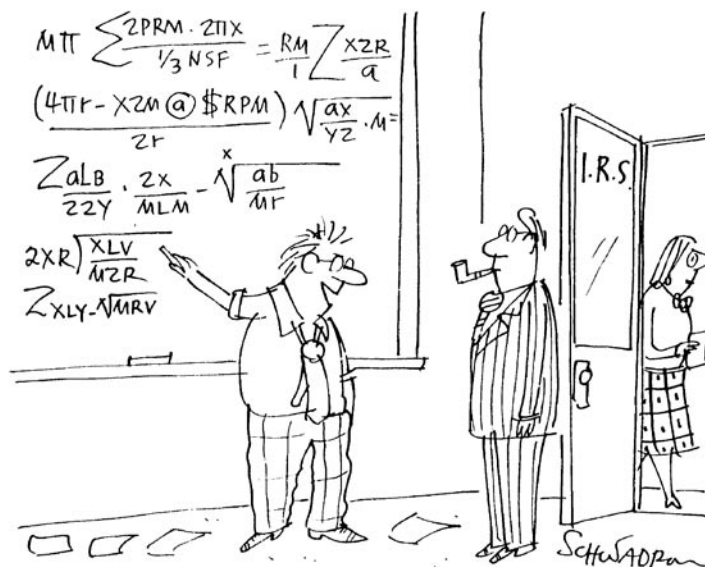


Appendix

Additional Details



"Now are you convinced that the tax simplification plan will work, chief?"

During the course of its work, the Panel examined the current corporate and individual income tax systems and evaluated a variety of proposals for reform. The Panel relied on the help of experts who appeared before the Panel, the Panel staff, the Treasury Department, the Internal Revenue Service, and interested parties who submitted comments.

The Panel had a finite amount of time to develop options, and, therefore, focused its efforts on the goals it hoped to achieve. Although the Panel could not consider every issue or problem, there were several issues for which the Panel developed detailed solutions, these are presented in this Appendix. Much of the discussion is intended to provide background regarding implementation of the Panel's recommendations. The Panel believes that providing this information will aid in understanding its recommendations and will serve as a starting point as policymakers consider changes to the tax code.

This Appendix is not intended to be a comprehensive or systematic discussion of the issues addressed. Moreover, the range of issues addressed in the Appendix is not intended to imply that there are not other important issues. For every issue discussed

here, the Panel discovered that there were many more that could not be thoroughly analyzed in the limited amount of time the Panel had to accomplish its mission.

The Appendix is organized by report chapter. Additional distribution tables for the Simplified Income Tax Plan, the Growth and Investment Tax Plan, and the Progressive Consumption Tax Plan, and sample tax forms appear in the last section of this Appendix.

Chapter Four: Our Starting Point

Details on the Macroeconomic Analysis of the Tax Reform Proposals

The Treasury Department used variants of three standard economic growth models to estimate the dynamic response associated with the Panel's reform options. The use of multiple models reflects both the uncertainty in these types of estimates and provides a reasonable range of results that are consistent with the range of estimates found in the economic literature. These types of models have been used in academic research on the dynamic effects of tax reform and by the staffs of the Joint Committee on Taxation and the Congressional Budget Office.

The three models used by the Treasury Department were a neoclassical growth model, an overlapping generations (OLG) life-cycle model, and a Ramsey growth model. The Treasury Department used the OLG model developed by Tax Policy Advisors, LLC. All three models are supply-side models that emphasize the effects on economic growth of reducing the effective tax rates on capital and labor income. The models ignore demand-side or cyclical variations in the economy, assuming instead that the economy is always at full employment. The neoclassical and Ramsey growth models are closed economy models that ignore international capital flows and foreign trade. The OLG model includes a simple international sector.

The Ramsey growth model, which assumes fixed labor supply, but an infinitely elastic supply of capital at a fixed after-tax required return, yields the smallest growth effects over the ten-year revenue window. This is because it does not account for the labor supply responses that are built into the other models. The intertemporal elasticity of substitution in the Ramsey growth model is smaller (0.25) than that in the overlapping generations model (0.35). The within-period substitution elasticity between labor and goods is greater in the Ramsey model (0.80) than in the overlapping generations model (0.60).

Each of the three models is calibrated to replicate certain economic aggregates using the Administration's policy baseline over the ten-year budget window. The changes to the tax system are assumed to occur simultaneously and without anticipation by households or firms. As households and firms respond to the effect of the tax changes on after-tax wages and interest rates, savings and investment increase, the capital stock increases and individuals change the amount of labor they are willing to supply. These changes occur for many years until eventually the economy returns to the original steady-state growth rate, at a higher level than the previous steady-state

growth path. Before the tax changes are imposed, the economic growth rate equals the combined population growth rate and rate of growth in technological change, both of which are held fixed over time.

Each of the recommended plans has been estimated by the Treasury Department to be revenue neutral over the budget window. Yet given the level of aggregation in the dynamic models, as well as the embedded behavioral responses, there is no reason to expect that budget neutrality would be maintained for any particular year by applying the implied labor and capital tax rates that result from Treasury's standard revenue estimating analysis into the dynamic models. There are numerous fiscal policy responses that could be applied to maintain the government's intertemporal budget balance through the period of reform. The analysis in this report assumes that average and marginal tax rates are adjusted in each year to maintain a constant level of real government spending for each year after the reforms.

The treatment of the initial tax system in the model, while similar across the models, is also slightly different. The initial tax system for the Ramsey model and the neoclassical growth model includes a flat rate tax on wages and an effective tax rate on capital income. Investment incentives (e.g., accelerated depreciation and tax exemption of the return to owner-occupied housing) reduce the effective tax rate on capital income below the statutory tax rate. The OLG model has a more detailed treatment of the tax system in that labor income taxes are progressive over the life cycle. The OLG model also includes state taxes and a simplified Social Security system, with both state spending and Social Security transfers held constant during the reform. Because the tax system is modeled in a stylized way in each of these models, and the models make simplifying assumptions about a variety of factors, including international capital flows and investment risk, they provide only rough guidance about how tax reforms might affect economic growth. Nevertheless, these models are representative of the types of models that are commonly applied in academic and government research.

Chapter Five: The Panel's Recommendations

Consolidated Family and Work Credit

Eligibility for Family and Work Credits

Chapter Five describes the Family and Work Credits that individuals would be entitled to claim instead of the complex system of tax benefits provided for families under current law. The base amount of the Family Credit depends on family status, as described below. It also allows an additional non-refundable tax credit of \$1,500 for each child dependent and \$500 for each other dependent. The refundable Work Credit provides higher credits and income ceilings for taxpayers who have at least one child dependent.

Chapter Five describes the Panel's recommendations for simpler set of eligibility rules for the Family and Work Credits. Under current law, each family tax benefit,

such as the personal exemption, the child tax credit, and the EITC, requires its own complex determination of whether the taxpayer can claim the benefit. The Panel recommends that simple rules be used to determine whether taxpayers qualify for the Family Credit, and that eligibility for the Work Credit flow intuitively from that determination. For the vast majority of taxpayers who qualify for the Family Credit, the question of whether they also qualify for the Work Credit will turn only on the amount of their unused Family Credit and their income.

The Working Families Tax Relief Act of 2004 made eligibility for family tax benefits more uniform by simplifying the test for whether a taxpayer can treat a child or another person as a dependent in order to claim a personal exemption, child tax credit, or EITC for that person. The Panel adopted the approach of the legislation, but recommends additional reforms aimed at further simplifying eligibility tests for the Family and Work Credits.

The following discussion illustrates how a taxpayer would determine whether he or she qualifies for the Family Credit and Work Credit. The Panel recommends an approach that carefully balances the need for simple rules against the need to target the credits appropriately. These rules are designed to allow the IRS to determine each taxpayer's eligibility for the credits, and to be able to calculate the Work Credit if asked to do so by the taxpayer. This design mandates streamlined rules that also would make it easier for taxpayers to calculate the tax credits for themselves.

Amount of the Credits

The Panel's recommendations would eliminate much of the complexity flowing from current-law rules that reduce the value of various tax benefits as a taxpayer's income increases. Under current law, taxpayers must apply a different mechanism under the personal exemption, the child tax credit, and each of a number of other tax provisions to determine what portion, if any, of the tax benefit they can claim. Thus, for example, the amount of personal exemptions and itemized deductions the taxpayer can deduct and the amount of child tax credits the taxpayer can claim decline as the taxpayer's adjusted gross income rises. The rules limiting or reducing the tax benefits are not uniform, however, forcing many taxpayers to do several different complex calculations. By contrast, the Family Credit would not phase out as income rises. This would represent a meaningful simplification for many taxpayers.

Under current law, a taxpayer may be entitled to a tax refund if his child tax credit exceeds his income tax liability (determined before the credit), provided he meets certain other complex tests. These tests are especially burdensome. As discussed earlier in Chapter Five, the options would be much simpler for these taxpayers because the Family Credit would be effectively refundable for low-income workers through the operation of the Work Credit.

The Work Credit, like the EITC, would increase with a taxpayer's earnings up to a ceiling, and would then decrease as the taxpayer's earnings rise further. Like the EITC, this is intended to encourage work while also limiting the credit to low-income taxpayers.

| | | |
|---|--|-----------------------|
| What Family Credits are available? | Family Credits For: | Would be: |
| | • A single taxpayer with no child dependent | \$1,650 |
| | • A single taxpayer with one child dependent | \$2,800 |
| | • Married taxpayers filing joint returns | \$3,300 |
| | • A taxpayer who could be claimed as a dependent by another taxpayer | \$1,150 |
| | And for each of the following: | An additional: |
| | • A child dependent | \$1,500 |
| • Other dependent | \$ 500 | |

**What Work Credit
is available?**

The Work Credit would approximate the EITC and refundable child tax credit under current law. Taxpayers would determine the amount of their Work Credit by consulting two simple schedules included at the end of this section of the Appendix. The following explains the formulas on which those schedules are based.

The Work Credit would be the amount by which the taxpayer's Family Credit exceeds tax liability before the credit limited to:

- No child dependent: the lesser of 7.65 percent of work income or \$412;
- One child dependent: the lesser of 34 percent of work income or \$2,120
- Two or more child dependents: the lesser of 40 percent of work income or \$3,200.

With an additional credit of:

- up to \$1,450 if the taxpayer has one child dependent
 - o phased in at a rate of 34 cents for every dollar of work income (or taxable income, if lower) over \$6,235;
- up to \$2,600 if the taxpayer has two or more child dependents
 - o phased in at a rate of 40 cents for every dollar of work income (or taxable income, if lower) over \$8,000;

The additional credit would phase out at a rate of 12.5 cents for every dollar of the taxpayer's work income (or taxable income, if higher) above \$17,000 (or \$21,000 if the taxpayer is filing a joint return). Taxable income for these purposes would include any tax-exempt interest and dividends.

The amount of Work Credit a taxpayer can claim depends on work income. What is a taxpayer's work income?

Work income would include a taxpayer's taxable wages and salaries, self-employment income, and labor income for a statutory employee. If a taxpayer makes an election, non-taxable combat pay would be included in work income. This would allow some active duty military families to qualify for a greater Work Credit than they otherwise would have.

Could a taxpayer have investment income and still qualify for the Work Credit?

The Panel recommends simplifying the eligibility rules by eliminating the investment income test for the Work Credit. Under the current-law EITC, a taxpayer who earns more than \$2,800 of investment income in 2006 is ineligible for the credit. This rule discourages low-income workers from saving, because a taxpayer who earns one dollar more than the limit forfeits the entire amount of the EITC.

Under the Panel's options, investment income would be taken into account to determine how much Work Credit the taxpayer could claim. The portion of the Work Credit that is in addition to any excess of the Family Credit over tax liabilities would phase in with the lesser of work income or taxable income, and phase out with the greater of work income or taxable income. Taxable income would include the taxpayer's taxable investment income and, for this purpose, tax exempt dividends and interest on state and local bonds as well. Taxpayers would not be required to satisfy a separate investment income test to claim the Work Credit.

Taxpayer Eligibility

A taxpayer must meet certain qualifications to be eligible to claim the Family and Work Credits. These qualifications are similar to the tests that apply to taxpayers claiming standard deductions, personal exemptions, child tax credits, and the EITC under current law, but are simpler and more consistent. The requirements for claiming the Family Credit are the foundation for Work Credit eligibility. Because the Work Credit is intended as a subsidy for low-income working families, a person who qualifies for the Family Credit must satisfy several other tests to claim the Work Credit.

Who could claim a Family Credit?

Almost anyone who files an individual income tax return could claim the Family Credit.

A taxpayer who could be claimed as a dependent or child dependent on someone else's return, however, could claim a Family Credit of only \$1,150. The Panel recommends this approach to limit available credits when a person's income does not reflect his or her financial status. This represents a simplification of current law, which denies the dependency exemption, the child tax credit, and the EITC to any taxpayer who can be claimed as a dependent or qualifying child on another's return, and imposes a complex formula to calculate how much of the standard deduction the taxpayer can claim.

Who can claim the Work Credit?

A taxpayer would be eligible for the Work Credit if:

- The taxpayer's Family Credit exceeds tax liability before the credit;
- The taxpayer has one child dependent and income below \$28,600 (\$32,600 if married); or
- The taxpayer has two or more child dependents and income below \$37,800 (\$41,800 if married).

The Work Credit would not be available if the taxpayer or the taxpayer's spouse could be claimed as a dependent on someone else's tax return.

Does it matter whether the taxpayer is single or married?

Generally, a family's aggregate Family Credits would be the same regardless of the taxpayer's filing status, but married taxpayers who file as singles may lose a portion of some credits.

The Panel has recommended that a married taxpayer be allowed to choose between filing returns jointly with his or her spouse and filing as a single person, and the Panel's recommendations would reduce the significance of this choice. Moreover, there would be no married-filing-separately status and no head-of-household filing status. This would significantly reduce complexity for many taxpayers.

Instead of having special filing categories, there would be a higher Family Credit available to a person filing as a single taxpayer who has a child dependent (in addition to the credit that could be claimed for the child). A married taxpayer who files as a single taxpayer would generally be unable to claim this higher Family Credit.

In addition, a married taxpayer who files as a single taxpayer would generally be ineligible for the Work Credit.

This limit on the Family and Work Credits for married taxpayers filing as singles would not apply, however, to a taxpayer who lived apart from the taxpayer's spouse for an entire year, and who satisfied certain other conditions that show that the taxpayer and the taxpayer's spouse are no longer a family unit. These rules would be consistent with special rules under current law for separated spouses, but would be somewhat simplified.

The Panel believes this approach would balance the need to simplify the arcane filing status rules and the restrictions on married taxpayers who file separate returns with the need to provide fair and administrable rules for families.

Would a taxpayer have to be a certain age to qualify for the credits?

There would be no age restrictions on taxpayers who claim the Family and Work Credits (although there would be for the taxpayer's dependents, as discussed below). The Panel's recommendations would eliminate the current-law rules that limit the EITC to childless taxpayers between the ages of 25 and 65. The Panel saw no compelling reason to retain this rule in light of other recommendations.

Would the taxpayer need to be a citizen or resident of the United States to claim the credits?

The Family Credit would not apply a citizenship or residency requirement. Like the current law EITC, the Work Credit would be available only to U.S. citizens or individuals who are residents of the United States for the entire year. A taxpayer also would need a Social Security number authorizing work in the United States to claim the Work Credit. In addition, a taxpayer could only qualify for the Work Credit if he lived in the United States for at least half of the year for which the credit is claimed. Special rules would apply to individuals on active duty with the military.

The Panel recognizes that these special Work Credit requirements would impose a burden on a small minority of taxpayers, but believes they are necessary to insure the credit is targeted to low-income workers who live in the U.S.

Would a taxpayer's spouse need to be a citizen or resident for the taxpayer to claim the credits?

A taxpayer who is married to a non-resident alien could not file a joint return or claim the Family Credit for his or her spouse. Thus, in general, under rules described above for married taxpayers filing as singles, the taxpayer could only claim the Family Credit for a single taxpayer, and not the higher amount available to a single taxpayer with a child dependent. The taxpayer would, however, be entitled to claim the additional \$1,500 Family Credit for any child dependent. The taxpayer would not be able to claim the Work Credit.

The restriction on filing a joint return would not apply, however, to a taxpayer who is a citizen or full-year resident of the United States if the spouse elected to be taxed as a full-year U.S. resident. This is consistent with current law, which prohibits a taxpayer who is married to a non-resident alien from filing a joint return or from claiming a dependency exemption for the spouse unless the spouse makes the election to be taxed as a full-year U.S. resident.

Are credits available to U.S. citizens or residents who work abroad?

Family Credits would be available to taxpayers who claim an exemption for income earned abroad. The Work Credit would not be available for these taxpayers.

Credits for Children and Other Dependents—Eligibility

Under the Panel’s recommendations, a taxpayer could claim a \$1,500 Family Credit for each child who was the taxpayer’s “child dependent.” A taxpayer could also take such a child into account under the Work Credit if certain other tests are met. A taxpayer would be able to claim a \$500 Family Credit for other individuals whom the taxpayer supports but who would not qualify as child dependents.

