



UNITED STATES  
**DEPARTMENT OF  
THE TREASURY**



# TAX RELIEF KIT

U.S. DEPARTMENT OF TREASURY, OFFICE OF TAX POLICY

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## **MILLIONS OF AMERICAN FAMILIES ARE BENEFITING FROM TAX RELIEF**

As a result of the President's Economic Growth and Tax Relief Reconciliation Act of 2001, the Jobs and Growth Tax Relief Reconciliation Act of 2003, and the Working Families Tax Relief Act of 2004 every taxpayer who paid income taxes will get tax relief this year.

- 111 million taxpayers will see their taxes decline by an average of \$1,877.
- A family of four earning \$40,000 will receive tax relief of \$2,010.
- Over 5 million individuals and families will see their income tax liabilities completely eliminated.
- 44 million families with children will receive an average tax cut of \$2,493.
- 14 million elderly individuals will receive an average of \$2,043.
- 25 million small business owners will save an average of \$3,641.
- Low-income families will also benefit from provisions that make the child credit refundable for more families and reduce marriage penalties.

President Bush has called on Congress to act now to prevent tax increases. If Congress does not act, failure to extend these tax cuts permanently would raise taxes on American taxpayers in future years.

- In 2008, the small business expensing limit will shrink from \$100,000 to just \$25,000, increasing the cost of capital investments for America's small businesses;
- In 2009, the top tax rate on dividends will increase from 15 to 35 percent, while the tax on capital gains will climb from 15 to 20 percent, raising the tax burden on retirees and families investing for their future; and
- In 2011, the tax rate relief, the new 10-percent tax bracket, death tax repeal, marriage penalty relief, and all the remaining tax relief enacted over the past few years will sunset, resulting in tax increases for every individual American man or woman who pays income taxes.

The economy is stronger today because of the timely tax relief measures enacted during President Bush's administration. The success of the President's economic program, including tax relief, can be seen throughout the economy.

- Economic growth has averaged more than 3.7 percent since the end of 2002.
- The economy has generated 2 million net new jobs in the year ending December 2005, and almost 5 million since May 2003, when the last tax relief package was enacted.
- At 4.8 percent, the unemployment rate remains below its average of the 1970s, 1980s, and 1990s.
- Real, after-tax incomes are 14 percent higher since December 2000.
- Led by strong home values and a steadily rising stock market, household wealth is at an all-time high.
- Homeownership remains very close to its all-time high of more than 69 percent reached in early 2005.



## TAX RELIEF ENCOURAGES INVESTMENT

The President’s tax cuts have reduced the marginal effective tax rate (METR) on new investment, which is measured as the share of an investment’s economic income needed to cover taxes over its lifetime. Lower METRs encourage additional investment, capital accumulation, and, in the long-term, higher living standards.

As shown in the table below, reductions in personal income tax rates (including the tax rates on dividends and capital gains) enacted in 2001 and 2003 have reduced the METR in the corporate sector by 15.5 percent and in the overall economy by 17.4 percent.

The temporary bonus depreciation provision enacted in 2001 and expanded in 2003 to 50% provided a potent short-term investment stimulus. Before expiring at the end of 2004, this provision lowered by one-half or more the METR on qualifying investment.

### Effect of President's tax cuts on the marginal effective tax rate on new investment

	Business Sector			Owner-Occupied Housing	Economy-wide
	Corporate	Noncorporate	Total		
Without tax relief	33.0	20.6	28.0	-2.7	17.2
With tax relief*	27.9	17.5	23.6	-2.0	14.2
% Change	-15.5	-15.0	-15.7	25.9	-17.4

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

\* Includes the effects of the lower regular tax rates and lower tax rates on dividends and capital gains income, but not the temporary 50 bonus depreciation provision.

### Leveling the Playing Field

Taxing income from alternative investments at a more uniform METR – “leveling the playing field” – promotes efficient allocation of resources within the economy by allowing market fundamentals, rather than taxes, to guide financing and investment decisions.

By lowering the tax rate on dividends and capital gains, the 2003 Tax Act *increased* tax uniformity by substantially reducing the METR on income from corporate equity financed investment, relative to other sources of capital income, such as debt and noncorporate income.

