump's Tax Reform Plan

GDP	11.5%
Capital Investment	29.0%
Wage Rate	6.5%
Full-time Equivalent Jobs (in thousands)	5,329

Source: Tax Foundation Taxes and Growth Model, Sept. 2015.

Revenue Impact

Overall, the plan would reduce federal revenue on a static basis by $11.98 trillion over the next ten years. Most of the revenue loss is due to the reduction in individual income tax rates, which we project to reduce revenues by approximately $10.20 trillion over the next decade. The changes to the corporate income tax will reduce revenues by an additional $1.54 trillion over the next decade, with the remaining static cost ($238 billion) due to the elimination of the estate tax.

However, if we account for the economic growth that the plan would produce, the plan would end up lowering revenue by $10.14 trillion over the next decade. The larger economy would increase wages, which would narrow the revenue lost through the individual income tax by about $666 billion and increase payroll tax revenues by $839 billion, with the remainder of the recouped revenue coming from other taxes.

Table 3.

Ten-Year Revenue Impact of Donald Trump's Tax Reform Plan (Billions of Dollars)

Tax	Static Revenue Impact (2015-2024)	Dynamic Revenue Impact (2015-2024)
Individual Income Taxes	-$10,201	-$9,535
Payroll Taxes	$0	$839
Corporate Income Taxes	-$1,541	-$1,371
Excise Taxes	$0	$69
Estate and Gift Taxes	-$238	-$238
Other Revenue Sources	$0	$101
Total	-$11,980	-$10,135

Source: Tax Foundation Taxes and Growth Model, Sept. 2015.
Note: Individual items may not sum to the total due to rounding.

Distributional Impact

On a static basis, Donald Trump's tax plan would increase the after-tax income across all taxpayers by 10.2 percent, on average, and taxpayers in all income classes would see higher after-tax income.

Taxpayers in the bottom deciles (the 0-10 and 10-20 percent deciles), would see increases in after-tax adjusted gross income (AGI) of 1.4 and 0.6 percent, respectively. Middle-income taxpayers with incomes that fall within the 30th to 80th percentiles would see larger increases in their after-tax AGI, of between 3.0 and 8.3 percent. Taxpayers with incomes that fall in the highest income class (the 90-100 percent decile) would see an increase in after-tax income of 14.6 percent. The top 1 percent of all taxpayers would see a 21.6 percent increase in after-tax income.

On a dynamic basis, the plan would increase after-tax incomes by 20 percent on average. All deciles would see an increase in after-tax AGI of at least 10.6 percent over the long-term. Taxpayers that fall in the bottom three deciles would see their after-tax AGIs increase between 10.6 and 11.5 percent. Middle-income taxpayers in the 30th to 70th percentiles would see increases in their after-tax AGI by as much as 19.7 percent. The top 1 percent of all taxpayers would see an increase in after-tax AGI of 27.0 percent.

Table 4.

Distributional Analysis for Donald Trump's Tax Reform Plan
Effect of Tax Reform on After-Tax Income Compared to Current Law

All Returns by Decile	Static Distributional Analysis	Dynamic Distributional Analysis
0% to 10%	1.4%	10.7%
10% to 20%	0.6%	10.6%
20% to 30%	1.2%	11.5%
30% to 40%	3.0%	14.3%
40% to 50%	5.3%	17.7%
50% to 60%	7.2%	19.5%
60% to 70%	8.0%	19.7%
70% to 80%	8.3%	19.4%
80% to 90%	8.9%	19.5%
90% to 100%	14.6%	22.6%
99% to 100%	21.6%	27.0%
TOTAL FOR ALL	10.2%	20.0%

Source: Tax Foundation Taxes and Growth Model, Sept. 2015.

Conclusion

Donald Trump's tax plan would enact a number of tax reforms that would both lower marginal tax rates on workers and significantly reduce the cost of capital. These changes in the incentives to work and invest would greatly increase the U.S. economy's size in the long run, leading to higher incomes for taxpayers at all income levels. The plan would also be a large tax cut, which would increase the federal government's deficit by over $10 trillion, both on a static and dynamic basis.

Modeling Notes

We modeled the most significant provisions outlined above, and most of the less-significant provisions. The exception to this, generally, is provisions that refer to unspecified closing of loopholes. We also did not model the unspecified changes to the Personal Exemption Phase-out or the Pease Limitation on Itemized Deductions. However, we approximated this by substantially scaling back the value of itemized deductions other than those that Mr. Trump specifically noted he would like to keep. A more aggressive assumption here could have further mitigated the revenue effects of the personal income tax cut. However, neither of the provisions mentioned has nearly the impact of the rate reductions.

We assumed that the standard deduction (which resembles a zero bracket) was folded into the zero bracket proposed by Mr. Trump, rather than adding the zero bracket on top of the standard deduction.

While Mr. Trump did not state specifically which corporate tax expenditures he wanted to eliminate (other than deferral), we approximated this by eliminating those that did not have to do with capital cost recovery. We increased revenues accordingly, though their value was substantially lower under a 15 percent rate than under today's 35 percent rate.

We did not account for profit shifting from abroad due to a lower U.S. corporate income tax rate. An increase in reported income in the U.S. could somewhat mitigate the revenue effects of the corporate rate cut. We also did not model the revenue impact of ending deferral. These are likely to be small in tandem with a corporate tax rate of 15 percent, because the 15 percent is lower than the average corporate tax rate abroad, so foreign tax credits make the additional U.S. tax in that case relatively small.[3]

Finally, it is worth noting that the Taxes and Growth Model does not take into account the fiscal or economic effects of interest on debt. It also does not require budgets to balance over the long term. It also does not account for the potential macroeconomic effects of any spending cuts that may be required to finance the plan.

3 Michael Schuyler and William McBride, *The Economic Effects of the Rubio-Lee Tax Reform Plan*, Tax Foundation Fiscal Fact No. 457, http://taxfoundation.org/article/economic-effects-rubio-lee-tax-reform-plan#_ftnref10.