Who would qualify as a taxpayer’s child dependent?

A child dependent would be someone who meets three simple eligibility tests: relationship with the taxpayer, age, and residency.

Who meets the relationship test?

An individual would meet the relationship test if, as under current law, he or she is the taxpayer’s child, stepchild, adopted child (including a foster child officially placed with the taxpayer), stepchild, sibling or stepsibling, or descendants of any of these relations.

Who meets the age test?

The age test would be met by an individual who is 18 years old or younger or is permanently disabled. A child who is 19 or 20 years old and a full-time student would also meet the age test. As discussed earlier in Chapter Five, the age requirement would be a change from current law and reflects the Panel’s view that credits should be available for children over 18 if they are still dependent on their families.

Who would meet the residency test?

The residency test would be satisfied if a child lived with the taxpayer for more than half of the year, including periods when the child is temporarily away from home. For example, a student who does not live with his parents while attending college could still meet the residency requirement. This approach follows current law. Unlike current law, however, if parents are divorced or legally separated, the noncustodial parent generally would not be able to satisfy the residency test and thus could not claim the couple's children as child dependents. The Panel did not adopt the special rule under current law that allows a custodial parent to release the dependency exemption and child tax credit to a noncustodial parent because it creates unnecessary complexity.

Would a taxpayer be required to show he or she supported a child dependent?

There would be no general support test for child dependents under the Panel's recommendations. If a child is self-supporting (i.e., provides more than half his own support), however, the child may not be claimed as a child dependent. This test would simplify the rules under current law and preserve the ability of financially independent children to claim credits on their own returns.

What if two or more taxpayers claim the same child dependent?

Only one person would be able to claim the child on a tax return. If two or more people entitled to treat a child as a child dependent cannot agree on who will claim the child, the Panel recommends application of the so-called tie-breaker rules of current law. In general, if both a parent and a non-parent claim the child, only the parent would be eligible to take the Family Credit and higher Work Credit for that child. If two parents who do not file joint returns claim the child, only the parent with whom the child lived longest (or if time is equal, the parent who had the highest adjusted gross income) would be eligible. If neither of the taxpayers claiming the child was the child's parent, only the taxpayer with the highest adjusted gross income would be eligible.

If an individual does not meet the tests for being a child dependent, can the taxpayer still claim a Family Credit for that person?

Yes, a \$500 Family Credit could be claimed for a dependent who is not a child dependent. But only child dependents would be taken into account for purposes of the Work Credit.

Who would qualify as a taxpayer's dependent?

A dependent would be someone who is a relative of the taxpayer or a member of the taxpayer's household, has gross income below \$3,300, is provided with more than half his or her support by the taxpayer, and cannot be claimed as a child dependent by any other taxpayer. The income limit is the approximate amount that, if taxed at the lowest 15 percent marginal rate, would result in a tax liability of \$500. The Panel's options would waive the income test for full-time students ages 21 to 23. Thus, for example, if a full-time, 22-year-old student met all of the tests for being a child dependent except that he exceeded the age limit of 20, the student's parents could claim a \$500 Family Credit regardless of the student's income.

These requirements are similar to the rules under current law that allow a taxpayer to claim the personal exemption for a qualified relative who is not a qualified child, but do not allow the taxpayer to claim the EITC or child tax credit for that person.

The Panel recognizes that the lower Family Credit for dependents who do not qualify as child dependents introduces additional complexity into the Panel's recommendations. The Panel believes that the balance between fairness and simplicity weighs in favor of allowing a Family Credit when a taxpayer financially supports an individual for whom the taxpayer cannot claim the higher credit. Moreover, the Panel believes that most taxpayers will not need to apply these additional tests.

Would there be any other general requirements to claim a child dependent or dependent?

A taxpayer could not claim an individual as a dependent or a child dependent without providing the individual's name and valid social security number on the federal income tax return. This is generally consistent with the current-law requirement that a taxpayer provide a child's name and taxpayer identification number to claim the dependency exemption and the child tax credit, but is more liberal than the rule for the EITC, which requires the child to have a social security number that is valid for work in the United States.

The preceding discussion describes the rules that the vast majority of taxpayers would have to apply to claim the Family and Work Credits. The Panel would recommend additional special rules for determining whether an individual could be claimed as a taxpayer's child dependent or other dependent, but the application of those rules would be limited.

Could a married individual qualify as a child dependent or dependent?

If an individual is married and files a federal income tax return jointly with his or her spouse, no taxpayer could treat that individual as a dependent or child dependent. This would be consistent with the current-law rule for the personal exemption and the EITC.

Could an individual who is a nonresident alien qualify as a child dependent or dependent?

To qualify as a child dependent or as a dependent, an individual would have to be a resident or citizen of the United States. Thus, a parent of a non-resident alien child could not claim the Family Credit for that child or qualify for the higher Work Credit for that child. This rule is consistent with current law, but provides more uniformity: the rules for the dependency exemption under current law allow taxpayers to claim children who are residents of Canada and Mexico.

Would there be any additional U.S. residency rules to qualify for the higher Work Credit available to taxpayers with child dependents?

Yes. To qualify for the Work Credit, a taxpayer's child dependent would be required to have lived with the taxpayer in the United States for more than half of the year. This is identical to the requirements under the current-law EITC. Although this rule adds complexity by creating an additional eligibility test under the Work Credit, it was retained to ensure the Work Credit would be limited to families that reside within the United States.

The Panel believes that navigating these rules should be as simple as possible for taxpayers and has recommended a structure that gives taxpayers the option of allowing the IRS to compute the Work Credit for them. For those taxpayers who choose to compute the Work Credit themselves, the Panel developed the worksheet and instructions shown in the last section of this Appendix to illustrate the process.

Home Credit

As discussed in Chapter Five, the Panel recommends that the current home mortgage interest deduction be converted into a tax credit of 15 percent of home mortgage interest. The Panel also recommended limiting the credit to interest on a standard principal amount, based on the average price of single-family homes in the United States, adjusted annually to take into account regional variations in housing costs. Each year, taxpayers would apply the current year's mortgage limit. Thus, the amount of home mortgage debt for which the interest credit could be claimed would increase each year if home prices rise.

The Panel recommends basing the average home price on the ceilings that the Federal Housing Administration (FHA) sets for the amount of a home mortgage loan that it will insure. The ceilings are determined using median home prices and are provided on a county-by-county basis to account for regional variations in housing costs. These amounts would be adjusted to reverse a discount the FHA applies and to account for the difference between median and average prices. To determine mortgage loan limits, the amount the FHA reports would be grossed-up to 100 percent of median values and then increased by 125 percent. This is the equivalent of dividing the FHA amount by 0.76. If the credit were in place today, the limits would be between approximately \$227,147 and \$411,704. The IRS currently provides guidelines for average sales prices using a similar methodology for other tax purposes. Thus, if an individual living in Los Angeles, California (a high-cost area) had a home mortgage loan of \$400,000, all of the interest on that loan could qualify for the credit because the loan principal would be below the \$411,704 ceiling for high-cost areas. If the principal amount of the loan was \$500,000, interest on the first \$411,704 of loan principal would qualify.

Currently, banks and other lending institutions that service home mortgage loans are required to report deductible interest and points to the IRS and borrowers annually on Form 1098. Under the Panel's recommendations, these institutions would determine how much of each borrower's interest payments qualify for the Home Credit using the information available from the FHA and would provide that information to borrowers and the IRS. Borrowers who had only one mortgage on their principal residence could simply use the information provided by the lending institution to claim the Home Credit. Borrowers who did not receive annual information statements from a lending institution, or who received a report on more than one loan, could calculate creditable home mortgage interest themselves, using information provided by the IRS.

As under the current law deduction, the Home Credit would be available for interest on a loan that is used to buy, build or substantially improve an individual's principal

residence, and that is secured by the residence. It would also be available for the refinancing of such a loan (limited to the loan's outstanding principal amount). Current rules determine how a loan is used by tracing the loan proceeds. In light of the recommended limitations on benefits for home mortgage interest, these rules should be simplified and should provide straightforward guidelines to reduce complexity for taxpayers.

To claim the credit for home mortgage interest, an individual would have to be legally liable on the mortgage and actually have paid such interest. This rule is the same as current law. Married couples would face the same interest limitation as single taxpayers. Thus, as under current law, married taxpayers who file as singles would have to divide the limit on their one primary residence among themselves. Together, they would only be entitled to claim credits for a single property, which must be the principal residence of one of them.

As described in Chapter Five, the Panel recommends that the changes to the mortgage interest deduction be phased in over five years. During the transitional period, taxpayers would be allowed to claim either the Home Credit or the mortgage interest deduction on existing mortgages. The current-law \$1 million mortgage interest limit would be reduced annually during the five-year transition period. Table A.1 summarizes the transition schedule.

| Year | Mortgage Interest Limit | Tax Benefit |
|-------------|--------------------------------|------------------------|
| 1 | \$900,000 of principal | Deduction |
| 2 | \$700,000 of principal | Deduction |
| 3 | \$500,000 of principal | Deduction |
| 4 | Regional limit of principal | Deduction |
| 5 | Regional limit of principal | 15 percent Home Credit |

Interest on a second home or a home equity loan would not be eligible for transition relief. Interest on new or refinanced mortgages would not qualify for the transitional mortgage interest deduction, but would be eligible for the new Home Credit.

Charity

As described in Chapter Five, the Panel recommends a number of reforms that would improve the deduction for charitable giving. Among these reforms are information reporting for large gifts and better standards for valuing non-cash gifts.

To minimize the recordkeeping burden associated with information reporting, the Panel recommends that information reporting be required only for donors whose total annual contributions to a charity exceed \$600, which is consistent with current-law information reporting thresholds for mortgage interest and trade or business

payments. All cash and non-cash contributions of \$250 or more would count toward the \$600 threshold. The Panel also recommends that small charities that do not receive (1) more than 250 contributions of \$600 or more, or (2) total contributions of more than \$150,000 be exempted from the information reporting requirements. Taxpayers would not be required separately to substantiate contributions for which the charity reported to the taxpayer and the IRS.

The lack of clear, objective standards for establishing the fair market value of donated property has led to many recent valuation abuses. The Panel recommends new rules requiring that appraisals be prepared by a qualified appraiser in accordance with generally accepted and customary appraisal standards. New guidelines should also specify that fair market value is the price that would be received if the property were sold in the appropriate market. For a taxpayer or charity selling property, this would generally be the price received from selling to a dealer or other private party. Standards for appraisers would be imposed to ensure that appraisers have achieved a minimum level of certification or education, have not been barred from practice, are independent and unrelated to the donor or donee, and do not have an interest in the outcome of an appraisal.

To improve the reporting of valuations of contributed property for which a taxpayer is entitled to receive a fair market value deduction, the Panel recommends that appraisers be required to report the value of the contributed property directly to the IRS, the donor, and the charity. The charity would use the appraiser's valuation as the basis for its information reporting.

The Panel believes that current law penalties applicable to appraisers for aiding and abetting the understatement of tax by taxpayers are inadequate to prevent valuation abuses. Accordingly, the Panel recommends that new penalties be imposed on appraisers who misstate the value of property by more than 50 percent. The penalty would be imposed as a percentage of the valuation overstatement up to a maximum penalty.

Chapter Six: The Simplified Income Tax Plan

Territorial Tax Regime

Under the new territorial regime, income earned abroad by controlled foreign corporations and foreign branches of U.S. corporations would fall into one of two categories: (1) "Foreign Business Income," which would generally be exempt from U.S. taxation, and (2) "Mobile Income," which would be taxed by the United States on a current basis.

Foreign Business Income

Income earned abroad by a controlled foreign corporation (a "foreign affiliate") in the conduct of an active business ("Foreign Business Income") would not be subject to U.S. tax at the business level when repatriated as a dividend. Foreign Business

Income is net income after deductions. The general rule is that any payment that is deductible abroad would be taxed in the United States. Thus, non-dividend payments from foreign affiliates to U.S. corporations (e.g., interest, royalties, payments for intercompany transfers) would be subject to U.S. tax. A hybrid security rule would be required to prevent a payment that is treated as deductible interest abroad from being treated as an exempt dividend in the United States.

The Simplified Income Tax Plan would provide that exempt earnings of foreign affiliates could be redeployed to other foreign affiliates in different foreign jurisdictions without losing the benefit of exemption. There would be no tax on the gains from the sale of assets that generate exempt income and losses from the sales of such assets would be disallowed.

Businesses would not receive foreign tax credits for foreign taxes (including both corporate level taxes and dividend withholding taxes) attributable to Foreign Business Income because this income would not be subject to tax in the United States. As a result, the foreign tax credit system would serve a more limited function than it does under present law.

Income of foreign branches would be treated like income of foreign affiliates under rules that would treat foreign trades or businesses conducted directly by a U.S. corporation as foreign affiliates. These rules would be needed to place branches and foreign affiliates on an equal footing. For example, a rule would be needed to impute royalties to foreign branches. All trades or businesses conducted predominantly within the same country would be treated as a single foreign affiliate for this purpose.

Further rules would be needed to address the taxation of Foreign Business Income earned by a U.S. multinational that owns at least 10 percent of the stock of a foreign corporation that is not controlled by U.S. shareholders (so-called "10/50" companies).

All distributed earnings of foreign affiliates would be subject to the new international tax regime following the effective date, regardless of whether such distributions were paid out of pre-effective date or post-effective date earnings.

Mobile Income

Passive and highly mobile income ("Mobile Income") would be subject to tax when earned. Mobile Income would include foreign personal holding company income (e.g. interest, dividends, rents, and royalties arising from passive assets), certain types of foreign active business income that is not likely to be taxed in any foreign jurisdiction (e.g., certain income from personal services and income from international waters and space), and income from the sale of property purchased from or sold to a related person by a foreign corporation located in a country that is neither the origin nor the destination of that property. Small amounts of Mobile Income (measured using a *de minimis* rule based on a percentage of gross income or total assets) would be ignored for simplicity.

A foreign tax credit would be available to offset foreign tax paid (including withholding taxes) on Mobile Income. The current complex foreign tax credit basket rules would be replaced with a single overall foreign tax credit limitation.

Financial services businesses, such as banks, securities dealers, and insurance companies, earn interest and other types of Mobile Income in the conduct of their active business. Special rules would need to provide that qualifying financial services business income is treated as Foreign Business Income to the extent such income is earned through active business operations abroad. Anti-abuse rules would be needed to prevent passive investment income earned by financial services businesses from being treated as Foreign Business Income.

Expense Allocation

Under the Simplified Income Tax Plan, the active business earnings of foreign affiliates would not be subject to U.S. tax at the business level. Accordingly, business expenses that are attributable to these foreign earnings should not be allowed as a deduction against U.S. taxable income. For example, interest and other expenses incurred by a U.S. business to earn exempt foreign earnings would be allocated to those earnings and therefore disallowed. The question of how to allocate expenses to exempt foreign income is a difficult one. Detailed expense allocation rules similar to current law would be necessary. These rules would inevitably involve some complexity, but could be simpler than current-law expense allocation rules.

Interest expense should only be disallowed to the extent that the U.S. operations of a U.S. multinational are more heavily leveraged than the multinational's foreign operations; that is, interest expense should be disallowed to the extent that the ratio of foreign debt to foreign assets is lower than the worldwide ratio of debt to assets. Therefore, the Panel recommends that interest expense be allocated between U.S. and foreign affiliates under rules similar to those recently enacted as part of the American Jobs Creation Act of 2004.

General and administrative expenses that are not charged out to foreign subsidiaries or otherwise recovered by intercompany fees (such as certain stewardship expenses) would be allocated to gross foreign affiliate income in the same proportion that gross foreign affiliate income of the U.S. multinational bears to overall gross income of the worldwide affiliated group. General and administrative expense allocated to foreign affiliate income would then be further allocated between exempt and non-exempt foreign income, with expenses related to exempt foreign affiliate income disallowed.

The Panel recommends that research and experimentation expenses be allocated between domestic source income and foreign-source Mobile Income only. No research and experimentation expenses would be allocated against exempt foreign-source income because all royalty income associated with those research and experimentation expenses would be taxable at the U.S. rate.

Transfer Pricing Enforcement

In a territorial system, U.S. multinationals would have incentives to use transfer pricing to minimize taxable income generated by domestic operations and maximize lightly-taxed income generated in foreign operations. These pressures also exist under current law, and a large body of rules has evolved to enforce “arm’s length” transfer pricing among related parties. Because these pressures are more pronounced in a territorial system, it would be necessary to continue to devote resources to transfer pricing enforcement.

Taxation of Foreign-Source Dividend Income by OECD Countries

Table A.2 provides information regarding the tax treatment of resident corporations on their receipt of direct (non-portfolio) foreign dividends paid out of active business income in OECD countries. Some countries generally exempt such income, while other countries generally tax it with a credit for foreign taxes paid. However, the exact treatment of dividends paid out of active business income varies by country and often is not straightforward. For example, many countries that are classified as “exemption” countries tax some (low-tax) active income currently and exempt other (high-tax) active income. New Zealand and France are examples.