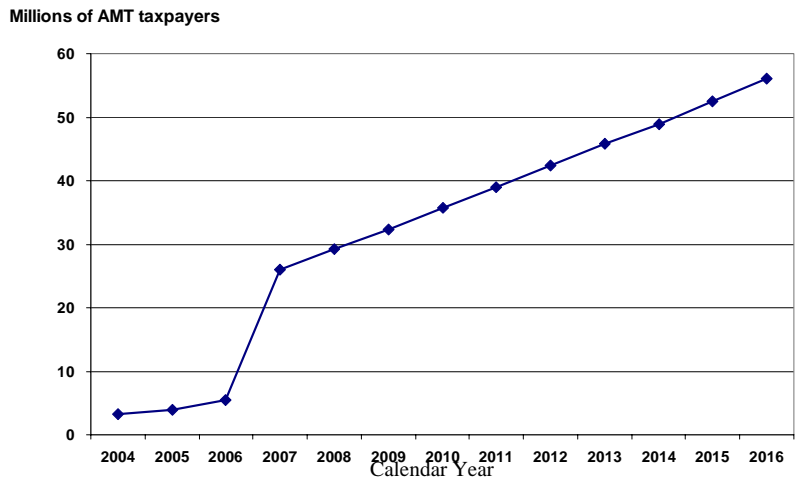


## THE TOLL OF TWO TAXES: THE REGULAR INCOME TAX AND THE AMT

The alternative minimum tax (AMT) is a second income tax system that runs parallel to the regular individual income tax. First enacted in the late 1960's, the AMT was intended to target a small group of high-income individuals – who had managed to avoid all taxes – to ensure they paid a minimum amount of tax. Changes since the AMT's original enactment mean that today it reaches into the ranks of the middle class, potentially denying them the benefit of many of the deductions, credits, and lower tax rates available under the regular income tax system. The AMT also significantly increases the complexity of tax filing for taxpayers subject to the AMT and for millions of additional taxpayers who must complete AMT forms to determine they are not subject to the AMT.

Left unchanged, the AMT will affect increasing numbers of taxpayers. As can be seen in the graph to the right, assuming the 2001 and 2003 tax cuts are made permanent and the temporary AMT provisions are extended through 2006, the number of taxpayers with increased taxes due to the AMT will increase from 5.5 million in 2006 to 25.9 million in 2007 and to 56.1 million in 2016.

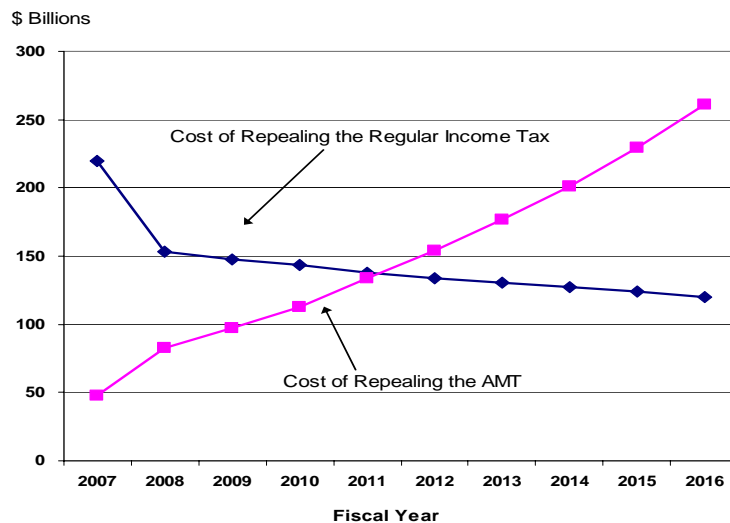
**Number of Individual AMT Taxpayers**  
(Assumes the '01 and '03 tax relief is permanently extended and the temporary AMT provisions are extended through 2006)



The cost of addressing the AMT will also grow rapidly. Assuming the 2001 and 2003 tax cuts are made permanent and the temporary AMT provisions are extended through 2006, in 2007 the AMT will increase the amount of tax individuals pay by \$48B, rising to \$261B in 2016.

The graph shows that by 2012 less revenue would be lost from repealing the regular income tax than from repealing the AMT.

