Chapter 4: Revenue Options

Revenues—Option 1

Increase Individual Income Tax Rates

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Raise all tax rates on ordinary income by 1 percentage point	54.7	81.4	85.7	90.3	95.3	89.0	89.8	94.7	99.2	103.8	407.4	884.0
Raise all tax rates on ordinary income in the top four brackets by 1 percentage point	13.1	19.8	21.0	22.3	23.8	20.0	19.3	20.4	21.3	22.3	100.0	203.3
Raise all tax rates on ordinary income in the top two brackets by 1 percentage point	7.0	10.6	11.2	11.8	12.6	11.6	11.6	12.1	12.5	12.9	53.2	113.8

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

The estimates include the effects on outlays resulting from changes in refundable tax credits.

As specified by the tax code, different statutory tax rates apply to different portions of people's taxable ordinary income. (Taxable ordinary income is all income subject to the individual income tax other than most long-term capital gains and dividends, minus allowable adjustments, exemptions, and deductions.) Tax brackets—the income ranges to which different rates apply—vary depending on taxpayers' filing status and are adjusted, or indexed, each year to include the effects of inflation. Through calendar year 2025, taxable ordinary income earned by most individuals is subject to the following seven statutory rates: 10 percent, 12 percent, 22 percent, 24 percent, 32 percent, 35 percent, and 37 percent. At the end of 2025, nearly all provisions of the 2017 tax act that affect individual income taxes are scheduled to expire, and the rates will revert to those under pre-2018 tax law. Beginning in 2026, the rates will be 10 percent, 15 percent, 25 percent, 28 percent, 33 percent, 35 percent, and 39.6 percent.

This option consists of three alternative approaches for increasing statutory rates under the individual income tax. The first alternative would raise all tax rates on ordinary income by 1 percentage point; the second would raise all tax rates on ordinary income in the top four brackets by 1 percentage point; and the third would raise all tax rates on ordinary income in the top two brackets by 1 percentage point. Under all three alternatives, the scheduled changes to the underlying tax brackets and rates would still take effect in 2026.

RELATED OPTION: Revenues, "Raise the Tax Rates on Long-Term Capital Gains and Qualified Dividends by 2 Percentage Points" (page 60)

RELATED CBO PUBLICATION: *The Distribution of Household Income, 2017* (October 2020), www.cbo.gov/publication/56575

Revenues—Option 2

Raise the Tax Rates on Long-Term Capital Gains and Qualified Dividends by 2 Percentage Points

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	1.4	6.4	7.1	7.6	8.1	8.5	8.4	8.8	9.3	9.6	30.6	75.2

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

When people sell an asset for more than the price at which they obtained it, they generally realize a capital gain that is subject to taxation. Under current law, long-term capital gains (those realized on assets held for more than a year) and qualified dividends (which includes most dividends) are usually taxed at lower rates than other sources of income, such as wages and interest. The statutory rate on most long-term capital gains and qualified dividends is 0 percent, 15 percent, or 20 percent, depending on a taxpayer's filing status and taxable income.

This option would raise the statutory tax rates on long-term capital gains and qualified dividends by 2 percentage points. The new rates would then be 2 percent, 17 percent, and 22 percent. It would not change other provisions of the tax code that affect taxes on capital gains and dividends.

RELATED OPTIONS: Revenues, "Increase Individual Income Tax Rates" (page 59), "Change the Tax Treatment of Capital Gains From Sales of Inherited Assets" (page 64), "Expand the Base of the Net Investment Income Tax to Include the Income of Active Participants in S Corporations and Limited Partnerships" (page 66), "Increase the Corporate Income Tax Rate by 1 Percentage Point" (page 77), "Impose a Tax on Financial Transactions" (page 86)

RELATED CBO PUBLICATIONS: *The Distribution of Asset Holdings and Capital Gains* (August 2016), www.cbo.gov/publication/51831; *The Distribution of Major Tax Expenditures in the Individual Income Tax System* (May 2013), www.cbo.gov/publication/43768; Tim Dowd, Robert McClelland, and Athiphat Muthitacharoen, *New Evidence on the Tax Elasticity of Capital Gains*, Working Paper 2012-09 (June 2012, updated August 2012), www.cbo.gov/publication/43334

Revenues—Option 3

Eliminate or Modify Head-of-Household Filing Status

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Eliminate head-of-household filing status	10.7	15.8	16.9	17.8	18.8	15.4	14.4	15.2	15.9	16.6	80.0	157.6
Limit head-of-household filing status to unmarried people with a qualifying child under 17	4.1	6.2	6.5	6.9	7.4	6.1	5.7	6.1	6.4	6.6	31.1	62.0

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

On their tax returns, people must indicate their filing status (such as married, single, or head of household), which has implications for the amount of taxes they owe. Those who are not married generally file as single or as a head of household. A head of household receives tax preferences that are not available to other unmarried individuals: They are eligible for a larger standard deduction, and lower tax rates apply to a greater share of their income. Moreover, heads of households qualify for some tax preferences at higher levels of income than those who file as single.