Table A.2. Home Country Tax Treatment of Foreign-Source Dividend Income Received by Resident Corporations Paid out of Active Business Income

| Exemption | Foreign Tax Credit |
|------------------|---------------------------|
| Australia* | Czech Republic |
| Austria | Iceland |
| Belgium | Japan |
| Canada* | Korea |
| Denmark | Mexico |
| Finland | New Zealand |
| France# | Poland |
| Germany | United Kingdom |
| Greece* | United States |
| Hungary | |
| Iceland | |
| Italy# | |
| Luxembourg | |
| Netherlands | |
| Norway | |
| Portugal* | |
| Slovak Republic | |
| Spain | |
| Sweden | |
| Switzerland | |
| Turkey | |

Note: In general, tax treatment depends on qualifying criteria (e.g. minimum ownership level, minimum holding period, the source country, the host country tax rate). The table reports the most generous treatment of foreign direct dividends in each case.

* Exemption by treaty arrangement.

Exemption of 95 percent.

Source: Table compiled from information provided by the OECD Secretariat. Information as of January 2005.

Calculating the Dividend Exclusion Percentage

Under the Panel's proposal, shareholders of U.S. corporations could exclude from income 100 percent of the dividends paid from income of the corporation reported as taxable in the United States. Corporations would report each year on their information reports to shareholders the total dividends paid and the amount which is taxable. For corporations that report all their income in the U.S., 100 percent of dividends paid would be nontaxable to their shareholders. Corporations which earn part of their worldwide income in the U.S. would have to compute the fraction

of worldwide income that is reported as taxable in the U.S. each tax year, and this fraction would be used to calculate the dividend exclusion for dividends paid in the following year. Because of the clean tax base recommended by the Panel, the Panel believes that rules specifying how this percentage is calculated can and should emphasize simplicity over precision. For example, this percentage can be calculated simply by dividing taxable U.S. income each year by worldwide pretax income as reported on the corporation's financial statements for the same year. For simplicity, foreign tax credits on foreign Mobile Income reported as taxable in the U.S. could be ignored in this calculation. Taxpayers who wished to adjust for the difference between accelerated depreciation allowed in the U.S. and book depreciation could be allowed to do so by adding back the difference to U.S. taxable income before calculating the fraction of worldwide income taxable in the U.S., but other adjustments would not be allowed or required.

Disclosure of Foreign Earnings

The Simplified Income Tax Plan would require additional disclosures that would complement the new international tax regime. U.S. businesses with Foreign Business Income would be required to file with their tax return a schedule showing their consolidated worldwide revenues and income before taxes, as reported in their financial statements. The new schedule would disclose the proportion of domestic and foreign revenues and income. In addition, businesses would be required to reconcile the consolidated revenues and income reported on their financial statements with the taxable revenues and income reported on their tax returns.

This disclosure, combined with the exclusion of dividends paid out of domestic earnings, would provide disincentives for corporations to understate the amount of income subject to U.S. tax. A business that understates the amount of income reported on its tax return would increase the amount of tax required to be paid on dividends received by its shareholders. In addition, businesses whose securities are publicly traded would be required by existing disclosure rules to report in their financial statements the proportion of United States and foreign income and revenues computed under tax and accounting rules. This public disclosure would increase the transparency of the business's calculations and provide a better top-down view of a corporation's global operations to shareholders, potential investors, and regulators.

Chapter Seven: The Growth and Investment Tax Plan

As described in Chapter Seven, the Growth and Investment Tax Plan would shift our current tax system towards a consumption tax. Making this shift would represent a substantial change to the U.S. tax system that would present a number of implementation issues. Among these issues are the treatment of financial transactions and financial institutions, transactions between businesses and taxpayers not subject to the cash flow tax (such as individuals and non-profits), and cross-border transactions.

The following sections identify some of the issues considered by the Panel and potential approaches for addressing them. There are additional issues that would need

to be covered in greater detail and require additional rules. Some of these rules would be similar to those that exist under current law.

Distinguishing Between Financial and Non-Financial Business Transactions

One of the central issues in implementing the Growth and Investment Tax Plan would arise in distinguishing between non-financial, or “real” business transactions, whose receipts are generated from business operations, and financial transactions, whose receipts are generated from interest, dividends, or other financial returns. The Growth and Investment Tax Plan excludes financial transactions by non-financial firms from the business tax base, so firms with positive tax liabilities would have an enormous incentive to characterize transactions as financial rather than non-financial. For example, a car dealership would have an incentive to post a low sales price for cars, but to sell cars on credit with a high financing charge. The dealership would benefit by characterizing the interest proceeds from the sale as a financial transaction, making it tax-free.

Another area where there may be an incentive to recharacterize non-financial transactions is the treatment of derivatives. Purchases and sales of commodities generally are cash flows subject to the cash flow tax. Derivatives on commodities, in contrast, are generally thought of as financial in nature, the gains and losses on which generally should not be treated as cash flows subject to the business cash flow tax. However, there may be circumstances in which purchases and sales of these derivatives should be subject to the cash flow tax. For example, a derivative entered into to hedge a non-financial business asset or liability should be treated similarly to the underlying asset as a non-financial business transaction subject to the cash flow tax. Absent special rules, businesses would be able to use combinations of derivatives to create deductions without offsetting income.

Implementation rules would be required to avoid creating incentives for firms to disguise non-financial transactions as financial transactions, and vice versa. For example, transactions that bundle financial and non-financial components could be required to be treated as taxable cash flow. Such implementation rules serve two functions. First, they prevent firms from devoting resources to complex tax planning with the objective of reducing tax liability. While expenditures on such planning may yield private benefits for the firm, they do not have any broader business purpose and they absorb resources that could be deployed elsewhere in more productive manner. Second, tax avoidance reduces the revenue collected from the tax system, which in turn requires higher tax rates to raise a required level of revenue.

Financial Services

As described in Chapter Seven, the taxation of financial services presents difficulties in both consumption and income taxes. Rather than exempting these transactions as is done in most VATs, the Growth and Investment Tax Plan would adopt a special regime for financial institutions that includes both real business and financial cash flows in their business tax base.

There are several alternative approaches that could be used instead of this regime. One alternative approach would be to tax all businesses, not just financial institutions, on the full amount of all transactions between businesses and non-businesses that combine financial and non-financial transactions. This approach would eliminate the necessity of determining whether a business is a financial institution. It would, however, make it necessary to identify those transactions that have both a business and a financial component. Another alternative would be to subject financial institutions to the cash flow tax like other businesses. The disadvantage of this approach would be that, to the extent a transaction includes both real business and financial components, the real business components would be untaxed, which is inconsistent with the general approach of the Growth and Investment Tax Plan. This approach, however, avoids distinguishing between financial and non-financial institutions and transactions that have both real and financial components.

Tax-Free Formations and Mergers and Acquisitions of Businesses

Under current law, there are a number of rules that permit tax-free formations and combinations of businesses. These rules generally provide that no gain or loss is recognized when assets are exchanged for an ownership interest in an entity.

Rules could be crafted to allow for the tax-free treatment of a transfer of assets by an individual to a business and by a business to another business in exchange for an equity interest. These rules could be similar to those under current law, which provide for tax-free treatment for certain transfers of property to a corporation or partnership. In addition, the Growth and Investment Tax Plan could include rules permitting tax-free business combinations similar to the reorganization rules of current law.

The adoption of these rules, however, may create opportunities to transfer losses between businesses. For example, a business could easily transfer assets without tax by contributing them to a subsidiary and selling the stock in a tax-free financial transaction. The rules described in Chapter Seven to address the transferability of negative and positive cash flow may mitigate some of these concerns. It may be necessary, however, to incorporate additional rules similar to current-law judicial doctrines, such as the step transaction doctrine and the business purpose test, which recharacterize or disregard transactions carried out to achieve tax advantages.

Taxation of Employee Stock Options

Employee stock options may present a challenge under the Growth and Investment Tax Plan because they are a form of compensation that is difficult to value. Current tax law has two sets of rules for employee stock options. The first set of rules, which apply to incentive stock options, do not create deductions for the employer and provide employees capital gains tax treatment when they eventually sell the stock that is purchased upon exercise of the options. In contrast, the second set, which apply to nonqualified options that do not have an ascertainable value, create a deduction for the employer when the options are exercised equal to the difference between the market price when exercised and the strike price; employees include the same amount in ordinary income at the exercise date.

Under the Growth and Investment Tax Plan, rules similar to those for incentive stock options could be adopted. Business would not receive a deduction for employee stock options at any point in time; the employee would not recognize any compensation from the option. The effect of this tax treatment would be that options would increase tax collections from business taxation to the extent that employees accept options in lieu of wage compensation. Firms that include employee options in their compensation packages would have a larger tax base, holding other factors equal, than firms that did not use employee stock options. Alternatively, firms could be required to calculate the value of the options at the grant date and would be entitled to a deduction equal to the value of the options when they are granted, with employees recognizing taxable wages at the grant date. Under this approach, the options would have no further consequences for the firm; the transaction would be considered a financial transaction of the firm and capital income for the employee after the grant date.

Small Businesses

The taxation of small businesses, such as sole proprietorships, presents some special issues. Most countries that administer a value-added tax (VAT) provide an exemption for small businesses. However, these countries typically administer an income tax in addition to a VAT. If small businesses were exempted from the Growth and Investment Tax Plan, there would be an incentive for small businesses to pay little or no wages and to retain earnings within the business. Moreover, the U.S. income tax does not provide a small business exemption. The Panel, therefore, concluded that small businesses should be taxable under the Growth and Investment Tax Plan.

One approach to taxing sole proprietorships would be to treat them like other business entities subject to tax on cash flow at the 30 percent rate. A sole proprietorship would be permitted to pay its owner deductible wages and to make distributions of positive cash flow that would be treated as dividends. The difficulty with this approach is that a sole proprietorship would have to file tax returns and maintain separate records even though it is indistinguishable from its owner.

The Panel adopted an alternative approach that would tax positive cash flow from sole proprietorships on individual tax returns and at the graduated individual tax rates. Some have suggested that this approach properly reflects the fact that sole proprietorship income represents a return to labor rather than a return to capital. Cash flow of the sole proprietorship subject to the cash flow tax would not be subject to the 15 percent capital income tax. To the extent that the sole proprietorship receives cash flow that is not subject to the business cash flow tax (e.g., stock gains, dividends, and interest), such cash flow would be subject to the capital income tax when received by the sole proprietorship.

As under our current system, rules would be needed to distinguish between personal activities and business activities. In addition, special issues arise with respect to business assets withdrawn from a sole proprietorship if those assets have been previously expensed. Once withdrawn from the sole proprietorship, the asset future

cash flow attributable to the asset would not be subject to the cash flow tax. Therefore, it may be necessary to treat a withdrawal as a disposition of the asset that results in cash flow equal to the fair market value of the asset.

Use of Businesses to Avoid Tax on Capital Income

One consequence of adding the 15 percent tax on dividends, interest, and capital gains under the Growth and Investment Tax Plan is that individuals may have an incentive to hold financial assets indirectly through a business entity rather than directly. Absent special rules, non-financial businesses could be used to defer tax on returns from financial assets until the business makes distributions to its owners, or permanently if current law rules providing for a step-up in basis to fair market value at death are retained. This potential for tax deferral may contribute to perceptions of unfairness, and may lead to additional tax planning to avoid tax on capital income altogether.

Under current law, there are a number of so-called “anti-deferral” regimes designed to discourage the accumulation of untaxed amounts within a corporation. In some cases, these rules require that the income of a business be imputed to the owners of the business, and in other cases tax is imposed at the business level. One or more of the current anti-deferral regimes could be adopted, or modified, under the Growth and Investment Tax Plan to limit opportunities to defer the capital income tax. For example, to address situations involving individual owners of closely-held businesses, each owner might be required to report his share of the entity’s financial income on his U.S. tax return. Similar rules might be adopted to address other situations. Special rules would be required to determine when the anti-deferral rule should apply. Although anti-deferral rules may prevent some tax avoidance, these rules often require factual inquiries and may not be completely effective in preventing deferral of capital income in a realization-based tax.

Additional Issues in the Tax Treatment of Cross-Border Transactions

Under the destination-basis Growth and Investment Tax Plan, purchases from businesses outside the United States would not be allowed as a deduction against sales in calculating taxable business cash flow. The resale by the importing business would give rise to a taxable receipt. The reseller might “gross up” the resale price to cover the tax cost to the importer of the denial of the deduction for the cost of the import. Alternatively, some importers may try to avoid the tax burden.

If the “importer” is not a taxable U.S. business, it would be outside of the tax system and, as a result, border adjustments would be ineffective. This would be a particularly challenging problem with respect to taxing internet sales and other businesses that have a minimal presence in the United States. Appropriate mechanisms would have to be developed to enforce the tax collection responsibilities for consumption in the United States.

Sourcing the Destination: “Domestic” versus “Foreign” Consumption

Determining when and if goods have been “exported” for foreign consumption would be necessary in order to make border adjustments. Rules exist under current law to determine when a sale of goods occurs (i.e., when beneficial ownership and risk of loss have passed to a buyer either within or outside the United States). A set of rules similar to these so-called “passage-of-title” tests could be used to track the intended ultimate destination of sales of goods under the Growth and Investment Tax Plan.

Determining when and if services have been exported is also necessary to make appropriate border adjustments. Rules would need to be developed to ascertain where services are used or consumed. These rules would be similar to those used in countries that operate a VAT. Service businesses include a range of technical and professional service providers, such as law firms, accounting firms, engineering firms, and management consulting firms.

Tax Treaties

Bilateral income tax treaties that facilitate cross-border investment may need to be renegotiated to account for the new business tax system under the Growth and Investment Tax Plan. Bilateral income tax treaties help prevent double taxation and ensure that U.S. individuals and corporations investing in foreign markets and foreign individuals and corporations investing in the United States receive tax treatment in the treaty country that is comparable to the tax treatment received by home country residents. For example, these treaties provide for interest expense to be deducted by an entity carrying on business through a permanent establishment in the other country for purposes of determining income tax liability to that other country.

Some of the benefits the United States currently provides to foreign businesses through its bilateral tax treaties would be less valuable if the Growth and Investment Tax Plan were adopted. For example, the Growth and Investment Tax Plan would not provide interest deductions to permanent establishments of treaty partner businesses. As a result, foreign governments could seek to renegotiate or terminate their tax treaty arrangements with the United States. The Panel suggests that the Growth and Investment Tax Plan retain withholding taxes on dividends and non-portfolio interest consistent with current law, but these taxes could be reduced or eliminated by treaty.

Chapter Eight: Value-Added Tax

VAT Exemptions

In evaluating a proposal to adopt a broad based value-added tax (VAT), the Panel assumed that all domestic consumption would be included in the tax base unless specifically exempted. Exemptions for goods and services could be provided either with or without a credit for “input tax” previously paid on goods or services used to produce the exempt good. When a good or service is “exempt with credit,” a supplier of that good or service is allowed to claim input tax credits associated with the exempt

good or service even though no tax is assessed on the exempt sale. If a supplier's input tax credits exceed VAT liability, the supplier would receive a refund from the government. In contrast, when a good or service is "exempt without credit," the good or service supplier would not assess VAT on sale of the exempt good, but could not claim input tax credits associated with that sale.

Substantial administrative complications arise in a VAT when business entities sell both taxable and exempt goods, or assess different VAT rates on different goods. In these cases, administrative rules must be established to allocate input credits between exempt, preferred-rate, and taxable sales. A broad based VAT that taxes virtually all goods and services using a single rate and implements necessary omissions from that base using an exemption with credit minimizes economic distortions and simplifies compliance and administration. For this reason, providing exemptions with credit would generally be preferable to exempting goods or services without credit. Charitable and religious services are a special exception to this general rule.

It is inappropriate to tax exports in a destination-based VAT because exports do not represent domestic consumption. Exports would therefore be exempt with credit under the VAT. Further discussion of this issue appears in Chapter Eight. Other types of goods and services that would be excluded, exempt with credit, exempt without credit, or receive other unique treatment under the VAT studied by the Panel are described in Table A.3.

| Table A.3. Domestically Consumed Goods and Services Receiving Distinctive Treatment | | |
|--|--|--|
| Exempt with Credit (Zero-rated) | Exempt without Credit | Other |
| <ul style="list-style-type: none"> • Noncommercial government services • Primary and secondary education | <ul style="list-style-type: none"> • Charitable and religious services • Food produced and consumed on farms | <ul style="list-style-type: none"> • Residential housing (prepayment method) • Financial services (same as the Growth and Investment Tax Plan treatment) |

Government Services

For reasons of administrative simplicity and to preserve economic neutrality between the private sector and the public sector, governments would pay VAT on purchases just like other businesses and individuals. However, like a business selling taxable goods and services, governments would be entitled to claim input tax credits on all inputs used to provide services.

Non-commercial government services provided to the public for a fee would be exempt with credit. Other noncommercial government services and intra-government transfers would be excluded from the base. No VAT would be imposed on taxes or fines, because these charges are not paid in return for a specific good or service.