**Cost of Repealing Regular Income Tax vs. Cost of Repealing the AMT**  
(Assumes the '01 and '03 tax relief is permanently extended and the temporary AMT provisions are extended through 2006)





## WHO PAYS MOST INDIVIDUAL INCOME TAXES?

The individual income tax is highly progressive - a small group of higher-income taxpayers pay most of the individual income taxes each year.

- In 2003, the latest year of available data, the top 5 percent of taxpayers paid more than one-half (54.4 percent) of all individual income taxes, but reported roughly one-third (31.2 percent) of income.
- The top 1 percent of taxpayers paid 34.3 percent of all individual incomes taxes in 2003. This group of taxpayers has paid more than 30 percent of individual income taxes since 1995. Moreover, since 1990 this group's tax share has grown *faster* than their income share.
- Taxpayers who rank in the top 50 percent of taxpayers by income pay virtually all individual income taxes. In all years since 1990, taxpayers in this group have paid over 90 percent of all individual income taxes. In 2000, 2001, 2002, and 2003, this group paid over 96 percent of the total.

<b>Share of Individual Income Taxes and Income, 1990-2003</b>						
Share of Individual Income Taxes [Share of Adjusted Gross Income]						
	Top 1%	Top 5%	Top 10%	Top 25%	Top 50%	Bottom 50%
2003	34.3 [16.8]	54.4 [31.2]	65.8 [42.4]	83.9 [64.9]	96.5 [86.0]	3.5 [14.0]
2000	37.4 [20.8]	56.5 [35.3]	67.3 [46.0]	84.0 [67.2]	96.1 [87.0]	3.9 [13.0]
1995	30.3 [14.6]	48.9 [28.8]	60.8 [40.2]	80.4 [63.4]	95.4 [85.5]	4.6 [14.5]
1990	25.1 [14.0]	43.6 [27.6]	55.4 [38.8]	77.0 [62.1]	94.2 [85.0]	5.8 [15.0]

Source: Internal Revenue Service. Percentiles based on adjusted gross income.

The President's tax cuts have shifted a larger share of the individual income taxes paid to higher income taxpayers. In 2006, with nearly all of the tax cut provisions fully in effect (e.g., lower tax rates, the \$1,000 child credit, marriage penalty relief), the projected tax share for lower-income taxpayers will *fall*, while the tax share for higher-income taxpayers will *rise*.

- The share of taxes paid by the bottom 50 percent of taxpayers will fall from 4.0 to 3.4 percent.
- The share of taxes paid by the top 1 percent of taxpayers will rise from 32.3 percent to 32.4 percent.
- The average tax rate for the bottom 50 percent of taxpayers falls by 27 percent as compared to a 14 percent decline for taxpayers in the top 1 percent.

<b>Projected Share of Individual Income Taxes and Income in 2006</b>						
Share of Individual Income Taxes <sup>1</sup> [Share of Adjusted Gross Income]						
	Top 1%	Top 5%	Top 10%	Top 25%	Top 50%	Bottom 50%
With Tax Cuts	32.4 [17.2]	53.3 [31.6]	65.7 [42.9]	84.1 [65.4]	96.6 [86.6]	3.4 [13.4]
Without Tax Cuts	32.3 [17.2]	51.6 [31.6]	63.6 [42.9]	82.6 [65.4]	96.0 [86.6]	4.0 [13.4]

Source: U.S. Department of Treasury, Office of Tax Analysis.  
<sup>1</sup>Estimates of tax paid ignore any behavioral responses to the tax cuts.  
 NOTE: Percentile groups begin at income of: Top 50% \$33,705; Top 25% \$66,961; Top 10% \$111,528; Top 5% \$151,708; Top 1% \$341,773.



