

Would the Lee-Rubio Tax Plan Help Lower-Income Households?

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Since the roll-out of the Lee-Rubio tax proposal in March 2015, the Center on Budget and Policy Priorities and the Tax Foundation have disagreed whether the plan would benefit people at all lower income levels.¹ The short answer is: It depends.



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The Tax Foundation found that, on average, taxpayers in every income group would have higher after-tax incomes under Lee-Rubio, particularly low-income earners. However, the Center on Budget and Policy Priorities argues that if the current child tax credit were eliminated, the Lee-Rubio plan would reduce the after-tax income of minimum-wage income earners.

The Lee-Rubio plan is short on details regarding several provisions that could make a significant difference, particularly for those between poverty and the middle class. Overall, though, low-income taxpayers will be better off under Lee-Rubio if Congress continues existing tax credits that are not discussed in the proposal, such as the earned income tax credit (EITC) and the additional child tax credit.

Eliminating Exemptions. The Lee-Rubio plan would eliminate the standard deduction — the amount taxpayers are allowed to subtract from their taxable incomes if they do not itemize. Also, under the Lee-Rubio plan there would no longer be a personal exemption; nor could taxpayers file a return under a “head-of-household” classification, which currently has a higher deductible than “single” status.

The senators’ white paper on the tax proposal does not say whether dependent exemptions are also eliminated; under current law, these are worth up to \$4,000 per child or other dependent relative.² This could be particularly problematic for low-income households because all of their gross income would be taxable, and Lee-Rubio increases the tax rate for the lowest earners from 10 percent to 15 percent. The Tax Foundation’s analysis assumes that all exemptions, including the dependent exemption, would be eliminated.³

New Personal Tax Credit. In lieu of the personal exemption, the Lee-Rubio plan provides a \$2,000 personal

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Table I		
Single Individual With No Children		
	2015 Tax Law	Lee-Rubio
Income	\$12,000	\$12,000
Deductions	(6,300)	0
Exemptions	<u>(4,000)</u>	<u>0</u>
Taxable Income	1,700	12,000
Tax rate	<u>x 10%</u>	<u>x 15%</u>
Income Tax	\$ 170	\$ 1,800
Personal Credit	N/A	(2,000)
EITC (est.)	<u>(196)</u>	<u>(196)</u>
Net Tax Liability	\$ (26)	\$ (396)

Source: Author's calculations.

Compared to the current tax code, replacing the standard deduction and personal exemption with a personal credit would increase refunds to individuals with, say, \$12,000 of annual income. Indeed, under the Lee-Rubio plan, the refund for a single individual earning \$12,000 a year would increase by a few hundred dollars [see Table I].

New Child Tax Credit. One of the primary ways Lee-Rubio claims to assist low-income families is through the addition of a new \$2,500 child tax credit (CTC), which would be in addition to the current child tax credit and the earned income tax credit. The white paper indicates that the new credit is “charged last,” after all other tax credits, and is partially refundable up to the sum of income and payroll taxes paid by an individual and his employer on the tax filer’s behalf. The “charged last” portion likely means that the new child tax credit will only be refunded

credit, or \$4,000 credit for married couples. While a deduction reduces taxable income, a credit is subtracted from the amount of taxes owed.

How much better off households are depends on whether or not the personal credit would be refundable if the tax credit exceeds an individual’s tax obligations. This is an issue the senators’ white paper does not specifically address. The Tax Foundation assumed that it is fully refundable, based on conversations with members of Lee’s and Rubio’s staffs, according to Michael Schuyler and Kyle Pomerleau.⁴ The calculations below adopt the same assumption. (The Tax Foundation also assumes that the credit would be “revenue neutral,” which would put the credit closer to \$1,750 for individuals and \$3,500 for married couples.⁵ The calculations below, however, assume the full \$2,000 credit stated in the Lee-Rubio plan.)

Table II		
Single Head of Household with One Child		
	2015 Tax Law	Lee-Rubio
Income	\$12,000	\$12,000
Deductions	(9,250)	0
Exemptions	<u>(8,000)</u>	<u>0</u>
Taxable Income	\$ 0	\$12,000
Tax rate		<u>x 15%</u>
Income Tax	\$ 0	\$ 1,800
Personal Credit	N/A	(2,000)
EITC (est.)	(3,305)	(3,305)
Current Child Tax Credit	<u>(1,000)</u>	<u>(1,000)</u>
Lee-Rubio CTC	N/A	0
Net Tax Liability	\$(4,305)	\$(4,505)

Source: Author's calculations.