Commercial services provided by government (state, local, or federal) for a fee would be taxed. For example, VAT would be collected on services such as transportation services provided by a local transit authority or water provided by a government-owned utility. Rules would be needed to distinguish between commercial and noncommercial government activities, and would inevitably entail some substantial complexity.

Education

Most primary and secondary education is provided by state and local governments at public schools, generally free of charge. Applying a VAT to privately provided primary and secondary education would discriminate against private education by making it more expensive relative to public schools. The Panel concluded that introducing the VAT should not change the competitive balance between public and private education. Thus, primary and secondary education would be exempt with credit, regardless of whether provided by government or private institutions. Rules would be needed to prevent non-educational exempt consumption through schools (such as cafeterias set up on school premises to avoid VAT).

Postsecondary education is provided by public and private institutions for a fee. In addition to educating students, postsecondary institutions engage in a broad array of research activities, many of which overlap with activities conducted in the private sector. For these reasons, the Panel determined that it would be appropriate to apply the VAT to postsecondary education, whether provided by public or private institutions.

Charitable and Religious Services

Charitable and religious services provided by non-profit organizations would be exempt without credit. When a charitable or religious organization supplies goods or services free of charge, no VAT would be assessed. However, when a charitable or religious organization supplied new goods or services that compete with other businesses and are offered at market prices, those goods and services would be taxed. For example, memberships that provide access to cultural or recreational institutions would be taxable. Rules would be needed to define the boundary between exempt charitable or religious services and commercial services. These rules could also exempt charitable or religious services provided for a nominal fee. Donations and government grants received by charities would not be considered payments in return for goods or services and therefore also would not be taxed.

Charitable and religious services would be exempted without credit because of the sector's heavy reliance on used goods and donations and the consequent administrative complications and abuses that might arise under a regime providing exemption with credit. Any charitable or religious service provider would remain eligible to claim input tax credits with respect to their VAT liability for any commercial services they provide, just like any other business. The threshold for mandatory VAT collection of \$100,000 in annual gross taxable receipts would allow charitable and religious organizations that provide only a small amount of commercial services to remain outside the VAT system entirely, even if their non-taxable operations were quite extensive. For those charitable and religious organizations with receipts from commercial services in excess of the VAT threshold, or that elect to collect VAT, allocation rules would be required to distinguish input credits related to tax-free charitable and religious services from input credits related to commercial services.

Housing

The purchase price of new residential real estate would be taxed. Taxing housing services in this way is more administratively feasible than taxing the imputed value of owner-occupied housing, but excludes pre-existing housing from VAT. Activities related to renovating existing housing (e.g., purchasing building materials or repair and maintenance services) would be taxed. To ensure both that renters and owners receive comparable treatment and that new residential real estate that is subject to a lease would not be double taxed, leases of residential housing would be exempt from VAT, as would the imputed value of owner-occupied housing services. Rules would be needed to define the appropriate VAT treatment if real estate were to be converted from residential to non-residential use or vice versa.

Financial Services

Financial services would be taxed using an approach similar to that proposed for the Growth and Investment Tax Plan.

Modified Family Credit and Work Credit for Partial Replacement VAT

Modified Family Credit

The modified Family Credit described in Chapter Eight would be computed by starting with a base amount for household type and adding additional amounts for the number of children and other dependent members of the household. The base Family Credit amounts are provided in Table A.4.

Table A.4. Family Credit Amounts under Partial Replacement VAT

| Household Type | Base Credit |
|---|-------------|
| Married Taxpayers Filing Joint Returns | \$4,300 |
| Single Taxpayers With Dependent Children | \$3,300 |
| Single Taxpayers with no Child Dependent | \$2,150 |
| Taxpayers Who Could be Claimed as a Dependent | \$1,650 |

Each family would add to the base credit amount \$2,000 for each child and \$1,000 for each other dependent. The Family Credit amounts would be adjusted annually for inflation.

Modified Work Credit

The modified Work Credit would be the amount by which the taxpayer's modified Family Credit exceeds tax liability before the credit limited to:

- No child dependent: the lesser of 17.65 percent of work income or \$1,832;
- One child dependent: the lesser of 44 percent of work income or \$4,870;
- Two or more child dependents: the lesser of 50 percent of work income or \$6,650

With an additional credit of:

- up to \$1,950 if the taxpayer has one child dependent
 - phased in at a rate of 44 cents for every dollar of work income (or taxable income, if lower) over \$11,100;
- up to \$3,100 if the taxpayer has two or more child dependents
 - phased in at a rate of 50 cents for every dollar of work income (or taxable income, if lower) over \$13,300;

The additional credit would phase out at a rate of 12.5 cents for every dollar of the taxpayer's work income (or taxable income, if higher) above \$22,000 (or \$26,000 if the taxpayer is filing a joint return).

Evolution of VAT Rates in Developed Economies

In addition to reviewing econometric research relating to the money machine argument, the Panel examined the evolution of VAT rates in developed countries. The table below shows the basic VAT rates in OECD countries for the period from 1976 to 2005. The shaded years represent the most recent periods during which the basic VAT rate either did not change or was lowered.

In examining the Table A.5, it is worth noting that more than half of the countries represented are members of the European Union (EU). The European Economic

| Table A.5. Standard VAT/GST in OECD Member Countries | | | | | | | | | | | | |
|--|-------|-------|-------|-------|-------|------|------|------|------|------|------|------|
| | 1976 | 1980 | 1984 | 1988 | 1990 | 1992 | 1994 | 1996 | 1998 | 2000 | 2003 | 2005 |
| Australia | - | - | - | - | - | - | - | - | - | 10.0 | 10.0 | 10.0 |
| Austria | 18.0 | 18.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 |
| Belgium | 18.0 | 16.0 | 19.0 | 19.0 | 19.0 | 19.5 | 20.5 | 21.0 | 21.0 | 21.0 | 21.0 | 21.0 |
| Canada | - | - | - | - | - | 7.0 | 7.0 | 7.0 | 7.0 | 7.0 | 7.0 | 7.0 |
| Czech Republic | - | - | - | - | - | - | 22.0 | 22.0 | 22.0 | 22.0 | 22.0 | 19.0 |
| Denmark | 15.0 | 22.0 | 22.0 | 22.0 | 22.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 |
| Finland | - | - | - | - | - | - | 22.0 | 22.0 | 22.0 | 22.0 | 22.0 | 22.0 |
| France | 20.0 | 17.6 | 18.6 | 18.6 | 18.6 | 18.6 | 18.6 | 20.6 | 20.6 | 20.6 | 19.6 | 19.6 |
| Germany | 11.0 | 13.0 | 14.0 | 14.0 | 14.0 | 14.0 | 15.0 | 15.0 | 16.0 | 16.0 | 16.0 | 16.0 |
| Greece | - | - | - | 16.0 | 18.0 | 18.0 | 18.0 | 18.0 | 18.0 | 18.0 | 18.0 | 18.0 |
| Hungary | 0.0 | - | - | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 |
| Iceland | - | - | - | - | 22.0 | 22.0 | 24.5 | 24.5 | 24.5 | 24.5 | 24.5 | 24.5 |
| Ireland | 20.0 | 25.0 | 23.0 | 25.0 | 23.0 | 21.0 | 21.0 | 21.0 | 21.0 | 21.0 | 21.0 | 21.0 |
| Italy | 12.0 | 15.0 | 18.0 | 19.0 | 19.0 | 19.0 | 19.0 | 19.0 | 20.0 | 20.0 | 20.0 | 20.0 |
| Japan | - | - | - | - | - | 5.0 | 3.0 | 3.0 | 5.0 | 5.0 | 5.0 | 5.0 |
| Korea | - | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 |
| Luxembourg | 10.0 | 10.0 | 12.0 | 12.0 | 12.0 | 15.0 | 15.0 | 15.0 | 15.0 | 15.0 | 15.0 | 15.0 |
| Mexico | - | - | 10.0 | 10.0 | 10.0 | 10.0 | 10.0 | 15.0 | 15.0 | 15.0 | 15.0 | 15.0 |
| Netherlands | 18.0 | 18.0 | 19.0 | 20.0 | 18.5 | 17.5 | 17.5 | 17.5 | 17.5 | 17.5 | 19.0 | 19.0 |
| New Zealand | - | - | - | - | - | - | 12.5 | 12.5 | 12.5 | 12.5 | 12.5 | 12.5 |
| Norway | - | - | - | - | - | - | 22.0 | 23.0 | 23.0 | 23.0 | 24.0 | 24.0 |
| Poland | - | - | - | - | - | - | - | - | 22.0 | 22.0 | 22.0 | 22.0 |
| Portugal | - | - | - | 17.0 | 17.0 | 16.0 | 16.0 | 17.0 | 17.0 | 17.0 | 19.0 | 19.0 |
| Slovak Republic | - | - | - | - | - | - | 25.0 | 23.0 | 23.0 | 23.0 | 20.0 | 19.0 |
| Spain | - | - | - | 12.0 | 12.0 | 13.0 | 16.0 | 16.0 | 16.0 | 16.0 | 16.0 | 16.0 |
| Sweden | 17.65 | 23.46 | 23.46 | 23.46 | 23.46 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 | 25.0 |
| Switzerland | - | - | - | - | - | - | 6.5 | 6.5 | 6.5 | 7.5 | 7.6 | 7.6 |
| Turkey | - | - | - | - | - | - | 15.0 | 15.0 | 15.0 | 17.0 | 18.0 | 18.0 |
| United Kingdom | 8.0 | 15.0 | 15.0 | 15.0 | 15.0 | 17.5 | 17.5 | 17.5 | 17.5 | 17.5 | 17.5 | 17.5 |
| Unweighted average | 14.0 | 16.9 | 17.2 | 17.5 | 17.7 | 16.9 | 17.4 | 17.6 | 17.9 | 17.8 | 17.8 | 17.7 |

Note: Shaded years represent most recent periods during which the VAT rate either did not change or was lowered.
Source: OECD Secretariat. Rates as of January 2005.

Community, the predecessor to today's EU, required member countries to impose a VAT in the late 1960s. Thus, Belgium, Denmark, France, Germany (then West Germany), Ireland, Italy, Luxembourg, the Netherlands, and the United Kingdom all adopted VATs between 1967 and 1973. Similarly, Greece, Portugal, and Spain adopted VATs in the late-1980s in preparation for EU membership.

Chapter Nine: National Retail Sales Tax

Tax-Inclusive Rates

As explained in Box 9.1, it is equally valid to think of tax rates in tax-inclusive or tax-exclusive terms. The most appropriate way to compare a national retail sales tax rate to the state sales taxes paid by most Americans is to consider the tax-exclusive rate. On the other hand, it is appropriate to compare the retail sales tax rate with current income tax rates by utilizing the tax-inclusive rate. Table A.6 provides the tax-inclusive rates that correspond to the tax-exclusive rate estimates provided in Table 9.1.

| Table A.6. Retail Sales Tax Rate Estimates Reported as Tax-Inclusive Rates | | | |
|--|---------------|------------------------------|-----------------------------|
| Evasion Rate / Base | Extended Base | Partial Replacement VAT Base | Median State Sales Tax Base |
| Low Evasion (15%) | 25% | 28% | 39 % |
| Higher Evasion (30%) | 33% | 37% | 47% |

Source: Department of the Treasury, Office of Tax Analysis.

Uniform Cash Grant Program

The Treasury Department calculated the uniform cash grant program as the retail sales tax (inclusive) rate times the poverty guideline amount defined by the Department of Health and Human Services, providing double the single person amount for married couples. The projected poverty guideline amounts in 2006 are \$9,820 for a single person and \$3,360 for each additional person in the household. With this cash grant program, assuming 15 percent evasion for personal consumption spending, the revenue-neutral rate would be approximately 25 percent on a tax-inclusive basis (34 percent on a tax-exclusive basis). The rebate amounts in 2006 would therefore be \$2,494 (\$4,988 for married couples) plus \$853 for each dependent.

Targeted Cash Grant Program

The Treasury Department developed a targeted cash grant proposal with a phase-in range and a phase-out range. The proposal required providing an annual cash subsidy of as much as \$7,068 for married couples (\$3,534 for singles), plus \$2,570 for each dependent. Like the EITC, the program would phase in over a range. The program would begin to phase out when family income exceeds ten times the maximum

available rebate and be completely phased out when income reached 20 times the maximum available rebate. For example, a married couple with no children would receive a higher rebate as income increased up to an income level of \$17,670. This couple's rebate would begin to phase out once income exceeded \$70,680 and phase out completely once income exceeded \$141,360. By comparison, a married couple with two children would receive a higher rebate as income increased up to an income level of \$30,520. This family's rebate would begin to phase out once income exceeded \$122,080 and phase out completely once income exceeded \$244,160. Families that qualify under current law for the EITC would continue to receive those amounts as an additional cash subsidy.

Hypothetical Taxpayer Analysis

Standard distributional estimates, revenue estimates, and hypothetical taxpayer calculations performed by the Treasury Department for any tax proposal assume that the Administration's economic forecast, including the price level, is unchanged over the ten-year budget period. A retail sales tax would create a "wedge" between the prices producers receive for their goods and the amount that they would have left to pay wages and other forms of labor compensation and to pay the suppliers of capital (interest and profits). Since by standard assumption the price level cannot rise, this wedge must cause wages and payments to capital to fall. The reduction in wages reduces the payroll tax base, and therefore payroll taxes paid. This reduction in payroll taxes must be accounted for in hypothetical taxpayer examples for proposals, such as a retail sales tax or a value-added tax, that produce a wedge between producer and consumer prices.

An Example of a State Sales Tax Base: Florida

Existing state sales tax bases are narrower than the broad tax bases evaluated by the Panel, and the breadth of these tax bases may be illustrative of potential base erosion. For example, it is estimated that Florida has the 11th broadest tax base among states that impose retail sales taxes. In relative terms, Florida has a limited number of exemptions from its sales tax. Nevertheless, Florida's retail sales tax imposes sales tax on only a small number of services and has at least 90 exemption categories. For example, neither financial nor medical services are taxed. All sales to the U.S. government, a state or any county, municipality, or political subdivision of a state, and nonprofit religious, charitable, scientific or educational institutions are exempt. Moreover, churches and the federal government are exempt from the requirement to collect and remit sales tax.

Florida also exempts a wide variety of goods, including Bibles, hymnals, prayer books and other religious publications; church service and ceremonial raiment and equipment; food and drink for human consumption that is classified as "general grocery items," but not when sold by restaurants, cafeterias, concession stands, or other similar places of business; water (except certain mineral or carbonated water);

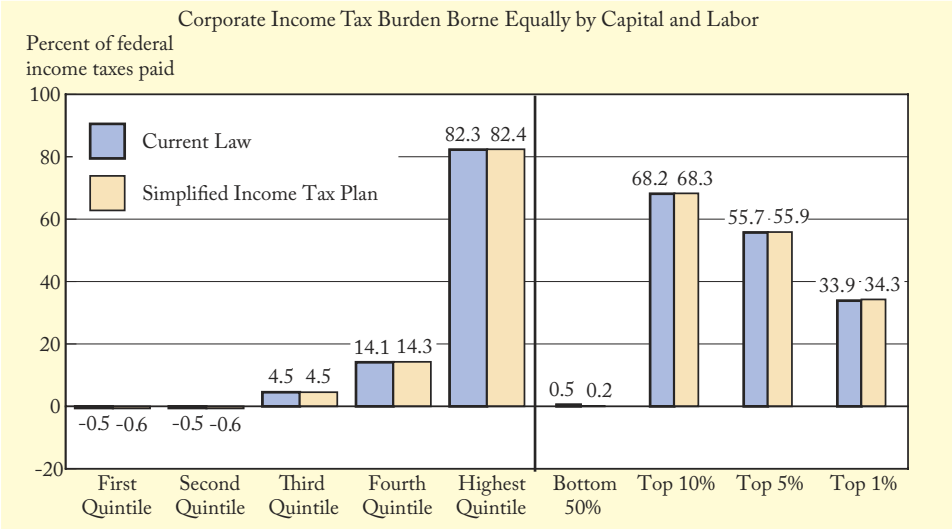
any food or beverage that is donated to a food bank by a retailer that sells food products; hospital meals and rooms; prescription medication and other products and supplies dispensed at retail by a licensed pharmacist on a physician's order; hypodermic needles; test kits used to treat or diagnose human disease; artificial eyes and limbs; hearing aids, crutches and prosthetics; sales or rentals of guide dogs for the blind and sales of food or other items for such dogs; certain prepared meals sold by a nonprofit organization to handicapped, elderly, or indigent people; rentals of more than six months' duration; school books and lunches sold at institutions of higher learning; firefighting and rescue service equipment and supplies purchased by volunteer fire departments; admissions to athletic or other events sponsored by schools; solar energy systems, fertilizers, insecticides, seedlings, and cuttings; sales of U.S. and Florida flags; purchases of office supplies made by the Florida Retired Educators Association; and the sale of a racing dog by its owner if the owner is also the breeder of the animal.

