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The Impact of Speaker Boehner's Millionaire Tax

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In the most recent twist of the fiscal cliff negotiations, Speaker Boehner has offered to allow the Bush tax cuts to expire for millionaires, meaning in this case those earning literally one million dollars or more in adjusted gross income. Speaker Boehner intends to put the bill to a vote in the House today, December 20, 2012. It is unclear if the votes are there, but perhaps many are persuaded by the idea that this tax increase would help pay down the debt. But, as the president has noted, there just isn't enough money there to make much of a dent. For instance, if all of the income of millionaires were confiscated, it would only cover about 60 percent of this year's deficit.[1] And after doing that, millionaires would disappear completely.

The most unfortunate thing is that this debate is happening in static terms and is not taking into account the negative effects on the economy.[2] Our model simulations indicate such a tax increase would in fact have large negative effects on the economy which are not at all isolated to millionaires. We find this tax increase would reduce GDP by 0.92 percent, reduce business stocks by 2.41 percent, wages by 0.72 percent, and hours worked by 0.25 percent. All of this would reduce the actual (dynamic) tax revenue that might be raised to $7.1 billion per year, and this does not take into account the income shifting that would certainly occur, e.g., the under-reporting of millionaire income, especially as they react to the tax increase by taking fewer capital gains and avoiding dividends. As it is, this dynamic revenue represents less than 1 percent of the deficit. It is also a far cry from the static revenue estimate of $40.1 billion per year. For each dollar of dynamic revenue raised, this tax increase would reduce GDP by more than $20 dollars (see Table 1).

The tax increase would hit millionaires the hardest, even taking into account the economic effects on the rest of the economy. It would reduce millionaire's average after-tax income by 4.5 percent. However, it would reduce the average after-tax incomes of all other income groups as well, though by a smaller amount of between 0.8 and 1 percent. Overall, it would reduce the average taxpayer's after-tax income by 1.3 percent (see Table 2).

[1] Scott Hodge & William McBride, *Putting a Face on America's Tax Returns: A Chart Book*, Chart 29 (Sept. 24, 2012), http://taxfoundation.org/article/putting-face-americas-tax-returns-chart-29.
[2] This is facilitated by government score keepers, particularly the Joint Committee on Taxation. *See* Joint Committee on Taxation, *Estimated Effects of An Amendment to the Senate Amendment to H.J. Res. 66,the "Permanent Tax Relief for Families and Small Businesses Act of 2012,"* (Dec. 19, 2012), http://waysandmeans.house.gov/uploadedfiles/jcx7812.pdf.

The Bill and How We Model It

Press reports[3] and legislative language[4] indicate the bill would:

1) Raise the top marginal rate on adjusted gross income (AGI) above $1 million, from the current rate of 35 percent to 39.6 percent.[5]
2) Raise the top rate on long-term capital gains and dividends earned by those with AGI above $1 million, from the current rate of 15 percent to 20 percent. The additional 3.8 percent tax on shareholders earning above $250,000 that is already law and set to go into effect January 1, 2013 would remain intact.
3) Permanently eliminate PEP and Pease phase outs of personal exemptions and deductions for high-income earners.
4) Extend Section 179 expensing for small business, allowing them to immediately expense the first $250,000 in investment.[6]
5) Extend current estate tax policy.
6) "Patch" the alternative minimum tax by maintaining the current exemption.

We use a tax calculator and a neo-classical growth model which accounts for how tax policy impacts the supply of capital and labor. For a full description of how the model works, see the Appendices in our earlier publications modeling President Obama's tax plan[7] and the fiscal cliff.[8]

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[3] Paul Kane & Rosalind S. Helderman, *'Cliff' standoff: Boehner works to wrangle votes for 'Plan B'; Obama threatens veto*, WASHINGTON POST, Dec. 19, 2012, http://www.washingtonpost.com/business/fiscal-cliff/obama-would-veto-boehners-plan-b-white-house-says/2012/12/19/5d49ef20-49f3-11e2-ad54-580638ede391_story.html?hpid=z3. *See also What's on the table now in 'fiscal cliff' talks*, YAHOO! FINANCE, Dec. 20, 2012, http://finance.yahoo.com/news/whats-table-now-fiscal-cliff-184340430.html; Office of the Speaker of the House, *What's in the "Plan B" Bill? Tax Relief for Nearly Every Taxpayer*, Dec. 18, 2012, http://www.speaker.gov/general/what-s-plan-b-bill-tax-relief-nearly-every-taxpayer.

[4] House of Representatives, Rules Committee, *Amendment to the Senate Amendment to H.J. Res. 66*, http://www.rules.house.gov/Media/file/PDF_112_2/LegislativeText/BILLS-112hjres66-HAmdt2.pdf.

[5] We assume a $1 million threshold for all filers, not $1 million for joint filers and $800 thousand for singles, which would be more in keeping with historical conventions.

[6] This slightly lowers the service price of capital, growing the capital stock by about $3 billion out of a total capital stock of about $30 trillion.

[7] Stephen Entin, *Simulating the Economic Effects of Obama's Tax Plan*, TAX FOUNDATION FISCAL FACT NO. 339 (Nov. 1, 2012), http://taxfoundation.org/article/simulating-economic-effects-obamas-tax-plan.

[8] Stephen Entin, *Diving Off the Fiscal Cliff: An Economy on the Rocks*, TAX FOUNDATION SPECIAL REPORT NO. 205 (Nov. 27, 2012), http://taxfoundation.org/article/diving-fiscal-cliff-economy-rocks.

Model Results

Table 1: Impact of Speaker Boehner's Millionaire Tax
(Dollar figures in billions of 2012 dollars except as noted)

Changes in:	
GDP	-0.92%
Private business GDP	-0.96%
Private business stocks	-2.41%
Wage rate	-0.72%
Private business hours of work	-0.25%
Federal revenue (dynamic)	$7.1
Federal spending	-$5.2
Federal deficit (+ = lower deficit)	$12.3
Static revenue estimate	$40.1
% Revenue reflow vs. dynamic	-82.2%
$GDP	-$145.1
$GDP/$tax increase	-20.4
Weighted Average Service Price	
Corporate	1.78%
Non-corporate	1.02%
All business	1.48%

Table 2: Distribution of Changes to After-tax Income

	Average after-tax income per return			
Adjusted Gross Income Class	**Static Change**	**Static % Change**	**Dynamic Change**	**Dynamic % Change**
< $0	-$1	0.00%	$908	n.a.
$0 - $5,000	$0	0.00%	-$26	-0.87%
$5,000 - $10,000	$0	0.00%	-$74	-0.84%
$10,000 - $20,000	$0	0.00%	-$143	-0.84%
$20,000 - $30,000	$0	0.00%	-$231	-0.86%
$30,000 - $40,000	$0	0.00%	-$315	-0.87%
$40,000 - $50,000	$0	0.00%	-$388	-0.84%
$50,000 - $75,000	$0	0.00%	-$518	-0.84%
$75,000 - $100,000	$0	0.00%	-$713	-0.83%
$100,000 - $150,000	$0	0.00%	-$922	-0.79%
$150,000 - $200,000	$0	0.00%	-$1,292	-0.81%
$200,000 - $250,000	$0	0.00%	-$1,621	-0.80%
$250,000 - $500,000	-$1	0.00%	-$2,406	-0.82%
$500,000 - $1,000,000	-$114	-0.02%	-$5,039	-0.88%
> $1,000,000	-$102,721	-3.67%	-$126,339	-4.51%
Total for All	**-$248**	**-0.46%**	**-$692**	**-1.29%**

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