## **FISCAL YEAR 2007 BUDGET INITIATIVE: DIVISION ON DYNAMIC ANALYSIS OFFICE OF TAX POLICY**

- As part of the rollout of the FY07 Budget, the Treasury Department is announcing its further development of its capability for dynamic analysis of tax policy changes.
- Dynamic analysis, which incorporates the full gamut of behavioral responses, including how tax policy changes affect total output, has the advantage of emphasizing the economic benefits of many of the President's tax policy initiatives.
- Dynamic analysis will also help frame the public dialogue on tax reform by highlighting its economic benefits. This type of analysis is already being done by the Joint Committee on Taxation and the Congressional Budget Office.
- The President's FY07 Budget includes a budget item to establish a dynamic analysis division within the Office of Tax Analysis (OTA) at the Treasury Department. Treasury would hire a director and several staff for the division. Treasury anticipates that it will conduct a dynamic analysis of the tax proposals included in the President's Budget for the Mid-Session Review (in July).
- What is Dynamic Analysis? In analyzing the revenue effect of potential tax policy changes, Treasury routinely considers how taxpayers might respond to the changes, but does not consider how the overall economy might be affected in its official scoring of tax proposals. In analyzing a reduction in marginal tax rates, for example, Treasury considers that workers would take more of their income in the form of taxable wages and salaries, but not how the tax reduction might increase workers' total compensation or the overall size of the economy.

Ignoring such macroeconomic impacts is not a problem when potential tax changes are relatively small. Large-scale tax reform, however, could have significant macro-economic effects, so it is important to supplement the traditional approach with fully dynamic analyses that consider how tax changes affect the overall level of resources employed in the economy and the efficiency with which those resources are employed.

- How does Dynamic Analysis differ from Dynamic Scoring? Dynamic analysis evaluates proposals to see how they would alter the overall level of economic activity. Dynamic scoring, by contrast, would take this a step further by estimating how the higher level of economic activity could translate into higher tax receipts.

Under the current proposal, Treasury would commit to conducting dynamic analysis of major tax policy changes, but not to dynamic scoring. It is envisioned that dynamic analysis eventually might evolve into dynamic scoring as the models become more sophisticated and the approach becomes more widely accepted. Treasury plans to continue to rely on their traditional approach for "official" estimates of the revenue effect of the tax proposals, and to present dynamic analyses as supplemental information.



**State-by-State Estimates of the Cumulative Effect of the President's Tax Cuts, 2001 through 2005  
(EGTRRA (2001), JCWAA (2002), JGTRRA (2003), WFTRA (2004) and AJCA (2004))**

(Billions of Dollars)

		<b>United States</b>	-882.7		
<b>Alabama</b>	-10.5	<b>Massachusetts</b>	-25.0	<b>South Dakota</b>	-2.0
<b>Alaska</b>	-2.1	<b>Michigan</b>	-29.2	<b>Tennessee</b>	-14.7
<b>Arizona</b>	-14.8	<b>Minnesota</b>	-16.6	<b>Texas</b>	-56.7
<b>Arkansas</b>	-5.9	<b>Mississippi</b>	-5.4	<b>Utah</b>	-5.9
<b>California</b>	-114.0	<b>Missouri</b>	-15.7	<b>Vermont</b>	-1.9
<b>Colorado</b>	-14.7	<b>Montana</b>	-2.4	<b>Virginia</b>	-24.6
<b>Connecticut</b>	-16.1	<b>Nebraska</b>	-4.9	<b>Washington</b>	-20.0
<b>Delaware</b>	-2.7	<b>Nevada</b>	-7.6	<b>West Virginia</b>	-3.8
<b>Florida</b>	-54.7	<b>New Hampshire</b>	-4.6	<b>Wisconsin</b>	-17.1
<b>Georgia</b>	-22.9	<b>New Jersey</b>	-34.6	<b>Wyoming</b>	-1.7
<b>Hawaii</b>	-3.7	<b>New Mexico</b>	-4.1	<b>DC</b>	-2.2
<b>Idaho</b>	-3.4	<b>New York</b>	-68.2	<b>Other Areas</b>	-6.9
<b>Illinois</b>	-41.4	<b>North Carolina</b>	-22.2		
<b>Indiana</b>	-16.8	<b>North Dakota</b>	-1.7		
<b>Iowa</b>	-8.1	<b>Ohio</b>	-32.0		
<b>Kansas</b>	-7.6	<b>Oklahoma</b>	-8.0		
<b>Kentucky</b>	-9.6	<b>Oregon</b>	-9.8		
<b>Louisiana</b>	-9.6	<b>Pennsylvania</b>	-38.0		
<b>Maine</b>	-3.6	<b>Rhode Island</b>	-3.3		
<b>Maryland</b>	-19.5	<b>South Carolina</b>	-9.9		

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Notes

The figures in the table are based on tabulations of all individual income tax returns filed and processed through the IRS Individual Master File (IMF) during calendar years 2002 through 2005.