Additional Distribution Tables

Alternative Distribution of the Corporate Income Tax

As explained in Chapter Three, for the purpose of distributional analysis, the Treasury Department assumes that the burden of the corporate income tax is borne entirely by owners of capital. The alternative distribution figures presented below show the distribution of the income tax burden under current law and each of the plans assuming that half of the burden of the corporate income tax is distributed to labor, while the other half is distributed to owners of capital. However, the change in corporate tax burden associated with the options is distributed to just owners of capital. This reflects the assumption that over the budget window owners of capital are the group that bears the burden of this tax. Over time, however, some (or all) of the burden of corporate taxes is likely to be shifted to workers and consumers.

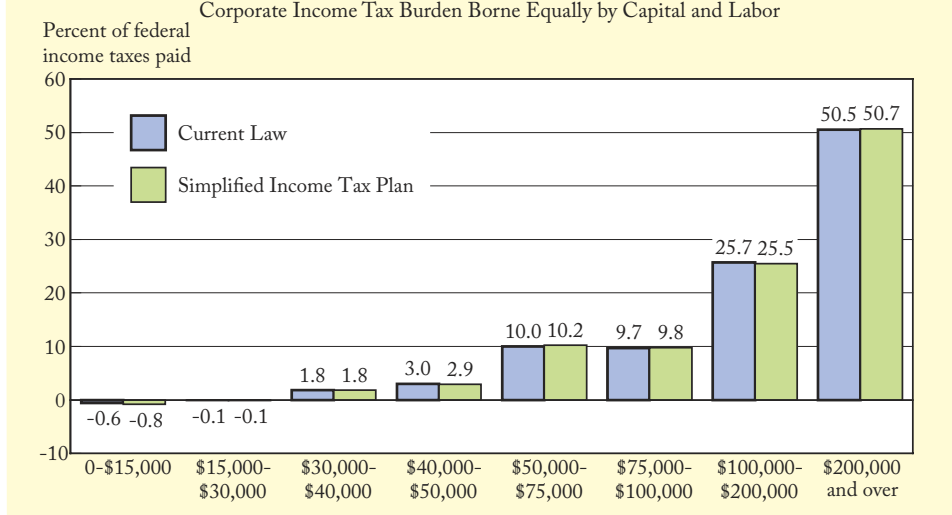
Figure A.1. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Simplified Income Tax Plan by Income Percentile (2006 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2006 law at 2006 cash income levels. Quintiles begin at cash income of; Second \$12,910; Third \$27,461; Fourth \$45,345; Highest \$84,124; Top 10% \$123,076; Top 5% \$169,521; Top 1% \$407,907; Bottom 50% below \$36,738.

Source: Department of the Treasury, Office of Tax Analysis.

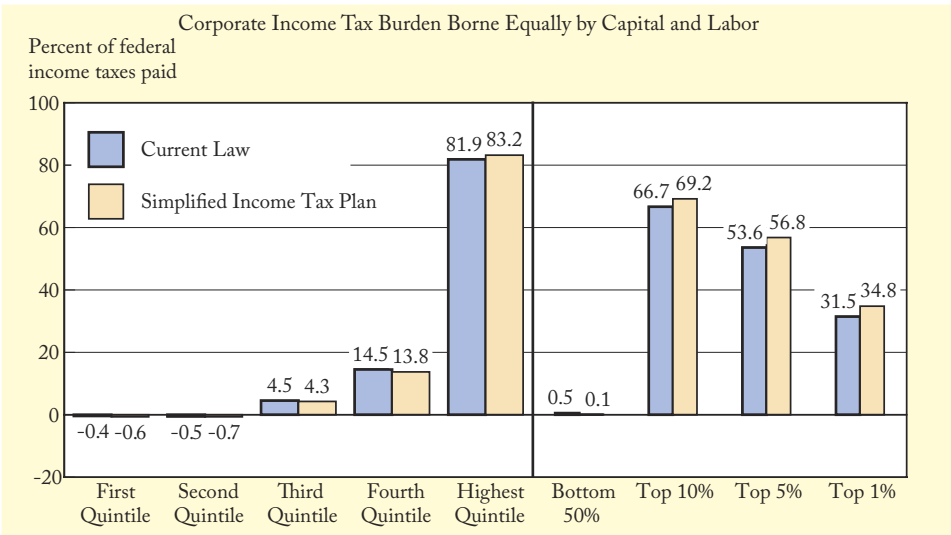
Figure A.2. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Simplified Income Tax Plan by Income Level (2006 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2006 law at 2006 cash income levels.

Source: Department of the Treasury, Office of Tax Analysis.

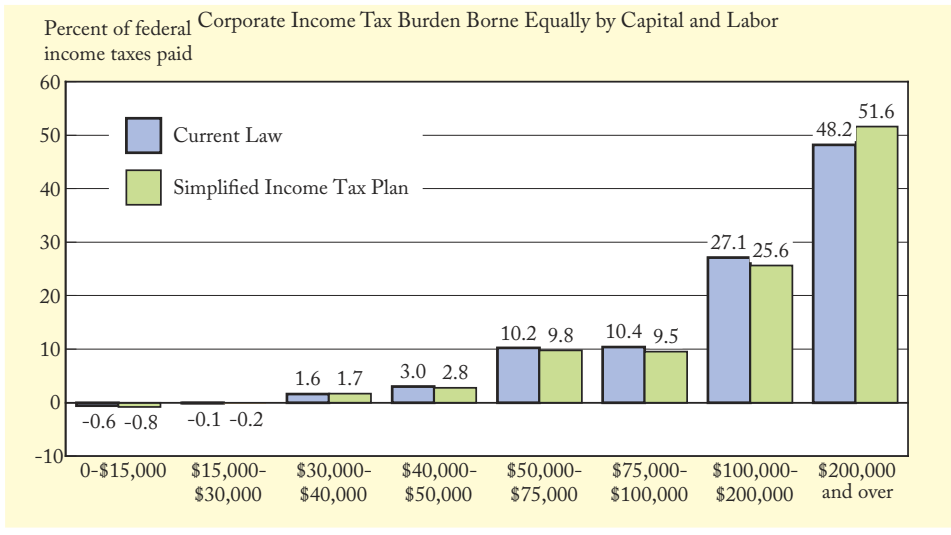
Figure A.3. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Simplified Income Tax Plan by Income Percentile (2015 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2015 law at 2006 cash income levels. Quintiles begin at cash income of; Second \$12,910; Third \$27,461; Fourth \$45,345; Highest \$84,124; Top 10% \$123,076; Top 5% \$169,521; Top 1% \$407,907; Bottom 50% below \$36,738.

Source: Department of the Treasury, Office of Tax Analysis.

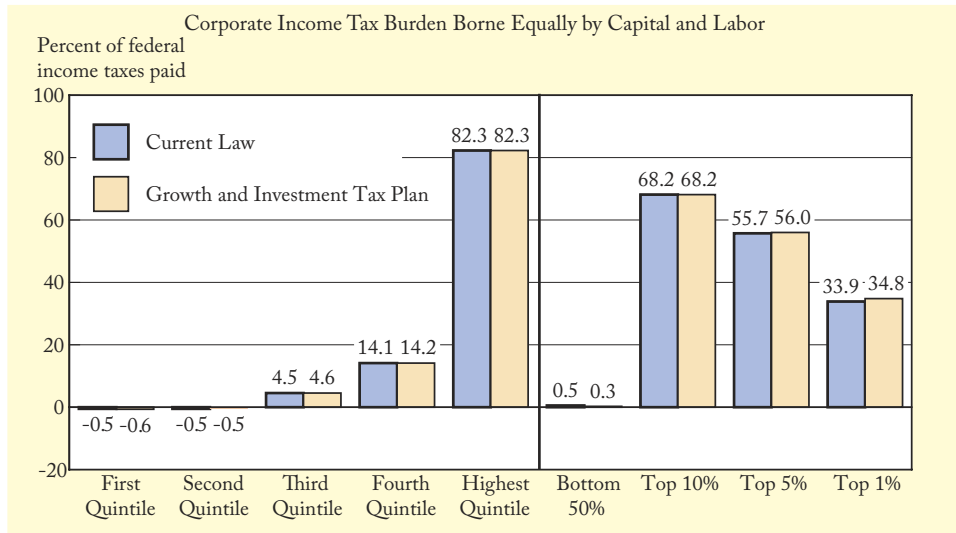
Figure A.4. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Simplified Income Tax Plan by Income Level (2015 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2015 law at 2006 cash income levels.

Source: Department of the Treasury, Office of Tax Analysis.

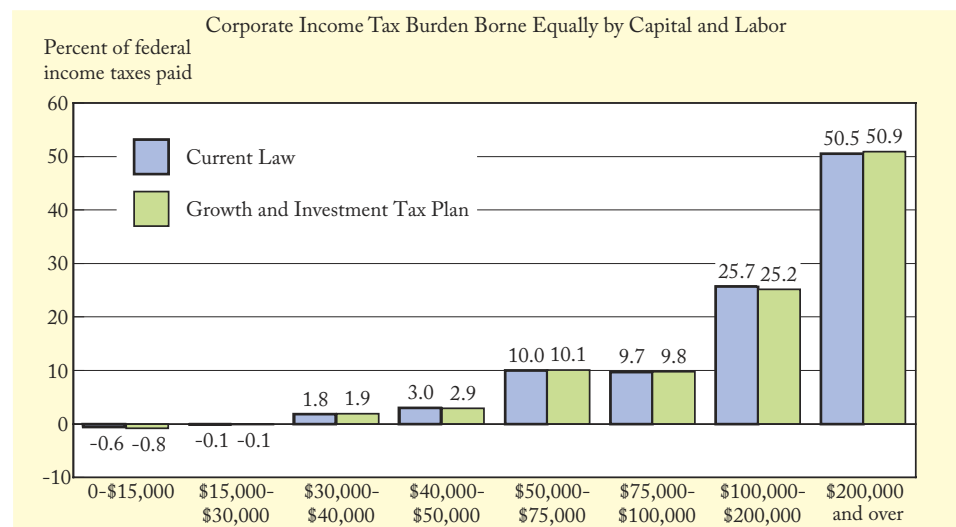
Figure A.5. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Growth and Investment Tax Plan by Income Percentile (2006 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2006 law at 2006 cash income levels. Quintiles begin at cash income of; Second \$12,910; Third \$27,461; Fourth \$45,345; Highest \$84,124; Top 10% \$123,076; Top 5% \$169,521; Top 1% \$407,907; Bottom 50% below \$36,738.

Source: Department of the Treasury, Office of Tax Analysis.

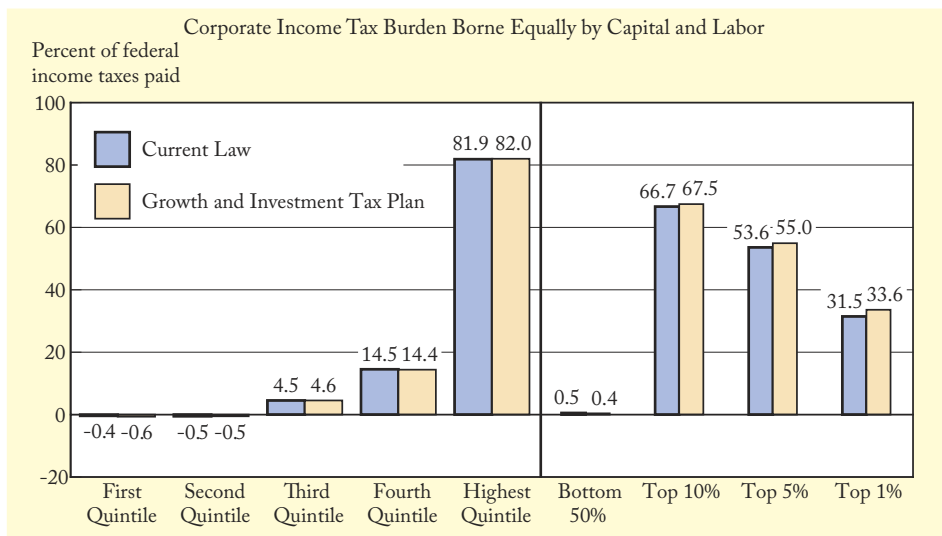
Figure A.6. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Growth and Investment Tax Plan by Income Level (2006 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2006 law at 2006 cash income levels.

Source: Department of the Treasury, Office of Tax Analysis.

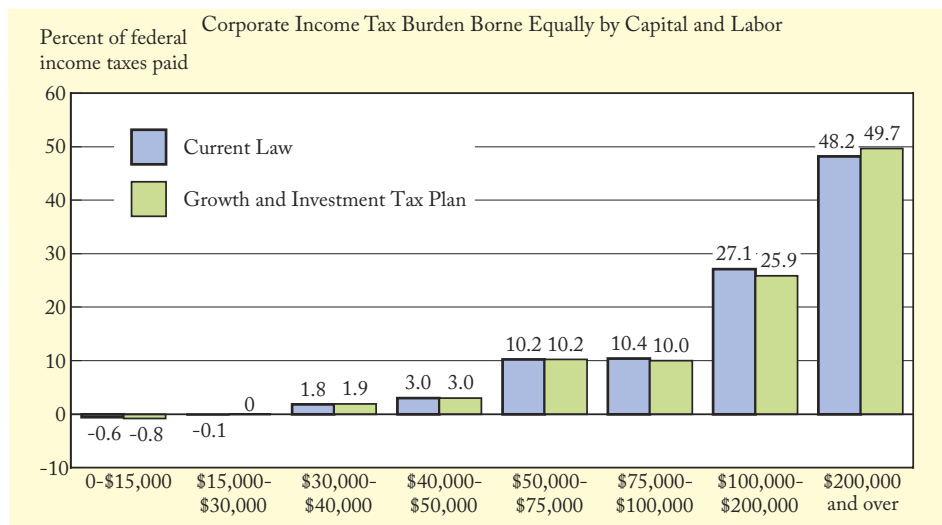
Figure A.7. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Growth and Investment Tax Plan by Income Percentile (2015 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2015 law at 2006 cash income levels. Quintiles begin at cash income of; Second \$12,910; Third \$27,461; Fourth \$45,345; Highest \$84,124; Top 10% \$123,076; Top 5% \$169,521; Top 1% \$407,907; Bottom 50% below \$36,738.

Source: Department of the Treasury, Office of Tax Analysis.

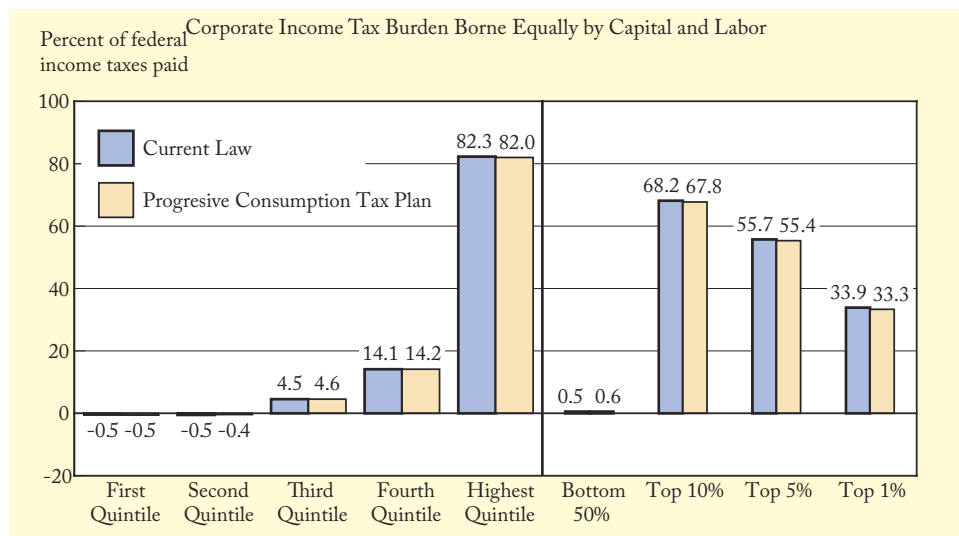
Figure A.8. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Growth and Investment Tax Plan by Income Level (2015 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2015 law at 2006 cash income levels.

Source: Department of the Treasury, Office of Tax Analysis.