To qualify as a head of household, unmarried people must pay most of the costs of maintaining the household in which they have resided with a qualifying person for more than half of the year. The rules for claiming a qualifying person vary. In addition to meeting certain residency and relationship criteria, a child claimed as a qualifying person must be under the age of 19, under 24 and a full-time student, or permanently and totally disabled. Other dependent relatives, who also must meet residency and relationship criteria, must receive more than half of their support from the head of household and have gross income below a specified amount ($4,300 in 2020).

This option consists of two alternatives. The first alternative would eliminate the head-of-household filing status. The second alternative would retain that status but limit it to taxpayers who pay more than half of the costs of maintaining the household in which they have resided with a qualifying child under the age of 17.

RELATED CBO PUBLICATION: *How Dependents Affect Federal Income Taxes* (January 2020), www.cbo.gov/publication/56004

Revenues—Option 4

Eliminate Itemized Deductions

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	42.1	77.1	80.3	84.3	89.1	188.8	268.2	280.4	296.2	311.5	372.9	1,718.0

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

When preparing their income tax returns, taxpayers may choose either to take the standard deduction—which is a fixed dollar amount—or to itemize and deduct certain expenses, such as state and local taxes, mortgage interest, charitable contributions, and some medical expenses. Taxpayers benefit from itemizing when the value of their deductions exceeds the amount of the standard deduction.

This option would eliminate all itemized deductions.

RELATED OPTION: Revenues, "Limit the Deduction for Charitable Giving" (page 63)

RELATED CBO PUBLICATION: *The Distribution of Major Tax Expenditures in the Individual Income Tax System* (May 2013), www.cbo.gov/publication/43768

Revenues—Option 5

Limit the Deduction for Charitable Giving

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Limit deductibility to charitable contributions in excess of 2 percent of adjusted gross income	2.7	13.5	14.2	14.9	15.7	19.0	29.6	31.3	32.9	34.3	61.0	208.1
Limit deductibility to cash contributions	3.4	17.3	18.2	19.3	20.5	23.0	28.8	31.3	33.8	36.1	78.7	231.7

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

Taxpayers who itemize can deduct the value of their contributions to qualifying charitable organizations. Two restrictions apply to the deduction. First, deductible charitable contributions may not exceed a certain percentage of a taxpayer's adjusted gross income (AGI). (AGI includes income from all sources not specifically excluded by the tax code, minus certain deductions.) The second restriction, which was temporarily lifted but will resume in 2026, reduces the total value of certain itemized deductions—including the deduction for charitable donations—for higher-income taxpayers.

This option consists of two alternatives that would curtail the deduction for charitable donations. Under the first alternative, only the amount of a taxpayer's contributions that exceeded 2 percent of his or her AGI would be deductible. Under the second alternative, the deduction would be eliminated for noncash contributions. Both alternatives would be limited to taxpayers who itemize, and higher-income taxpayers would still be subject to the additional reduction in the total value of certain deductions after 2025.

RELATED OPTION: Revenues, "Eliminate Itemized Deductions" (page 62)

RELATED CBO PUBLICATION: *Options for Changing the Tax Treatment of Charitable Giving* (May 2011), www.cbo.gov/publication/41452

Revenues—Option 6

Change the Tax Treatment of Capital Gains From Sales of Inherited Assets

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	1.2	4.8	7.0	9.0	11.3	12.8	14.1	15.1	16.5	18.4	33.3	110.3

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

When people sell an asset for more than the price for which they obtained it, they realize a net capital gain. The net gain is typically calculated as the sale price minus the asset's adjusted basis—generally the original purchase price adjusted for improvements or depreciation. To calculate the gains on inherited assets, taxpayers generally use the asset's fair-market value at the time of the owner's death, often referred to as stepped-up basis, instead of the adjusted basis derived from the asset's value when the decedent initially acquired it. When the heir sells the asset, capital gains taxes are assessed only on the change in the asset's value relative to the stepped-up basis. As a result, any appreciation in value that occurred while the decedent owned the asset is not included in taxable income and therefore is not subject to the capital gains tax.