Classification by state was based on the address used on the return. Usually this address is the taxpayer's home address. However, some taxpayers may have used the address of a tax attorney or accountant, or a place of business, and that address could be in a different state than the taxpayer's home.

Source: U.S. Department of Treasury, Office of Tax Analysis



**COMBINED EFFECT OF THE ECONOMIC GROWTH & TAX RELIEF  
ACT OF 2001 AND THE JOBS & GROWTH RELIEF ACT OF 2003**



	Specific Provisions of the Acts						Addendum: Returns with Business Income <sup>3</sup> Benefiting from Acts
	Entire EGTRRA and JGTRRA Acts <sup>1</sup>	New 10% Bracket	Reduction in Top Rates	Reduction of Marriage Penalty	Increase in Child Tax Credit	Reduction in Rates on Capital Gains and Dividends <sup>2</sup>	
United States	107,387	94,707	26,389	31,972	27,166	23,068	24,956
Alabama	1,503	1,288	280	454	443	281	324
Alaska	271	246	73	80	62	60	71
Arizona	1,961	1,727	453	594	514	407	420
Arkansas	883	759	140	281	254	161	211
California	12,658	11,079	3,554	3,630	3,050	2,893	3,265
Colorado	1,747	1,564	478	551	421	400	497
Connecticut	1,394	1,239	465	425	318	358	336
Delaware	331	297	90	97	83	73	63
Florida	6,553	5,717	1,442	1,815	1,636	1,337	1,541
Georgia	3,042	2,638	709	875	848	621	732
Hawaii	497	448	120	145	117	105	126
Idaho	474	418	81	168	130	93	138
Illinois	4,681	4,143	1,270	1,391	1,189	1,047	1,041
Indiana	2,295	2,057	494	740	612	471	484
Iowa	1,084	979	212	368	283	221	293
Kansas	986	879	207	332	260	206	253
Kentucky	1,387	1,221	257	453	371	272	310
Louisiana	1,441	1,229	261	396	424	259	322
Maine	500	449	95	158	124	100	135
Maryland	2,236	2,000	731	635	542	537	496
Massachusetts	2,564	2,299	821	751	553	633	632
Michigan	3,662	3,271	930	1,163	936	796	754
Minnesota	1,993	1,805	530	648	482	456	500
Montana	336	297	54	107	84	64	108
Mississippi	893	754	136	244	278	148	181
Missouri	2,066	1,834	429	651	541	418	460
North Carolina	3,034	2,645	623	927	846	601	711
North Dakota	242	219	41	79	60	48	76
Nebraska	650	584	127	214	168	132	173
Nevada	925	829	225	257	231	194	185
New Hampshire	536	486	147	174	127	125	130
New Jersey	3,416	3,004	1,138	1,015	811	858	749
New Mexico	642	559	124	183	171	121	145
New York	6,949	6,101	1,975	1,804	1,668	1,558	1,605
Ohio	4,427	3,991	1,047	1,214	1,032	902	883
Oklahoma	1,155	1,005	199	378	319	220	303
Oregon	1,299	1,157	292	414	325	274	336
Pennsylvania	4,676	4,185	1,106	1,443	1,160	1,002	943
Rhode Island	413	372	110	119	96	91	95
South Carolina	1,464	1,275	278	424	413	275	313
South Dakota	284	255	46	92	73	55	89
Tennessee	2,075	1,814	393	636	575	402	471
Texas	7,480	6,438	1,651	2,258	2,049	1,517	1,787
Utah	805	716	152	289	223	165	212
Vermont	247	224	53	76	58	52	72
Virginia	2,924	2,595	849	908	705	690	625
Washington	2,385	2,138	637	762	587	539	551
Wisconsin	2,144	1,946	496	697	536	459	465
West Virginia	582	510	94	199	156	110	111
Wyoming	195	176	42	65	50	41	56
DC	237	210	84	31	44	56	49
Other Areas	763	637	149	157	127	165	130

State-by-State  
Distribution  
(based on the number  
of returns filed in 2005  
that would have  
benefited from the acts  
– in thousands)

Source: U.S.  
Department of  
Treasury, Office of  
Tax Policy