Table III

Married Couple One Child

	2015 Tax Law	Lee-Rubio
Total Income	\$25,000	\$25,000
Deductions	(12,600)	0
Exemptions	<u>(12,000)</u>	<u>0</u>
Taxable Income	400	25,000
Tax rate	<u>x 10%</u>	<u>x 15%</u>
Income Tax	\$ 40	\$ 3,750
Personal Credit	N/A	(4,000)
EITC (est.)	(3,137)	(3,137)
Current Child Tax Credit	<u>(1,000)</u>	<u>(1,000)</u>
Net Tax Liability	\$(4,097)	\$ (4,387)
Lee-Rubio CTC	N/A	<u>0</u>
Net Tax Liability After LR-CTC	N/A	\$ (4,387)

Source: Author's calculations.

Similarly, the new credit would not be available to some lower-income married couples [see Tables III and IV]:

- A married couple with one child earning \$25,000 and filing jointly would not receive the new child tax credit at all; however, they would still be better off than current law due to the personal credit.
- A higher-earning couple with a \$40,000 income, however, would receive the full child tax credit (\$2,000).

A Benefit that Increases with Income. For taxpayers with children approaching middle class incomes, the new child tax credit could help lower their effective tax rates. While the EITC and other means-tested benefits phase out as income rises, this credit would offset that loss. Since filers with lower-incomes could probably claim more of the new child tax credit as their incomes rose, this could moderate the current tax disincentive for additional work and saving.

to the extent it *exceeds* the refund a tax filer would receive under existing tax credits.

For example, if the amount of income and payroll taxes paid is \$4,000, but the taxpayer already receives a \$3,500 refund due to the current child tax credit and earned income tax credit, the new credit would only add an additional \$500 refund rather than the full \$2,500. If this is the case, there would be only a small number of low-income taxpayers, in a narrow income range, who would receive the new child tax credit, and many of them would only receive a portion of it. Thus, a single parent earning \$12,000 a year with one child would likely not receive the new Child Tax Credit at all, assuming that the EITC and the current law child tax credit are still in place [see Table II]. However, they would still be better off by about \$200 under this plan, due to the personal credit.

Table IV

Married Couple One Child

	2015 Tax Law	Lee-Rubio
Total Income	\$40,000	\$40,000
Deductions	(12,600)	0
Exemptions	<u>(12,000)</u>	<u>0</u>
Taxable Income	\$15,400	\$40,000
Tax rate	<u>x 10%</u>	<u>x 15%</u>
Income Tax	\$ 1,540	\$ 6,000
Personal Credit	N/A	4,000
EITC (est.)	(740)	(740)
Current CTC	<u>(1,000)</u>	<u>(1,000)</u>
Net Tax Liability	\$ (200)	\$ 260
Lee-Rubio CTC	N/A	<u>(2,500)</u>
Net Tax Liability After LR-CTC	N/A	\$(2,240)

Source: Author's calculations.

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Conclusion. The Lee-Rubio tax proposal does not address the existing child tax credit or the EITC, which would likely be calculated differently than the examples used in this paper. In general, however, the Lee-Rubio plan appears to give lower- and middle-class taxpayers a break while simplifying the tax-filing system.

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Notes

1. Michael Schuyler and William McBride, “The Economic Effects of the Rubio-Lee Tax Reform Plan,” Tax Foundation, March 9, 2015, available at <http://taxfoundation.org/article/economic-effects-rubio-lee-tax-reform-plan>; and Chuck Marr, “Lee-Rubio Tax Plan Heavily Tilted Toward Top, Contrary to Tax Foundation Claims,” Center for Budget and Policy Priorities, Off the Charts, March 11, 2015, available at <http://www.cbpp.org/blog/lee-rubio-tax-plan-heavily-tilted-toward-top-contrary-to-tax-foundation-claims>.
2. Mike Lee and Marco Rubio, “Economic Growth and Family Fairness Tax Reform Plan,” United States Senate, 2015. Available at http://www.rubio.senate.gov/public/index.cfm/files/serve/?File_id=2d839ff1-f995-427a-86e9-267365609942.
3. Michael Schuyler and William McBride, “The Economic Effects of the Rubio-Lee Tax Reform Plan,” Tax Foundation, March 9, 2015. Available at <http://taxfoundation.org/article/economic-effects-rubio-lee-tax-reform-plan>.
4. The author spoke with Michael Schuyler and Kyle Pomerleau of the Tax Foundation.
5. Schuyler and McBride, 2015.