Under this option, taxpayers would generally adopt the adjusted basis of the decedent (known as carryover basis) on assets they inherit. As a result, the decedent's unrealized capital gain would be taxed at the heirs' tax rate when they eventually sell the assets. (This option would adjust the basis of some bequeathed assets that would be subject to both the estate tax and the capital gains tax. That adjustment would minimize the extent to which the asset's appreciation in value would be subject to both taxes.)

RELATED OPTION: Revenues, "Raise the Tax Rates on Long-Term Capital Gains and Qualified Dividends by 2 Percentage Points" (page 60)

RELATED CBO PUBLICATION: *The Distribution of Asset Holdings and Capital Gains* (August 2016), www.cbo.gov/publication/51831

Revenues—Option 7

Eliminate the Tax Exemption for New Qualified Private Activity Bonds

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	0.1	0.2	0.5	0.9	1.2	1.5	2.0	2.4	3.0	3.6	2.9	15.4

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

The U.S. tax code permits state and local governments to finance certain projects by issuing bonds whose interest payments are exempt from federal income taxes. For the most part, proceeds from tax-exempt bonds are used to finance public projects, such as the construction of highways and schools. In some cases, however, state and local governments issue tax-exempt bonds to finance private-sector projects. Such bonds—known as qualified private activity bonds—may be used to fund private projects that provide at least some public benefits. Eligible projects include the construction or repair of infrastructure and certain activities, such as building schools and hospitals, undertaken by nonprofit organizations.

This option would eliminate the tax exemption for new qualified private activity bonds.

RELATED CBO PUBLICATIONS: *Public-Private Partnerships for Transportation and Water Infrastructure* (January 2020), www.cbo.gov/publication/56003; *Federal Support for Financing State and Local Transportation and Water Infrastructure* (October 2018), www.cbo.gov/publication/54549; testimony of Joseph Kile, Assistant Director for Microeconomic Studies, before the Senate Committee on Finance, *The Status of the Highway Trust Fund and Options for Paying for Highway Spending* (June 18, 2015), www.cbo.gov/publication/50297; *Federal Grants to State and Local Governments* (March 2013), www.cbo.gov/publication/43967; testimony of Frank Sammartino, Assistant Director for Tax Analysis, before the Senate Committee on Finance, *Federal Support for State and Local Governments Through the Tax Code* (April 25, 2012), www.cbo.gov/publication/43047

Revenues—Option 8

Expand the Base of the Net Investment Income Tax to Include the Income of Active Participants in S Corporations and Limited Partnerships

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	10.1	15.9	17.8	19.5	21.1	23.0	24.6	25.3	25.8	26.5	84.4	209.8

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

In addition to the individual income tax, high-income taxpayers face two taxes on certain types of income above specified thresholds. The first—the additional Medicare tax—is a 0.9 percent tax on wages and self-employment income in excess of those thresholds (bringing their overall Medicare tax rate to 3.8 percent). The second tax faced by high-income taxpayers—the net investment income tax (NIIT)—is a 3.8 percent tax on qualifying investment income, such as interest, dividends, capital gains, rents, royalties, and passive income from businesses not subject to the corporate income tax.

Income generated by certain types of businesses—specifically, limited partnerships (wherein certain partners are not liable for the debts of the business in excess of their initial investment) and S corporations (which are not subject to the corporate income tax because they meet certain criteria defined in subchapter S of the tax code)—may be excluded from both taxes under certain circumstances. If a high-income taxpayer is actively involved in running such a business, as some limited partners and most owners of S corporations are, his or her share of the firm's net profits is not subject to either the additional Medicare tax or the NIIT. (If the taxpayer receives a salary from the firm, however, that income would be subject to the additional Medicare tax.)

This option would impose the NIIT on all income derived from business activity that is subject to the individual income tax but not to the additional Medicare tax.

RELATED OPTION: Revenues, "Raise the Tax Rates on Long-Term Capital Gains and Qualified Dividends by 2 Percentage Points" (page 60)

RELATED CBO PUBLICATION: *Taxing Businesses Through the Individual Income Tax* (December 2012), www.cbo.gov/publication/43750

Revenues—Option 9

Include Disability Payments From the Department of Veterans Affairs in Taxable Income

											Total	
Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2021–2025	2021–2030
Change in Revenues	1.0	9.7	10.8	11.0	10.8	11.8	12.6	13.4	16.6	15.7	43.3	113.4

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

The Department of Veterans Affairs (VA) provides disability compensation to veterans with medical conditions or injuries that occurred or worsened during active-duty service. VA's disability payments are intended to compensate the average earnings that veterans would be expected to lose given the severity of their service-connected medical conditions or injuries, whether or not a particular veteran's condition actually reduced his or her earnings.