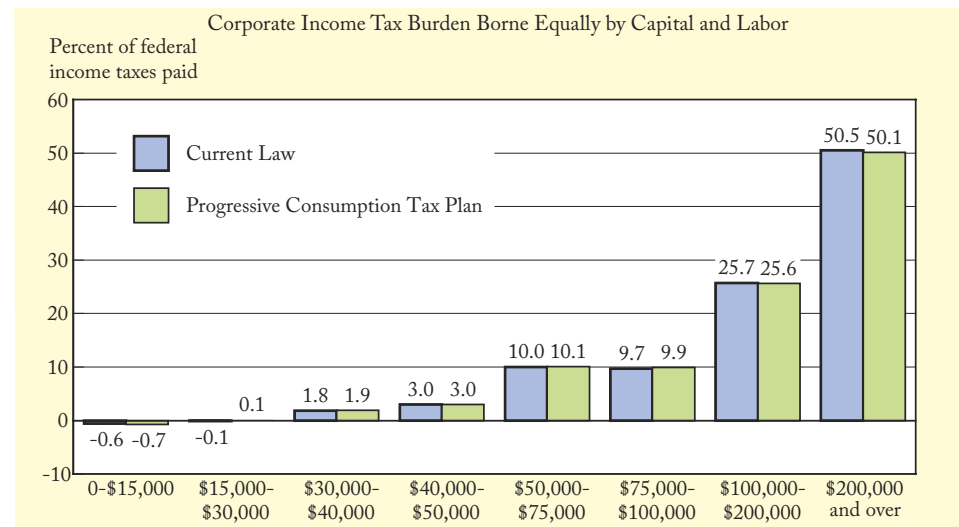
Figure A.9. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Progressive Consumption Tax Plan by Income Percentile (2006 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2006 law at 2006 cash income levels. Quintiles begin at cash income of; Second \$12,910; Third \$27,461; Fourth \$45,345; Highest \$84,124; Top 10% \$123,076; Top 5% \$169,521; Top 1% \$407,907; Bottom 50% below \$36,738.

Source: Department of the Treasury, Office of Tax Analysis.

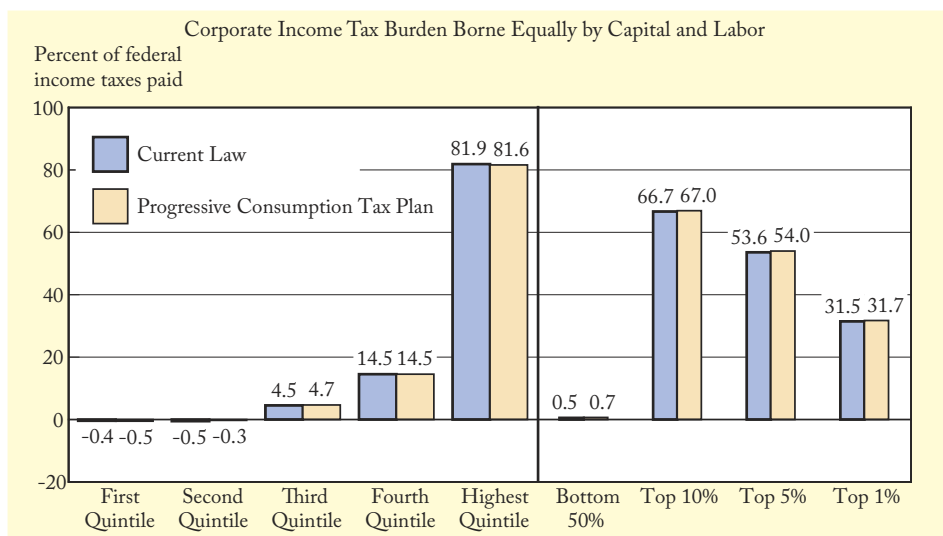
Figure A.10. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Progressive Consumption Tax Plan by Income Level (2006 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2006 law at 2006 cash income levels.

Source: Department of the Treasury, Office of Tax Analysis.

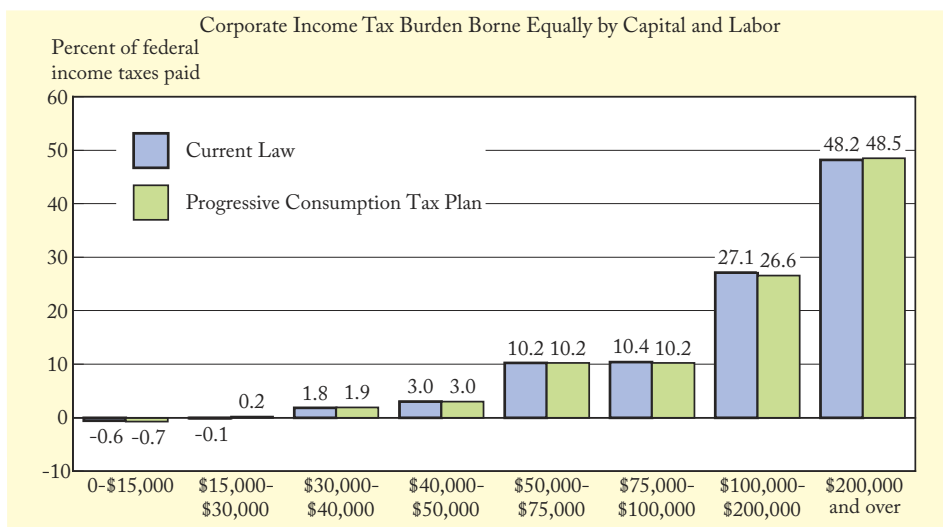
Figure A.11. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Progressive Consumption Tax Plan by Income Percentile (2015 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2015 law at 2006 cash income levels. Quintiles begin at cash income of; Second \$12,910; Third \$27,461; Fourth \$45,345; Highest \$84,124; Top 10% \$123,076; Top 5% \$169,521; Top 1% \$407,907; Bottom 50% below \$36,738.

Source: Department of the Treasury, Office of Tax Analysis.

Figure A.12. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Progressive Consumption Tax Plan by Income Level (2015 Law)



Note: Estimates assume the current corporate income tax burden is borne equally by labor and capital, but changes to the corporate income tax under the proposal are assumed to be borne by capital only. The standard assumption is that the corporate income tax is borne by capital generally. Estimates of 2015 law at 2006 cash income levels.

Source: Department of the Treasury, Office of Tax Analysis.

Distributional Analysis Over the Ten-Year Budget Period

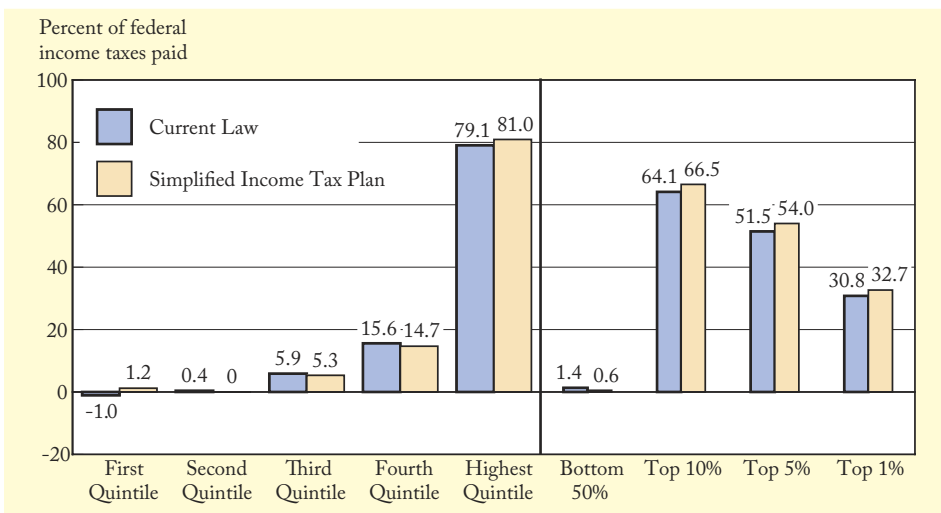
The Treasury Department provided the Panel with distributional analysis of the Simplified Income Tax Plan, the Progressive Consumption Tax Plan, and the Growth and Investment Tax Plan over the ten-year budget period. The technical explanation of the estimates that follows was provided by the Treasury Department at the request of the Panel.

The analysis uses a model that traces the income and taxes paid in each year for a sample of “tax families” constructed from income tax returns. A tax family is defined as the non-dependent primary taxpayer, the taxpayer’s spouse, and their dependents for income tax purposes. The analysis begins with the distribution of the individual income and corporate income tax to “tax families” in each year. Individual income tax liabilities are distributed to payers (which includes dependent filers) and corporate income tax liabilities to capital income generally. Tax liabilities are aggregated at the family level. The cash income of all family members is also aggregated at the family level.

Family-level income and tax liabilities in each year are then divided by an equivalence scale. The equivalence scale is based on family size and adjusts for economies of scale as family size increases. Each family’s “equivalenced” income and tax liabilities are then attributed to each member of the family in that year.

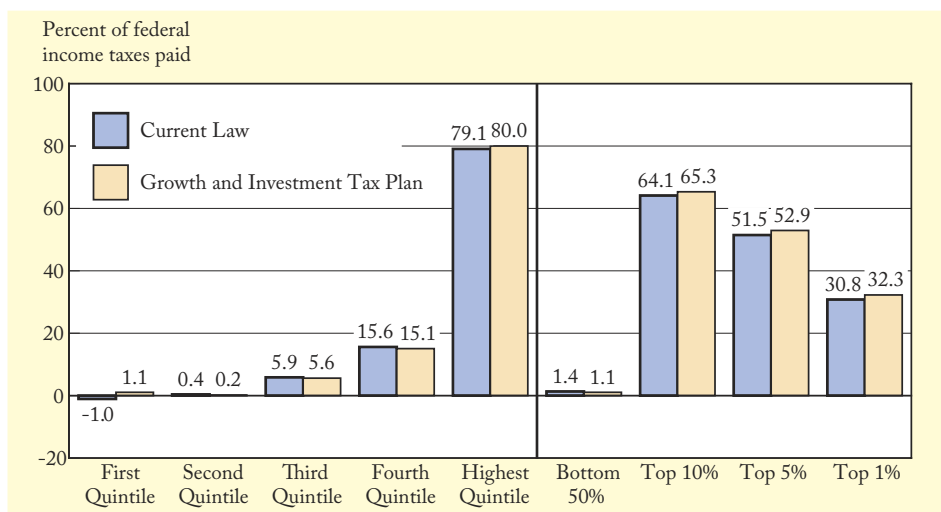
The present values of year-by-year “equivalenced” income and tax liabilities are then computed for each individual present in the first year of the ten-year budget period. The discount rate used is the sum of the forecast inflation rate (as measured by the CPI-U) and an assumed four percent real rate of return. These present values are converted to real level annuities over the ten-year budget period with the same present value. The real level annuity values of income are used to place individuals into income quintiles, and tax shares are computed from the real level annuity values for taxes and income.

Figure A.13. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Simplified Tax Income Plan by Income Percentile (Over Budget Period)



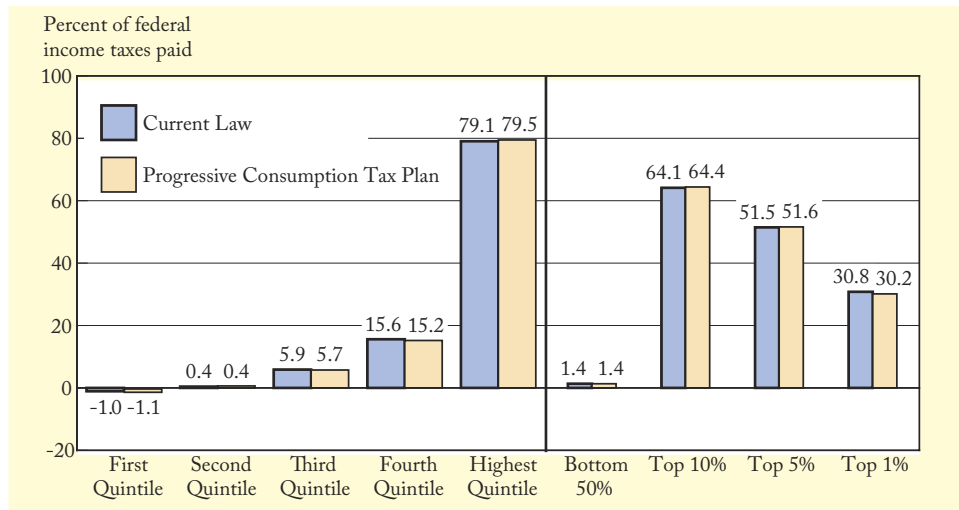
Note: See explanation in text.
Source: Department of the Treasury, Office of Tax Analysis.

Figure A.14. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Growth and Investment Tax Plan by Income Percentile (Over Budget Period)



Note: See explanation in text.
Source: Department of the Treasury, Office of Tax Analysis.

Figure A.15. Alternative Distribution of Federal Income Tax Burden Under Current Law and the Progressive Consumption Tax Plan by Income Percentile (Over Budget Period)



Note: See explanation in text.
 Source: Department of the Treasury, Office of Tax Analysis.

Additional Tax Forms

As discussed in Chapters Six and Seven, the tax returns that would be used under both the Simplified Income Tax Plan or the Growth and Investment Tax Plan would fit on a single page. These tax returns could even fit on the front and back of a postcard. Figures A.16 and A.17 show how these forms would appear if printed on a postcard instead of a regular sheet of paper. Figure A.18 shows the Work Credit worksheet and instructions.

Figure A.16. Form 1040-Simple

Postcard - Front

| | | | | | |
|---|--|--|-----------|---------------------------------|--|
| 1040-SIMPLE | | U.S. Individual Income Tax Return | | 200X | (99) |
| For the year Jan. 1-Dec. 31, 200X, or other tax year beginning | | , 200X, ending | | , 20 | OMB No. 1545-XXXX |
| L A B E L H E R E | Your first name and initial | Last name | | Your social security number | |
| | If married, spouse's first name and initial | Last name | | Spouse's social security number | |
| | Home address (number and street, city, town or post office, state, and ZIP code). If you have a P.O. box or a foreign address, see page xx. | | | | ▲ Important! ▲ You must enter your SSN(s) above. |
| 1 | Wages, salaries, tips, etc. Attach Form(s) W-2 | | | 1 | |
| 2 | Business income or (loss). Attach Schedule C, C-EZ, E, or F | + | | 2 | |
| 3 | Taxable interest and dividends | + | | 3 | |
| 4 | Gain or (loss) on stock. Attach Schedule D | + | | 4 | |
| 5 | Other gains or (losses). Attach Form 4797 | + | | 5 | |
| 6 | Taxable distributions (retirement and savings) | + | | 6 | |
| 7 | Social security benefits | + | | 7 | |
| 8 | Other income. List type and amount ▶ | + | | 8 | |
| 9 | Add lines 1 through 8 | | | 9 | |
| Total income = | | | | | |
| 10 | Charitable contributions | | 10 | | |
| 11 | Multiply line 9 by 1% (.01) | - | | 11 | |
| 12 | Subtract line 11 from line 10. If zero or less, enter -0- | | | 12 | |
| 13 | Social security benefits deduction (see page xx) | + | | 13 | |
| 14 | Health insurance deduction | + | | 14 | |
| 15 | Add lines 12 through 14 | | | 15 | |
| 16 | Subtract line 15 from line 9. If zero or less, enter -0- | - | | 16 | |
| Taxable income = | | | | | |
| For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page xx. Cat. No. 00000X 1040-SIMPLE (200X) | | | | | |

Postcard - Back

| | | | | | | | | | | | | | | | |
|--|---|---------------------|------------------------|--------------------------|-----------|----------------|------|-----------------|------------------------|--|------|---------------------|------|---|------------------------|
| 17 | Figure your tax (see page xx) | | | Tax = | 17 | | | | | | | | | | |
| 18 | Home credit (see page xx) | - | | | 18 | | | | | | | | | | |
| 19 | Subtract line 18 from line 17. If zero or less, enter -0- | | | | 19 | | | | | | | | | | |
| 20 | Family credit. Attach Schedule A if required | - | | | 20 | | | | | | | | | | |
| 21 | Subtract line 20 from line 19. If zero or less, enter -0- | | | | 21 | | | | | | | | | | |
| 22 | Self-employment tax | | | | 22 | | | | | | | | | | |
| 23 | Other taxes and foreign tax credit. Attach Schedule O | + | | | 23 | | | | | | | | | | |
| 24 | Add lines 21 through 23. If zero or less, enter -0- | | | Total tax = | 24 | | | | | | | | | | |
| 25 | Federal income tax withheld | | 25 | | | | | | | | | | | | |
| 26 | Work credit | + | | 26 | | | | | | | | | | | |
| 27 | Savers credit. Attach Form XXXX | + | | 27 | | | | | | | | | | | |
| 28 | Estimated tax and other payments | + | | 28 | | | | | | | | | | | |
| 29 | Add lines 25 through 28 | | | Total payments = | 29 | | | | | | | | | | |
| 30 | If line 29 is more than line 24, subtract line 24 from line 29. If you want to use direct deposit, attach Form XXXX | | | Amount overpaid = | 30 | | | | | | | | | | |
| 31 | Amount of line 30 you want applied to your 200Y estimated tax | | | | 31 | | | | | | | | | | |
| 32 | If line 24 is more than line 29, subtract line 29 from line 24 | | | Amount you owe = | 32 | | | | | | | | | | |
| <p>Sign Here Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.</p> <p>Married? See page xx. Keep a copy for your records. <input type="checkbox"/> If married but not filing with spouse, check here.</p> <table border="1" style="width: 100%;"> <tr> <td>Your signature</td> <td>Date</td> <td>Your occupation</td> <td rowspan="2">Preparer's SSN or PTIN</td> </tr> <tr> <td>Spouse's signature. If filing with spouse, both must sign.</td> <td>Date</td> <td>Spouse's occupation</td> </tr> </table> <p>Daytime phone number ()</p> <p>Preparer's signature</p> | | | | | | Your signature | Date | Your occupation | Preparer's SSN or PTIN | Spouse's signature. If filing with spouse, both must sign. | Date | Spouse's occupation | Date | Check if self-employed <input type="checkbox"/> | Preparer's SSN or PTIN |
| Your signature | Date | Your occupation | Preparer's SSN or PTIN | | | | | | | | | | | | |
| Spouse's signature. If filing with spouse, both must sign. | Date | Spouse's occupation | | | | | | | | | | | | | |
| Firm's name (or yours if self-employed), address, and ZIP code | EIN | Phone no. () | | | | | | | | | | | | | |
| 1040-SIMPLE (200X) | | | | | | | | | | | | | | | |

