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Floor Statement of Senator Chuck Grassley
Proposals to Restore Hidden Marginal Tax Rate Increases on Working Families
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As the upcoming presidential election approaches, we are learning more about the changes each of the major candidates would make to the tax system. Most of the attention in this regard is going to issues such as income tax rates, corporate tax rates, and the Alternative Minimum Tax. These are very important parts of our tax code and do deserve the attention they are getting. However, there are many lesser known parts of the tax code. Changes made in these areas can still make big differences in what citizens pay to the government every year.

I am here to discuss the “PEASE” limit, which is the overall limitation on itemized deductions, and “PEP”, the phase-out of personal exemptions.

“PEP” and “PEASE” were originally enacted by a Democratic Congress as a way to evade the first President Bush’s refusal to raise the top statutory tax rates. By phasing out personal exemption and itemized deductions for upper income taxpayers, the Democratic Congress was able to enact a “back door” tax increase. However, in 2001, Congress reduced “PEP” and “PEASE” in order to reduce taxpayer confusion and minimize inequalities based on a taxpayer’s understanding of the law. This bipartisan simplification was done at the recommendation of the non-partisan Joint Committee on Taxation.

Despite this, those who see more government spending as the solution to all problems are desperate to seize more money from the American taxpayer.

The Junior Senator from Illinois would need more money to fund all of the promises he is making. Restoring the phase-outs for itemized deductions and personal exemptions seems a likely source for some of that money. In discussing the tax proposals of the likely Democratic nominee, I am referring to a publication titled, “A Preliminary Analysis of the 2008 Presidential Candidates’ Tax Plans” prepared by the Tax Policy Center. The Tax Policy Center is a joint venture of the Urban Institute and Brookings Institution.

According to this publication, my distinguished colleague from Illinois would restore “PEP” and “PEASE.” That is, he would restore the phase-outs and the complexity they would mean for millions of taxpaying families. However, it is also noted that he would set an income threshold of

\$250,000 for married couples filing jointly. This is consistent with the candidate's stated goal of targeting tax breaks to low and middle income taxpayers while shifting more of the tax burden onto higher income taxpayers.

If your family makes less than \$250,000 a year, you might think this sounds like a good deal. For you singles, the threshold for the phase-out of personal exemptions would probably be lower but the phase-out of itemized deductions would not vary with filing status if current law is followed. As an aside, the distinguished Junior Senator from Illinois' proposal would create a new marriage penalty. For those considered by the Senator from Illinois to be low and middle income taxpayers, the idea of raising taxes on other people might sound like a good idea, but hold on.

On March 14, of this year this body approved a budget with 51 votes. One of those 51 "yea" votes was cast by a presidential candidate from Illinois. That same Senator voted again for the budget on June 4 when the Senate voted on the conference report. I'm not sure if he is not communicating with the rest of the Democratic caucus, or was too busy campaigning to become completely familiar with the budget, but he is making promises that the budget he voted for will not allow.

The budget passed by Congress earlier this year would protect taxpayers in the 10% and 15% brackets but would subject filers in the 25% bracket and above to "PEP" and "PEASE." To get an idea of what this means, I want to walk through the 25% bracket, the 28% bracket, and the 33% bracket. These particular brackets are important because they contain families with less than \$250,000 in income and singles with less than \$125,000 in annual income. It has been implied that the Junior Senator from Illinois would protect these filers from tax increases as President. Restoring "PEP" and "PEASE" within the confines of this year's budget resolution would subject filers in these tax brackets to a back door tax increase. The senator from Illinois may say he is going to protect families earning less than \$250,000 a year, but the budget he voted for will not do that.

According to the IRS, single individuals falling within the 25% bracket in 2008 start at taxable income of more than \$32,550. They earn taxable income of no more than \$78,850. Singles in the 28% bracket will earn taxable income of more than \$78,850 but less than \$164,550. The really important number here is \$125,000, in that many filers in the 25% and 28% brackets make less than that. Based on the Democratic budget, these taxpayers would be hit with "PEP" and "PEASE."

Now looking at brackets for married filers filing jointly for the 2008 tax year; according to the IRS, married filers in the 25% bracket will start at taxable income of more than \$65,100. Taxpayers in this bracket will earn taxable income of no more than \$131,450 annually. In the 28% bracket they will earn taxable income of no more than \$200,300.

For the 33% bracket married filers filing jointly will earn no more than \$357,700, but more than \$200,300. For married individual filing jointly, the important number is \$250,000. Those of you in the tax brackets I have walked through may expect the senator from Illinois to protect you from a tax increase if he is elected President, but the budget he voted for earlier this year makes that impossible.

As I said, the reinstatement of “PEP” and “PEASE” amounts to a back door tax increase. I say back door because it increases the effective rate for many filers without increasing the statutory tax rate. For a family of four, this back door tax increase would be significant. If your family falls in the 25% tax bracket, according to Finance Committee Republican staff analysis from March, 2001, “PEP” and “PEASE” could make your actual rate 26%.

The news is even worse for filers in the 28% and 33% brackets. In the 28% bracket a family of four could pay a real rate of 32%.

A family in the 33% brackets a family of four could pay a real rate of 37%.

I want to end by stating that I believe that taxes are a necessary part of life. We all benefit from the services our government provides and that government needs money to function. We collect that money with taxes. However, I think our tax system should be transparent and honest. Raising money by limiting personal exemptions and itemized deductions is not transparent, and, as I have said, amounts to a back door tax increase.

If anyone thinks people should hand over a greater percentage of their income to the government, that person should openly advocate increasing statutory tax rates. I’m also concerned that many people out there may be relying on the Junior Senator from Illinois’ latest campaign position. His latest campaign position says he intends to protect low and middle income filers from a tax increase. Right now he is at odds with his own party and with a budget he voted for.

I bet that being subjected to a back door tax increase is not the sort of change that most Americans believe in, to say nothing of restoring what the non-partisan Joint Committee on Taxation stated was a very serious source of complexity for millions of American taxpaying families.

I yield the floor.