Disability compensation is not means-tested (that is, restricted to those with income below a certain amount), and payments are exempt from federal and state income taxes. Payments are in the form of monthly annuities and typically continue until the beneficiary's death.

This option would include VA disability benefit payments in taxable income.

RELATED OPTIONS: Mandatory Spending, "End VA's Individual Unemployability Payments to Disabled Veterans at the Full Retirement Age for Social Security" (page 36), "Reduce VA's Disability Benefits to Veterans Who Are Older Than the Full Retirement Age for Social Security" (page 37), "Narrow Eligibility for VA's Disability Compensation by Excluding Veterans With Low Disability Ratings" (page 38)

RELATED CBO PUBLICATION: *Veterans' Disability Compensation: Trends and Policy Options* (August 2014), www.cbo.gov/publication/45615

Revenues—Option 10

Further Limit Annual Contributions to Retirement Plans

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	5.7	7.4	8.0	8.8	8.9	10.1	11.0	11.8	13.1	14.1	38.8	99.1

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

To the extent that the option would affect Social Security payroll taxes, a portion of the revenues would be off-budget. In addition, the option would increase outlays for Social Security by a small amount. The estimates do not include those effects on outlays.

Current law allows taxpayers to make contributions to certain types of tax-preferred retirement plans up to a maximum annual amount that varies depending on the type of plan and the age of the taxpayer. The most common such plans are defined contribution plans (any plan that does not guarantee a particular benefit amount upon retirement) and individual retirement accounts (IRAs). Defined contribution plans are sponsored by employers. Some—most commonly, 401(k) plans—accept contributions by employees; others are funded entirely by the employer. IRAs are established and funded by the participants themselves. Traditional tax-preferred retirement plans allow participants to exclude contributions from their taxable income and defer the payment of taxes until they withdraw funds. Contributions to Roth retirement plans, by contrast, cannot be excluded from taxable income but are not subject to tax when withdrawn.

People under the age of 50 may contribute up to $19,500 to 401(k) and similar employment-based plans in 2020; participants ages 50 and above are also allowed to make "catch-up" contributions of up to $6,500. Contributions to 457(b) plans, which are available primarily to employees of state and local governments, are subject to a separate limit. Employers may also contribute to their workers' defined contribution plans, up to a maximum of $57,000 per person in 2020, minus any contributions made by the employee.

Under current law, combined contributions to traditional and Roth IRAs are limited to $6,000 for taxpayers under the age of 50 and $7,000 for those age 50 or older. Taxpayers with income above certain thresholds are not allowed to contribute to Roth IRAs. However, some participants can circumvent those limits by contributing to a traditional IRA and then converting it to a Roth IRA.

Under this option, a participant's maximum allowable contributions would be reduced to $17,500 per year for 401(k)–type plans and $5,000 per year for IRAs, regardless of the person's age. The option would also require that all contributions to employment-based plans—including 457(b) plans—be subject to a single combined limit. Total allowable employer and employee contributions to a defined contribution plan would be reduced from $57,000 per year to $51,000. Finally, conversions of traditional IRAs to Roth IRAs would not be permitted for taxpayers whose income is above the top threshold for making Roth contributions.

RELATED OPTION: Revenues, "Tax Social Security and Railroad Retirement Benefits in the Same Way That Distributions From Defined Benefit Pensions Are Taxed" (page 69)

Revenues—Option 11

Tax Social Security and Railroad Retirement Benefits in the Same Way That Distributions From Defined Benefit Pensions Are Taxed

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	17.4	35.8	37.9	39.9	41.9	48.7	55.8	58.2	60.5	62.8	172.9	458.7

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

Under current law, roughly two-thirds of the benefits paid by the Social Security and Railroad Retirement programs are not subject to the federal income tax because most recipients have income below a specified threshold. By contrast, distributions from defined benefit pensions (plans offered by some employers that provide a fixed benefit amount upon retirement based on a predetermined formula) are taxable except for the portion that represents the recovery of an employee's "basis"—that is, the employee's after-tax contributions to the plan.

This option would treat Social Security and Railroad Retirement benefits in the same way that defined benefit retirement plan distributions are treated—by defining a basis and taxing the benefits that exceed that amount. For employed individuals, the basis would be the payroll taxes they contributed to those programs (but not the equal amount that their employers paid on their behalf). For self-employed people, the basis would be the portion (50 percent) of their self-employment taxes that were not deductible from their taxable income.