Figure A.17. Form 1

Postcard - Front

| | | | | | |
|--|---|---|-----------|--|---|
| Form 1 | | U.S. Individual Tax Return | | 200X | (99) |
| For the year Jan. 1-Dec. 31, 200X, or other tax year beginning, 200X, ending, 20 | | OMB No. 1545-XXXX | | | |
| Label (See instructions on page xx.) Use the IRS label. Otherwise, please print or type. | L A B E L H E R E | Your first name and initial | Last name | Your social security number | |
| | | If married, spouse's first name and initial | Last name | Spouse's social security number | |
| | | Home address (number and street). If you have a P.O. box, see page xx. | | Apt. no. | ▲ Important! ▲ You must enter your SSN(s) above. |
| City, town or post office, state, and ZIP code. If you have a foreign address, see page xx. | | | | | |
| Taxable Amount Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld. | 1 | Wages, salaries, tips, etc. Attach Form(s) W-2 | 1 | | |
| | 2 | Business cash flow. Attach Schedule 1 | 2 | | |
| | 3 | Taxable interest and dividends | 3 | | |
| | 4 | Gains or (losses) | 4 | | |
| | 5 | Taxable distributions (retirement and savings) | 5 | | |
| | 6 | Social security benefits | 6 | | |
| | 7 | Other income. List type and amount ▶ | 7 | | |
| | 8 | Total cash flow. Add lines 1 through 7 | 8 | | |
| | 9 | Charitable contributions | 9 | | |
| | 10 | Multiply line 8 by 1% (.01) | 10 | | |
| | 11 | Subtract line 10 from line 9. If zero or less, enter -0- | 11 | | |
| | 12 | Social security benefits deduction | 12 | | |
| | 13 | Health insurance deduction | 13 | | |
| | 14 | Add lines 11 through 13 | 14 | | |
| | 15 | Taxable amount. Subtract line 14 from line 8. If zero or less, enter -0- | 15 | | |
| For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page xx. | | Cat. No. 00000X | | Form 1 (200X) | |

Postcard - Back

| | | | | |
|---------------------------------|--|---|------------------------|---|
| Form 1 (200X) | | Page 2 | | |
| Tax and Credits | 16 | Tax (see page xx) | 16 | |
| | 17 | Home credit (see page xx) | 17 | |
| | 18 | Subtract line 17 from line 16. If zero or less, enter -0- | 18 | |
| | 19 | Family credit. Attach Schedule A if required | 19 | |
| | 20 | Subtract line 19 from line 18. If zero or less, enter -0- | 20 | |
| | 21 | Self-employment tax | 21 | |
| Payments | 22 | Other taxes. Attach Schedule O | 22 | |
| | 23 | Total tax. Add lines 20 through 22 | 23 | |
| | 24 | Federal tax withheld | 24 | |
| Refund or Amount You Owe | 25 | Work credit | 25 | |
| | 26 | Estimated tax and other payments | 26 | |
| | 27 | Total payments. Add lines 24 through 26 | 27 | |
| Sign Here | 28 | Amount overpaid. If line 27 is more than line 23, subtract line 23 from line 27. If you want to use direct deposit, attach Form XXXX | 28 | |
| | 29 | Amount of line 28 you want applied to your 200Y estimated tax | 29 | |
| | 30 | Amount you owe. If line 23 is more than line 27, subtract line 27 from line 23 | 30 | |
| Paid Preparer's Use Only | Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge. | | | |
| | Married? See page xx. Keep a copy for your records. | Your signature | Date | Your occupation |
| | | Spouse's signature. If filing with spouse, both must sign. | Date | Spouse's occupation |
| | | Preparer's signature | Date | Check if self-employed <input type="checkbox"/> |
| | Firm's name (or yours if self-employed), address, and ZIP code | EIN | Preparer's SSN or PTIN | Daytime phone number () |
| | | Phone no. () | | |
| | | Form 1 (200X) | | |

Figure A.18. Work Credit Worksheet and Instructions

Line 26—Work Credit

Step 1 How To Figure the Credit

1. Do you want the IRS to figure the credit for you?
 Yes. Just check the box and enter your tax-exempt interest and dividends at the bottom of Schedule A if you meet the conditions listed on Schedule A.
 No. Go to Step 2.

Step 2 Can You Take the Credit?

1. Can you or your spouse be claimed as a dependent on someone else's 200X return?
 Yes. STOP You cannot take this credit.
 No. Continue

2. Do you and your spouse have a social security number that allows you to work or is valid for the work credit (see page xx)?
 Yes. Continue
 No. STOP You cannot take this credit.

3. Did you and your spouse live in the United States for more than half of 200X? Members of the military, see page xx before you answer.
 Yes. Continue
 No. STOP You cannot take this credit.

4. Were you married at the end of 200X and are electing **not** to file your 200X return with your spouse? If you are separated from your spouse, see page xx.
 Yes. STOP You cannot take this credit.
 No. Continue

5. Were you a nonresident alien for any part of 200X?
 Yes. See *Nonresident aliens* on page xx.
 No. Continue

6. Are you filing Form 2555 or 2555-EZ (relating to foreign earned income)?
 Yes. STOP You cannot take this credit.
 No. Go to question 7.

Step 3 Work Income

1. Figure work income:
 1040-SIMPLE, line 1 _____
 Add:

- All of your nontaxable combat pay if you elect to include it in work income. See *Combat pay, Nontaxable* on page xx.
- Your business income or (loss) from 1040-SIMPLE, line 2. But if line 2 includes an amount from Schedule E or you were a statutory employee, see *Schedule E filers or Statutory employees*, whichever applies, on page xx.
- Any amounts from Schedule SE, lines 15 and 17, if you elected to use either optional method to figure your net earnings from self-employment.

 _____ + _____
Work Income =

2. Do any of the following apply to you?

- The amount on your Schedule A, line 4, is more than the amount on your Schedule A, line 5.
- You lived with 2 or more child dependents in the United States for more than half of 200X and your work income is less than \$37,800 (\$41,800 if married).
- You lived with 1 child dependent in the United States for more than half of 200X and your work income is less than \$28,600 (\$32,600 if married).


 Yes. Use the worksheet on page xx to figure your credit.
 No. STOP You cannot take this credit.

7. Do any of the following apply to you?

- The amount on your Schedule A, line 4, is more than the amount on your Schedule A, line 5.
- You lived with 2 or more child dependents in the United States for more than half of 200X and the amount on 1040-SIMPLE, line 16, is less than \$37,800 (\$41,800 if married).
- You lived with 1 child dependent in the United States for more than half of 200X and the amount on 1040-SIMPLE, line 16, is less than \$28,600 (\$32,600 if married).

 Yes. Go to Step 3.
 No. STOP You cannot take this credit.

Work Credit Worksheet—Line 26

Keep for Your Records 



The IRS can figure your work credit for you. Just check the box and enter your tax-exempt interest and dividends at the bottom of Schedule A if you qualify.

Otherwise, be sure you answered the questions on page XX to see if you can take this credit before completing this worksheet.

Part 1

All Filers

1 Is the amount on Schedule A, line 4, more than the amount on Schedule A, line 5?

- Yes.** Subtract Schedule A, line 5, from Schedule A, line 4, and enter the result.
- No.** Skip lines 1 through 3 and enter -0- on line 4.

1

2 Enter your work income from Step 3 on page XX.

2

3 Look up the amount on line 2 in the blue table on page XX to find the credit. Enter the credit here.

3

4 Enter the smaller of line 1 or line 3.

4

Next. If you have at least one child dependent who lived with you in the United States for more than half of 200X, go to Part 2. Otherwise, enter the amount from line 4 on line 11.

Part 2

Filers With At Least One Child Dependent

5 Look up the amount on line 2 in the orange table on pages XX through XX to find the credit. Enter the credit here.

5

6 Enter your taxable income from 1040-SIMPLE, line 16.

6

7 Enter your tax-exempt interest and dividends.

7

8 Add lines 6 and 7.

8

9 Look up the amount on line 8 in the orange table on pages XX through XX to find the credit. Enter the credit here.

9

10 Enter the smaller of line 5 or line 9.

10

Then, add the amounts on lines 4 and 10 and enter the result on line 11.

Part 3

Work Credit

11 **This is your work credit.**

11



CAUTION If you take the work credit even though you are not eligible, you may not be allowed to take the credit for up to 10 years. See Form 8862, Who must file, on page XX. You may also have to pay penalties.

Enter this amount on 1040-SIMPLE, line 26.



Definitions and Special Rules

(listed in alphabetical order)

Combat pay, Nontaxable. If you were a member of the U.S. Armed Forces who served in a combat zone, certain pay is excluded from your income. See *Combat Zone Exclusion* in Pub. 3. You can elect to include this pay in your work income when figuring the work credit. The amount of your nontaxable combat pay should be shown in Form(s) W-2, box 12, with code Q. If you are filing a return with your spouse and both you and your spouse received nontaxable combat pay, you can each make your own election.



Electing to include nontaxable combat pay may increase or decrease your work credit. Figure the credit with and without your nontaxable combat pay before making the election.

Form 8862, Who must file. Generally, you must file Form 8862 if your earned income credit (EIC) or your work credit for a year after 1996 was reduced or disallowed for any reason other than a math or clerical error. But do not file Form 8862 or take the work credit for the:

- 2 years after the most recent tax year for which there was a final determination that your EIC or work credit was reduced or disallowed due to reckless or intentional disregard of the EIC or work credit rules, or
- 10 years after the most recent tax year for which there was a final determination that your EIC or work credit was reduced or disallowed due to fraud.

Members of the military. If you were on extended active duty outside the United States, your home is considered to be in the United States during that duty period. Extended active duty is

military duty ordered for an indefinite period or for a period of more than 90 days. Once you begin serving extended active duty, you are considered to be on extended active duty even if you serve fewer than 90 days.

Nonresident aliens. If you are filing your return with your spouse, go to Step 2, question 6, on page xx. Otherwise, stop; you cannot take the work credit.

Schedule E filers. Do not include any income or (loss) from Schedule E in your work income. However, if you received a Schedule K-1, include in work income any amounts from Schedule K-1 (Form 1065), box 14, code A, and Schedule K-1 (Form 1065-B), box 9. Reduce these Schedule K-1 amounts by any partnership section 179 expense deduction claimed, unreimbursed partnership expenses claimed, and depletion claimed on oil and gas properties.

Social security number (SSN). For the work credit, a valid SSN is a number issued by the Social Security Administration unless "Not Valid for Employment" is printed on the social security card and the number was issued solely to apply for or receive a federally funded benefit.

To find out how to get an SSN, see page xx. If you will not have an SSN by April 15, 200X, see *What If You Cannot File on Time?* on page xx.

Statutory employees. If you received a Form W-2 and the "Statutory employee" box in box 13 of that form was checked, include in your work income the amount from box 13 of your Form W-2 instead of your net profit or (loss) from the Schedule C or C-EZ that you filed as a statutory employee and that is included on 1040-SIMPLE, line 2.

Use this table for line 3 of your worksheet

For All Work Credit Filers

1. To find your credit, read down the "At least - But less than" columns and find the line that includes your work income from Step 3 on page XX.

2. Then, go to the column that includes the number of child dependents who lived with you in the United States for more than half of 200X. Enter the credit from that column on line 3 of your worksheet.

Example. You have one child dependent who lived with you in the United States for more than half of 200X. Your work income is \$2,455. You would enter \$833 on line 3 of your worksheet.

| If your work income is— | | And you have— | | |
|-------------------------|---------------|---------------------|---------------------|------------------------------|
| At least | But less than | No child dependents | One child dependent | Two or more child dependents |
| 2,300 | 2,400 | 180 | 799 | 940 |
| 2,400 | 2,500 | 187 | 833 | 980 |

| If your work income is— | | And you have— | | | If your work income is— | | And you have— | | | If your work income is— | | And you have— | | |
|-------------------------|---------------|---------------------|---------------------|------------------------------|-------------------------|---------------|---------------------|---------------------|------------------------------|-------------------------|---------------|---------------------|---------------------|------------------------------|
| At least | But less than | No child dependents | One child dependent | Two or more child dependents | At least | But less than | No child dependents | One child dependent | Two or more child dependents | At least | But less than | No child dependents | One child dependent | Two or more child dependents |
| 1 | 100 | 4 | 17 | 20 | 3,000 | 3,100 | 233 | 1,037 | 1,220 | 6,000 | 6,100 | 411 | 2,057 | 2,420 |
| 100 | 200 | 11 | 51 | 60 | 3,100 | 3,200 | 241 | 1,071 | 1,260 | 6,100 | 6,200 | 411 | 2,091 | 2,460 |
| 200 | 300 | 19 | 85 | 100 | 3,200 | 3,300 | 249 | 1,105 | 1,300 | 6,200 | 6,300 | 411 | 2,120 | 2,500 |
| 300 | 400 | 27 | 119 | 140 | 3,300 | 3,400 | 256 | 1,139 | 1,340 | 6,300 | 6,400 | 411 | 2,120 | 2,540 |
| 400 | 500 | 34 | 153 | 180 | 3,400 | 3,500 | 264 | 1,173 | 1,380 | 6,400 | 6,500 | 411 | 2,120 | 2,580 |
| 500 | 600 | 42 | 187 | 220 | 3,500 | 3,600 | 272 | 1,207 | 1,420 | 6,500 | 6,600 | 411 | 2,120 | 2,620 |
| 600 | 700 | 50 | 221 | 260 | 3,600 | 3,700 | 279 | 1,241 | 1,460 | 6,600 | 6,700 | 411 | 2,120 | 2,660 |
| 700 | 800 | 57 | 255 | 300 | 3,700 | 3,800 | 287 | 1,275 | 1,500 | 6,700 | 6,800 | 411 | 2,120 | 2,700 |
| 800 | 900 | 65 | 289 | 340 | 3,800 | 3,900 | 295 | 1,309 | 1,540 | 6,800 | 6,900 | 411 | 2,120 | 2,740 |
| 900 | 1,000 | 73 | 323 | 380 | 3,900 | 4,000 | 302 | 1,343 | 1,580 | 6,900 | 7,000 | 411 | 2,120 | 2,780 |
| 1,000 | 1,100 | 80 | 357 | 420 | 4,000 | 4,100 | 310 | 1,377 | 1,620 | 7,000 | 7,100 | 411 | 2,120 | 2,820 |
| 1,100 | 1,200 | 88 | 391 | 460 | 4,100 | 4,200 | 317 | 1,411 | 1,660 | 7,100 | 7,200 | 411 | 2,120 | 2,860 |
| 1,200 | 1,300 | 96 | 425 | 500 | 4,200 | 4,300 | 325 | 1,445 | 1,700 | 7,200 | 7,300 | 411 | 2,120 | 2,900 |
| 1,300 | 1,400 | 103 | 459 | 540 | 4,300 | 4,400 | 333 | 1,479 | 1,740 | 7,300 | 7,400 | 411 | 2,120 | 2,940 |
| 1,400 | 1,500 | 111 | 493 | 580 | 4,400 | 4,500 | 340 | 1,513 | 1,780 | 7,400 | 7,500 | 411 | 2,120 | 2,980 |
| 1,500 | 1,600 | 119 | 527 | 620 | 4,500 | 4,600 | 348 | 1,547 | 1,820 | 7,500 | 7,600 | 411 | 2,120 | 3,020 |
| 1,600 | 1,700 | 126 | 561 | 660 | 4,600 | 4,700 | 356 | 1,581 | 1,860 | 7,600 | 7,700 | 411 | 2,120 | 3,060 |
| 1,700 | 1,800 | 134 | 595 | 700 | 4,700 | 4,800 | 363 | 1,615 | 1,900 | 7,700 | 7,800 | 411 | 2,120 | 3,100 |
| 1,800 | 1,900 | 142 | 629 | 740 | 4,800 | 4,900 | 371 | 1,649 | 1,940 | 7,800 | 7,900 | 411 | 2,120 | 3,140 |
| 1,900 | 2,000 | 149 | 663 | 780 | 4,900 | 5,000 | 379 | 1,683 | 1,980 | 7,900 | 8,000 | 411 | 2,120 | 3,180 |
| 2,000 | 2,100 | 157 | 697 | 820 | 5,000 | 5,100 | 386 | 1,717 | 2,020 | 8,000 | ---- | 411 | 2,120 | 3,200 |
| 2,100 | 2,200 | 164 | 731 | 860 | 5,100 | 5,200 | 394 | 1,751 | 2,060 | | | | | |
| 2,200 | 2,300 | 172 | 765 | 900 | 5,200 | 5,300 | 402 | 1,785 | 2,100 | | | | | |
| 2,300 | 2,400 | 180 | 799 | 940 | 5,300 | 5,400 | 409 | 1,819 | 2,140 | | | | | |
| 2,400 | 2,500 | 187 | 833 | 980 | 5,400 | 5,500 | 411 | 1,853 | 2,180 | | | | | |
| 2,500 | 2,600 | 195 | 867 | 1,020 | 5,500 | 5,600 | 411 | 1,887 | 2,220 | | | | | |
| 2,600 | 2,700 | 203 | 901 | 1,060 | 5,600 | 5,700 | 411 | 1,921 | 2,260 | | | | | |
| 2,700 | 2,800 | 210 | 935 | 1,100 | 5,700 | 5,800 | 411 | 1,955 | 2,300 | | | | | |
| 2,800 | 2,900 | 218 | 969 | 1,140 | 5,800 | 5,900 | 411 | 1,989 | 2,340 | | | | | |
| 2,900 | 3,000 | 226 | 1,003 | 1,180 | 5,900 | 6,000 | 411 | 2,023 | 2,380 | | | | | |

Use this table for lines 5 and 9 of your worksheet

For Work Credit Filers With At Least One Child Dependent

1. To find your credit, read down the "At least - But less than" columns and find the line that includes the amount you were told to look up from your work credit worksheet.