RELATED OPTION: Revenues, "Further Limit Annual Contributions to Retirement Plans" (page 68)

RELATED CBO PUBLICATION: *Social Security Policy Options, 2015* (December 2015), www.cbo.gov/publication/51011

Revenues—Option 12

Eliminate Certain Tax Preferences for Education Expenses

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	3.1	15.6	15.8	16.0	16.1	16.4	17.0	17.3	17.6	17.9	66.6	152.8

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

The estimates include the effects on outlays resulting from changes in refundable tax credits.

Three major tax preferences support higher education. First, the American Opportunity Tax Credit (AOTC) covers qualifying educational expenses for up to four years of postsecondary education. In 2020, the AOTC can total as much as $2,500 per student and is partially refundable—that is, families whose income tax liability (before the credit is applied) is less than the total amount of the credit may receive a portion of the credit as a payment. Second, the nonrefundable Lifetime Learning tax credit provides up to $2,000 per tax return per year for qualifying tuition and fees. Finally, tax filers may deduct from their taxable income up to $2,500 per year for interest payments on student loans. Those tax preferences are available to taxpayers whose income is below certain thresholds.

This option would eliminate the AOTC and the Lifetime Learning tax credit and would gradually phase out the deductibility of interest payments for student loans in annual increments of $250 over a 10-year period.

RELATED OPTIONS: Mandatory Spending, “Eliminate or Reduce the Add-On to Pell Grants, Which Is Funded With Mandatory Spending” (page 12), “Reduce or Eliminate Subsidized Loans for Undergraduate Students” (page 14); Discretionary Spending, “Tighten Eligibility for Pell Grants” (page 54)

RELATED CBO PUBLICATION: *Distribution of Federal Support for Students Pursuing Higher Education in 2016* (June 2018), www.cbo.gov/publication/53732

Revenues—Option 13

Lower the Investment Income Limit for the Earned Income Tax Credit and Extend That Limit to the Refundable Portion of the Child Tax Credit

											Total	
Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2021–2025	2021–2030
Change in Revenues	*	1.1	1.1	1.1	1.0	1.0	0.6	0.6	0.6	0.6	4.3	7.8

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

The estimates represent the change in the overall budget balance that would result from the sum of changes to revenues and outlays.

* = between zero and $50 million.

Low- and moderate-income people are eligible for certain refundable tax credits under the individual income tax if they meet specified criteria. Refundable tax credits differ from other tax preferences, such as deductions, in that their value may exceed the amount of income taxes that the person owes. If the amount of a refundable tax credit exceeds a taxpayer's tax liability before that credit is applied, the government pays the excess to that person. Refundable tax credits thus can result in net payments from the government to a taxpayer, and those payments are classified as outlays in the federal budget. Two refundable tax credits are available only to workers: the earned income tax credit (EITC) and the refundable portion of the child tax credit (referred to in the tax code as the additional child tax credit).

To qualify for the EITC and the refundable portion of the child tax credit, people must meet several income requirements. First, they must have income from wages, salaries, or self-employment. Second, their adjusted gross income cannot exceed certain thresholds, which vary according to family characteristics. Finally, for the EITC only, eligibility is restricted to filers with investment income that is $3,650 or less in 2020. (Investment income comprises interest including tax-exempt interest, dividends, capital gains, royalties and rents from personal property, and returns from passive activities—that is, business pursuits in which the person is not actively involved.)

This option would lower the EITC threshold for investment income to $1,800. As under current law, that threshold would be adjusted, or indexed, to include the effects of inflation. Moreover, the option would extend the investment threshold to the refundable portion of the child tax credit.

RELATED OPTION: Revenues, "Require Earned Income Tax Credit and Child Tax Credit Claimants to Have a Social Security Number That Is Valid for Employment" (page 72)

RELATED CBO PUBLICATIONS: *Marginal Federal Tax Rates on Labor Income, 1962 to 2028* (January 2019), www.cbo.gov/publication/54911; *Effective Marginal Tax Rates for Low- and Moderate-Income Workers in 2016* (November 2015), www.cbo.gov/publication/50923; *The Distribution of Major Tax Expenditures in the Individual Income Tax System* (May 2013), www.cbo.gov/publication/43768; *Growth in Means-Tested Programs and Tax Credits for Low-Income Households* (February 2013), www.cbo.gov/publication/43934; *Refundable Tax Credits* (January 2013), www.cbo.gov/publication/43767

Revenues—Option 14

Require Earned Income Tax Credit and Child Tax Credit Claimants to Have a Social Security Number That Is Valid for Employment

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	0.1	2.5	2.4	2.3	2.3	2.3	2.4	2.3	2.3	2.3	9.6	21.2

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

The estimates represent the change in the overall budget balance that would result from the sum of changes to revenues and outlays.

The earned income tax credit (EITC) and the child tax credit both provide assistance to certain low- and moderate-income taxpayers, but the eligibility rules differ. Most EITC claimants and their qualifying children must have a Social Security number that is issued by the Social Security Administration solely to people authorized to work in the United States. (However, there are exceptions for some Social Security numbers issued before 2003.) By contrast, eligibility for the child tax credit currently only requires that the qualifying child have a Social Security number that is valid for employment purposes. After 2025, noncitizens will be able to claim the credit if they and their qualifying child have a Social Security number (with no restriction on the reason for issuance) or an individual taxpayer identification number, which is issued by the Internal Revenue Service (IRS) to anyone who is required to file a tax return but cannot obtain a Social Security number.

Under this option, people who are not authorized to work in the United States would not be eligible for either the EITC or the child tax credit. For both credits, taxpayers, spouses, and qualifying children would be required to have Social Security numbers issued to U.S. citizens and noncitizens authorized to work in the United States. The IRS would be authorized to deny the credits using "mathematical and clerical error" (math-error) procedures when taxpayers and their children did not have those types of Social Security numbers. Using math-error procedures prevents the credits from being paid to those taxpayers and does not require the IRS to take further action, although the taxpayers retain the right to dispute the IRS's decision.

RELATED OPTION: Revenues, "Lower the Investment Income Limit for the Earned Income Tax Credit and Extend That Limit to the Refundable Portion of the Child Tax Credit" (page 71)

RELATED CBO PUBLICATIONS: *How Dependents Affect Federal Income Taxes* (January 2020), www.cbo.gov/publication/56004; *How Changes in Immigration Policy Might Affect the Federal Budget* (January 2015), www.cbo.gov/publication/49868; *Growth in Means-Tested Programs and Tax Credits for Low-Income Households* (February 2013), www.cbo.gov/publication/43934; *Refundable Tax Credits* (January 2013), www.cbo.gov/publication/43767

Revenues—Option 15

Increase the Payroll Tax Rate for Medicare Hospital Insurance

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Increase rate by 1 percentage point	50.4	78.8	82.0	85.2	88.8	91.6	95.0	98.4	101.9	105.4	385.2	877.5
Increase rate by 2 percentage points	99.8	156.0	162.2	168.7	175.7	181.3	188.0	194.8	201.4	208.5	762.4	1,736.3

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

Hospital Insurance (HI) benefits provided under Medicare Part A are primarily financed through the HI payroll tax, which is 2.9 percent of total earnings. For employees, 1.45 percent is deducted from their paychecks, and 1.45 percent is paid by their employers. Self-employed individuals generally pay 2.9 percent of their net self-employment income in HI taxes. Workers with higher earnings are also subject to a surtax on all earnings above a certain threshold.

This option consists of two alternatives. The first alternative would increase the HI tax on total earnings by 1 percentage point. The second alternative would increase the HI tax on total earnings by 2 percentage points. Those rate increases would be evenly split between employers and employees. The rate paid by self-employed people would rise by the full amount of the increase. Under both alternatives, workers with higher earnings would still be subject to the surtax.

RELATED OPTION: Revenues, “Increase the Payroll Tax Rate for Social Security” (page 74)

Revenues—Option 16

Increase the Payroll Tax Rate for Social Security

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Increase rate by 1 percentage point	44.9	63.5	66.2	68.9	71.8	73.9	76.2	79.2	82.2	85.1	315.3	711.9
Increase rate by 2 percentage points	88.8	125.5	130.8	136.2	141.8	146.0	150.4	156.4	162.1	167.9	623.1	1,406.0

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

The change in revenues would consist of an increase in receipts from Social Security payroll taxes (which would be off-budget), offset in part by a reduction in individual income tax revenues (which would be on-budget).

Social Security—which consists of Old-Age and Survivors Insurance and Disability Insurance—is financed primarily by payroll taxes on employers, employees, and the self-employed. Earnings up to a maximum ($137,700 in calendar year 2020) are taxed at a rate of 12.4 percent. Employees have 6.2 percent of earnings deducted from their paychecks, and the remaining 6.2 percent is paid by their employers. Self-employed individuals generally pay 12.4 percent of their net self-employment income.

This option consists of two alternative increases to the Social Security payroll tax rate. The first alternative would increase the rate by 1 percentage point; the second alternative would increase it by 2 percentage points. Those rate increases would be evenly split between employers and employees. The rate paid by self-employed people would rise by the full amount of the increase. This option would not change Social Security benefits in any way.