2. Then, go to the column that includes the number of child dependents who lived with you in the United States for more than half of 200X. Enter the credit from that column on your worksheet.

| If the amount you are looking up is— | Single And you have— | | Married And you have— | | If the amount you are looking up is— | Single And you have— | | Married And you have— | | If the amount you are looking up is— | Single And you have— | | Married And you have— | | | | |
|--------------------------------------|----------------------|------------------------------|-----------------------|------------------------------|--------------------------------------|----------------------|------------------------------|--------------------------|------------------------------|--------------------------------------|----------------------|------------------------------|-----------------------|------------------------------|-------|-------|-------|
| | One child dependent | Two or more child dependents | One child dependent | Two or more child dependents | | One child dependent | Two or more child dependents | One child dependent | Two or more child dependents | | One child dependent | Two or more child dependents | One child dependent | Two or more child dependents | | | |
| At least | But less than | Enter on your worksheet— | | | | At least | But less than | Enter on your worksheet— | | | | At least | But less than | Enter on your worksheet— | | | |
| 1 | 6,200 | 0 | 0 | 0 | 0 | 11,100 | 11,200 | 1,450 | 1,260 | 1,450 | 1,260 | 16,100 | 16,200 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,200 | 6,300 | 5 | 0 | 5 | 0 | 11,200 | 11,300 | 1,450 | 1,300 | 1,450 | 1,300 | 16,200 | 16,300 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,300 | 6,400 | 39 | 0 | 39 | 0 | 11,300 | 11,400 | 1,450 | 1,340 | 1,450 | 1,340 | 16,300 | 16,400 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,400 | 6,500 | 73 | 0 | 73 | 0 | 11,400 | 11,500 | 1,450 | 1,380 | 1,450 | 1,380 | 16,400 | 16,500 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,500 | 6,600 | 107 | 0 | 107 | 0 | 11,500 | 11,600 | 1,450 | 1,420 | 1,450 | 1,420 | 16,500 | 16,600 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,600 | 6,700 | 141 | 0 | 141 | 0 | 11,600 | 11,700 | 1,450 | 1,460 | 1,450 | 1,460 | 16,600 | 16,700 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,700 | 6,800 | 175 | 0 | 175 | 0 | 11,700 | 11,800 | 1,450 | 1,500 | 1,450 | 1,500 | 16,700 | 16,800 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,800 | 6,900 | 209 | 0 | 209 | 0 | 11,800 | 11,900 | 1,450 | 1,540 | 1,450 | 1,540 | 16,800 | 16,900 | 1,450 | 2,600 | 1,450 | 2,600 |
| 6,900 | 7,000 | 243 | 0 | 243 | 0 | 11,900 | 12,000 | 1,450 | 1,580 | 1,450 | 1,580 | 16,900 | 17,000 | 1,450 | 2,600 | 1,450 | 2,600 |
| 7,000 | 7,100 | 277 | 0 | 277 | 0 | 12,000 | 12,100 | 1,450 | 1,620 | 1,450 | 1,620 | 17,000 | 17,100 | 1,444 | 2,594 | 1,444 | 2,600 |
| 7,100 | 7,200 | 311 | 0 | 311 | 0 | 12,100 | 12,200 | 1,450 | 1,660 | 1,450 | 1,660 | 17,100 | 17,200 | 1,431 | 2,581 | 1,431 | 2,600 |
| 7,200 | 7,300 | 345 | 0 | 345 | 0 | 12,200 | 12,300 | 1,450 | 1,700 | 1,450 | 1,700 | 17,200 | 17,300 | 1,419 | 2,569 | 1,419 | 2,600 |
| 7,300 | 7,400 | 379 | 0 | 379 | 0 | 12,300 | 12,400 | 1,450 | 1,740 | 1,450 | 1,740 | 17,300 | 17,400 | 1,406 | 2,556 | 1,406 | 2,600 |
| 7,400 | 7,500 | 413 | 0 | 413 | 0 | 12,400 | 12,500 | 1,450 | 1,780 | 1,450 | 1,780 | 17,400 | 17,500 | 1,394 | 2,544 | 1,394 | 2,600 |
| 7,500 | 7,600 | 447 | 0 | 447 | 0 | 12,500 | 12,600 | 1,450 | 1,820 | 1,450 | 1,820 | 17,500 | 17,600 | 1,381 | 2,531 | 1,381 | 2,600 |
| 7,600 | 7,700 | 481 | 0 | 481 | 0 | 12,600 | 12,700 | 1,450 | 1,860 | 1,450 | 1,860 | 17,600 | 17,700 | 1,369 | 2,519 | 1,369 | 2,600 |
| 7,700 | 7,800 | 515 | 0 | 515 | 0 | 12,700 | 12,800 | 1,450 | 1,900 | 1,450 | 1,900 | 17,700 | 17,800 | 1,356 | 2,506 | 1,356 | 2,600 |
| 7,800 | 7,900 | 549 | 0 | 549 | 0 | 12,800 | 12,900 | 1,450 | 1,940 | 1,450 | 1,940 | 17,800 | 17,900 | 1,344 | 2,494 | 1,344 | 2,600 |
| 7,900 | 8,000 | 583 | 0 | 583 | 0 | 12,900 | 13,000 | 1,450 | 1,980 | 1,450 | 1,980 | 17,900 | 18,000 | 1,331 | 2,481 | 1,331 | 2,600 |
| 8,000 | 8,100 | 617 | 20 | 617 | 20 | 13,000 | 13,100 | 1,450 | 2,020 | 1,450 | 2,020 | 18,000 | 18,100 | 1,319 | 2,469 | 1,319 | 2,600 |
| 8,100 | 8,200 | 651 | 60 | 651 | 60 | 13,100 | 13,200 | 1,450 | 2,060 | 1,450 | 2,060 | 18,100 | 18,200 | 1,306 | 2,456 | 1,306 | 2,600 |
| 8,200 | 8,300 | 685 | 100 | 685 | 100 | 13,200 | 13,300 | 1,450 | 2,100 | 1,450 | 2,100 | 18,200 | 18,300 | 1,294 | 2,444 | 1,294 | 2,600 |
| 8,300 | 8,400 | 719 | 140 | 719 | 140 | 13,300 | 13,400 | 1,450 | 2,140 | 1,450 | 2,140 | 18,300 | 18,400 | 1,281 | 2,431 | 1,281 | 2,600 |
| 8,400 | 8,500 | 753 | 180 | 753 | 180 | 13,400 | 13,500 | 1,450 | 2,180 | 1,450 | 2,180 | 18,400 | 18,500 | 1,269 | 2,419 | 1,269 | 2,600 |
| 8,500 | 8,600 | 787 | 220 | 787 | 220 | 13,500 | 13,600 | 1,450 | 2,220 | 1,450 | 2,220 | 18,500 | 18,600 | 1,256 | 2,406 | 1,256 | 2,600 |
| 8,600 | 8,700 | 821 | 260 | 821 | 260 | 13,600 | 13,700 | 1,450 | 2,260 | 1,450 | 2,260 | 18,600 | 18,700 | 1,244 | 2,394 | 1,244 | 2,600 |
| 8,700 | 8,800 | 855 | 300 | 855 | 300 | 13,700 | 13,800 | 1,450 | 2,300 | 1,450 | 2,300 | 18,700 | 18,800 | 1,231 | 2,381 | 1,231 | 2,600 |
| 8,800 | 8,900 | 889 | 340 | 889 | 340 | 13,800 | 13,900 | 1,450 | 2,340 | 1,450 | 2,340 | 18,800 | 18,900 | 1,219 | 2,369 | 1,219 | 2,600 |
| 8,900 | 9,000 | 923 | 380 | 923 | 380 | 13,900 | 14,000 | 1,450 | 2,380 | 1,450 | 2,380 | 18,900 | 19,000 | 1,206 | 2,356 | 1,206 | 2,600 |
| 9,000 | 9,100 | 957 | 420 | 957 | 420 | 14,000 | 14,100 | 1,450 | 2,420 | 1,450 | 2,420 | 19,000 | 19,100 | 1,194 | 2,344 | 1,194 | 2,600 |
| 9,100 | 9,200 | 991 | 460 | 991 | 460 | 14,100 | 14,200 | 1,450 | 2,460 | 1,450 | 2,460 | 19,100 | 19,200 | 1,181 | 2,331 | 1,181 | 2,600 |
| 9,200 | 9,300 | 1,025 | 500 | 1,025 | 500 | 14,200 | 14,300 | 1,450 | 2,500 | 1,450 | 2,500 | 19,200 | 19,300 | 1,169 | 2,319 | 1,169 | 2,600 |
| 9,300 | 9,400 | 1,059 | 540 | 1,059 | 540 | 14,300 | 14,400 | 1,450 | 2,540 | 1,450 | 2,540 | 19,300 | 19,400 | 1,156 | 2,306 | 1,156 | 2,600 |
| 9,400 | 9,500 | 1,093 | 580 | 1,093 | 580 | 14,400 | 14,500 | 1,450 | 2,580 | 1,450 | 2,580 | 19,400 | 19,500 | 1,144 | 2,294 | 1,144 | 2,600 |
| 9,500 | 9,600 | 1,127 | 620 | 1,127 | 620 | 14,500 | 14,600 | 1,450 | 2,600 | 1,450 | 2,600 | 19,500 | 19,600 | 1,131 | 2,281 | 1,131 | 2,600 |
| 9,600 | 9,700 | 1,161 | 660 | 1,161 | 660 | 14,600 | 14,700 | 1,450 | 2,600 | 1,450 | 2,600 | 19,600 | 19,700 | 1,119 | 2,269 | 1,119 | 2,600 |
| 9,700 | 9,800 | 1,195 | 700 | 1,195 | 700 | 14,700 | 14,800 | 1,450 | 2,600 | 1,450 | 2,600 | 19,700 | 19,800 | 1,106 | 2,256 | 1,106 | 2,600 |
| 9,800 | 9,900 | 1,229 | 740 | 1,229 | 740 | 14,800 | 14,900 | 1,450 | 2,600 | 1,450 | 2,600 | 19,800 | 19,900 | 1,094 | 2,244 | 1,094 | 2,600 |
| 9,900 | 10,000 | 1,263 | 780 | 1,263 | 780 | 14,900 | 15,000 | 1,450 | 2,600 | 1,450 | 2,600 | 19,900 | 20,000 | 1,081 | 2,231 | 1,081 | 2,600 |
| 10,000 | 10,100 | 1,297 | 820 | 1,297 | 820 | 15,000 | 15,100 | 1,450 | 2,600 | 1,450 | 2,600 | 20,000 | 20,100 | 1,069 | 2,219 | 1,069 | 2,600 |
| 10,100 | 10,200 | 1,331 | 860 | 1,331 | 860 | 15,100 | 15,200 | 1,450 | 2,600 | 1,450 | 2,600 | 20,100 | 20,200 | 1,056 | 2,206 | 1,056 | 2,600 |
| 10,200 | 10,300 | 1,365 | 900 | 1,365 | 900 | 15,200 | 15,300 | 1,450 | 2,600 | 1,450 | 2,600 | 20,200 | 20,300 | 1,044 | 2,194 | 1,044 | 2,600 |
| 10,300 | 10,400 | 1,399 | 940 | 1,399 | 940 | 15,300 | 15,400 | 1,450 | 2,600 | 1,450 | 2,600 | 20,300 | 20,400 | 1,031 | 2,181 | 1,031 | 2,600 |
| 10,400 | 10,500 | 1,433 | 980 | 1,433 | 980 | 15,400 | 15,500 | 1,450 | 2,600 | 1,450 | 2,600 | 20,400 | 20,500 | 1,019 | 2,169 | 1,019 | 2,600 |
| 10,500 | 10,600 | 1,450 | 1,020 | 1,450 | 1,020 | 15,500 | 15,600 | 1,450 | 2,600 | 1,450 | 2,600 | 20,500 | 20,600 | 1,006 | 2,156 | 1,006 | 2,600 |
| 10,600 | 10,700 | 1,450 | 1,060 | 1,450 | 1,060 | 15,600 | 15,700 | 1,450 | 2,600 | 1,450 | 2,600 | 20,600 | 20,700 | 994 | 2,144 | 994 | 2,600 |
| 10,700 | 10,800 | 1,450 | 1,100 | 1,450 | 1,100 | 15,700 | 15,800 | 1,450 | 2,600 | 1,450 | 2,600 | 20,700 | 20,800 | 981 | 2,131 | 981 | 2,600 |
| 10,800 | 10,900 | 1,450 | 1,140 | 1,450 | 1,140 | 15,800 | 15,900 | 1,450 | 2,600 | 1,450 | 2,600 | 20,800 | 20,900 | 969 | 2,119 | 969 | 2,600 |
| 10,900 | 11,000 | 1,450 | 1,180 | 1,450 | 1,180 | 15,900 | 16,000 | 1,450 | 2,600 | 1,450 | 2,600 | 20,900 | 21,000 | 956 | 2,106 | 956 | 2,600 |
| 11,000 | 11,100 | 1,450 | 1,220 | 1,450 | 1,220 | 16,000 | 16,100 | 1,450 | 2,600 | 1,450 | 2,600 | 21,000 | 21,100 | 944 | 2,094 | 944 | 2,594 |

(continued on next page)

Use this table for lines 5 and 9 of your worksheet (Continued)

| If the amount you are looking up is— | Single And you have— | | Married And you have— | | If the amount you are looking up is— | Single And you have— | | Married And you have— | | If the amount you are looking up is— | Single And you have— | | Married And you have— | | | | |
|--------------------------------------|----------------------|------------------------------|-----------------------|------------------------------|--------------------------------------|----------------------|------------------------------|--------------------------|------------------------------|--------------------------------------|----------------------|------------------------------|-----------------------|------------------------------|---|---|-----|
| | One child dependent | Two or more child dependents | One child dependent | Two or more child dependents | | One child dependent | Two or more child dependents | One child dependent | Two or more child dependents | | One child dependent | Two or more child dependents | One child dependent | Two or more child dependents | | | |
| At least | But less than | Enter on your worksheet— | | | | At least | But less than | Enter on your worksheet— | | | | At least | But less than | Enter on your worksheet— | | | |
| 37,600 | 37,700 | 0 | 19 | 0 | 519 | 39,100 | 39,200 | 0 | 0 | 0 | 331 | 40,600 | 40,700 | 0 | 0 | 0 | 144 |
| 37,700 | 37,800 | 0 | 6 | 0 | 506 | 39,200 | 39,300 | 0 | 0 | 0 | 319 | 40,700 | 40,800 | 0 | 0 | 0 | 131 |
| 37,800 | 37,900 | 0 | 0 | 0 | 494 | 39,300 | 39,400 | 0 | 0 | 0 | 306 | 40,800 | 40,900 | 0 | 0 | 0 | 119 |
| 37,900 | 38,000 | 0 | 0 | 0 | 481 | 39,400 | 39,500 | 0 | 0 | 0 | 294 | 40,900 | 41,000 | 0 | 0 | 0 | 106 |
| 38,000 | 38,100 | 0 | 0 | 0 | 469 | 39,500 | 39,600 | 0 | 0 | 0 | 281 | 41,000 | 41,100 | 0 | 0 | 0 | 94 |
| 38,100 | 38,200 | 0 | 0 | 0 | 456 | 39,600 | 39,700 | 0 | 0 | 0 | 269 | 41,100 | 41,200 | 0 | 0 | 0 | 81 |
| 38,200 | 38,300 | 0 | 0 | | | | | | | | | | | | | | |

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