RELATED OPTIONS: Revenues, “Increase the Payroll Tax Rate for Medicare Hospital Insurance” (page 73), “Increase the Maximum Taxable Earnings for the Social Security Payroll Tax” (page 75), “Expand Social Security Coverage to Include Newly Hired State and Local Government Employees” (page 76)

RELATED CBO PUBLICATIONS: *CBO’s 2019 Long-Term Projections for Social Security: Additional Information* (September 2019), www.cbo.gov/publication/55590; *Social Security Policy Options, 2015* (December 2015), www.cbo.gov/publication/51011

Revenues—Option 17

Increase the Maximum Taxable Earnings for the Social Security Payroll Tax

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Raise Taxable Share to 90 Percent												
Change in Outlays	0.1	0.2	0.4	0.7	1.0	1.4	1.9	2.4	3.1	3.8	2.5	15.1
Change in Revenues	18.5	61.1	65.0	65.0	68.3	71.1	73.9	77.2	79.7	82.0	277.9	661.8
Decrease (-) in the Deficit	-18.4	-60.9	-64.6	-64.3	-67.3	-69.7	-72.0	-74.8	-76.6	-78.2	-275.4	-646.7
Subject Earnings Greater Than $250,000 to Payroll Tax												
Change in Revenues	26.6	88.9	93.6	98.0	104.0	109.5	115.1	122.5	129.4	136.5	411.1	1,024.0

Data sources: Staff of the Joint Committee on Taxation; Congressional Budget Office.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

The change in revenues would consist of an increase in receipts from Social Security payroll taxes (which would be off-budget), offset in part by a reduction in individual income tax revenues (which would be on-budget). The outlays would be for additional payments of Social Security benefits and would be classified as off-budget.

Social Security—which consists of Old-Age and Survivors Insurance and Disability Insurance—is financed primarily by payroll taxes on employers, employees, and the self-employed. Earnings up to a maximum ($137,700 in calendar year 2020) are taxed at a rate of 12.4 percent. In 2018, about 83 percent of earnings from employment covered by Social Security fell below the maximum taxable amount and were thus subject to the Social Security payroll tax.

This option considers two alternatives that would increase the share of earnings subject to Social Security payroll taxes. The first alternative would raise the threshold for maximum taxable earnings such that the taxable share of earnings from jobs covered by Social Security was 90 percent. (In later years, the maximum would grow at the same rate as average wages, as it would under current law.) The additional taxed earnings would be included in the benefit calculation. As a result, outlays for Social Security would increase, and that effect would grow for many decades beyond the 10-year period of the estimates as more individuals subject to the new taxable maximum claimed their benefits.

The second alternative would apply the 12.4 percent payroll tax to earnings over $250,000 in addition to earnings below the maximum taxable amount under current law. The taxable maximum would continue to grow with average wages but the $250,000 threshold would not change, so the gap between the two would shrink. The Congressional Budget Office projects that the taxable maximum would exceed $250,000 in calendar year 2039; after that, all earnings from jobs covered by Social Security would be subject to the payroll tax. Earnings under the current-law taxable maximum would still be used for calculating benefits, so scheduled benefits would not change under this alternative.

RELATED OPTIONS: Revenues, "Increase the Payroll Tax Rate for Social Security" (page 74), "Expand Social Security Coverage to Include Newly Hired State and Local Government Employees" (page 76)

RELATED CBO PUBLICATIONS: *The 2020 Long-Term Budget Outlook* (September 2020), www.cbo.gov/publication/56516; *CBO's 2019 Long-Term Projections for Social Security: Additional Information* (September 2019), www.cbo.gov/publication/55590; *Social Security Policy Options, 2015* (December 2015), www.cbo.gov/publication/51011

Revenues—Option 18

Expand Social Security Coverage to Include Newly Hired State and Local Government Employees

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	1.2	3.0	4.9	7.0	9.3	11.2	13.1	15.1	17.2	18.8	25.4	100.8

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

The change in revenues would consist of an increase in receipts from Social Security payroll taxes (which would be off-budget), offset in part by a reduction in individual tax revenues (which would be on-budget). In addition, the option would increase outlays for Social Security by a small amount. The estimates do not include those effects on outlays.

Under federal law, state and local governments can opt out of enrolling their employees in the Social Security program as long as they provide a separate retirement plan for those workers. As a result, about a quarter of workers employed by state and local governments are not covered by Social Security.

Under this option, Social Security coverage would be expanded to include all state and local government employees hired after December 31, 2020. Consequently, all newly hired state and local government employees would pay the Social Security payroll tax. Expanding Social Security coverage to all newly hired state and local government employees would have little impact on the federal government's spending for Social Security in the short term; therefore, the 10-year estimates shown above do not include any effects on outlays. The increased outlays for Social Security would grow in the following decades and would partly offset the additional revenues generated by newly covered employees.

RELATED OPTIONS: Revenues, "Increase the Payroll Tax Rate for Social Security" (page 74), "Increase the Maximum Taxable Earnings for the Social Security Payroll Tax" (page 75)

RELATED CBO PUBLICATIONS: *The 2020 Long-Term Budget Outlook* (September 2020), www.cbo.gov/publication/56516; *CBO's 2019 Long-Term Projections for Social Security: Additional Information* (September 2019), www.cbo.gov/publication/55590; *Social Security Policy Options, 2015* (December 2015), www.cbo.gov/publication/51011

Revenues—Option 19

Increase the Corporate Income Tax Rate by 1 Percentage Point

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	4.5	7.3	8.5	9.1	9.8	11.0	12.0	12.3	12.4	12.5	39.2	99.3

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

The U.S. statutory corporate income tax rate is 21 percent.

This option would increase the corporate income tax rate by 1 percentage point, to 22 percent.

Revenues—Option 20

Repeal the "LIFO" Approach to Inventory Identification and the "Lower of Cost or Market" and "Subnormal Goods" Methods of Inventory Valuation

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	6.7	13.5	13.5	13.5	7.3	1.1	1.1	1.1	1.2	1.2	54.5	60.2

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

To compute its taxable income, a business must first deduct from its receipts the cost of purchasing or producing the goods it sold during the year. Most companies calculate the cost of those goods by adding the value of the inventory at the beginning of the year to the cost of goods purchased or produced during the year, and then subtracting from that total the value of the inventory at the end of the year. To determine the value of its year-end inventory, a business must distinguish between goods that were sold from inventory that year and goods that remain in inventory.

Businesses can choose between several approaches to identify and determine the value of items in their inventory. Under one approach, the specific-identification approach, firms itemize and value goods by tracking each item in inventory and matching it to its actual cost. Other approaches do not require firms to track specific items. The "last in, first out" (LIFO) approach permits them to assume that the last goods added to the inventory were the first ones sold; the "first in, first out" (FIFO) approach allows them to assume that the first goods added to their inventory were the first ones sold.

Firms that use the FIFO approach or the specific-identification approach can then value their inventory using the "lower of cost or market" (LCM) method. The LCM method allows firms to use the current market value of an item (that is, the current-year cost to reproduce or repurchase it) in their calculation of year-end inventory values if that market value is less than the cost assigned to the item. In addition, businesses can qualify for the "subnormal goods" method of inventory valuation, which allows a company to value its inventory below cost if its goods cannot be sold at cost because they are damaged or flawed.

This option would eliminate the LIFO approach to identifying inventory, as well as the LCM and subnormal-goods methods of inventory valuation. Businesses would be required to use either the specific-identification or the FIFO approach to account for goods in their inventory and to set the value of that inventory on the basis of cost. Those changes would be phased in over a period of four years.

Revenues—Option 21

Require Half of Advertising Expenses to Be Amortized Over 5 or 10 Years

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Require half of advertising expenses to be amortized over 5 years	11.2	16.4	12.5	8.3	4.0	2.4	2.6	2.7	2.8	2.8	52.4	65.8
Require half of advertising expenses to be amortized over 10 years	11.9	19.2	17.9	16.4	15.0	14.0	12.7	10.9	8.8	6.7	80.4	133.4

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

Business expenses can generally be categorized as either investments, which create assets whose value persists over a multiyear period, or current expenses, which go toward goods or services whose value dissipates during the first year after they are purchased. They are often treated differently for tax purposes: Current expenses can be deducted from income in the year they are incurred, but some investment costs, such as the cost of constructing buildings, must be deducted over a multiyear period. Advertising is treated by the tax system as a current expense; its costs can therefore be immediately deducted, even in cases where it creates longer-term value.

This option consists of two alternatives. Both would recognize half of advertising expenses as immediately deductible current expenses. The other half would be treated as an investment in brand image and would be amortized over a period of years. Under the first alternative, that period of amortization would be 5 years; under the second alternative, it would be 10 years.

RELATED CBO PUBLICATION: *How Taxes Affect the Incentive to Invest in New Intangible Assets* (November 2018), www.cbo.gov/publication/54648

Revenues—Option 22

Repeal the Low-Income Housing Tax Credit

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	0.1	0.5	1.3	2.3	3.5	4.7	5.9	7.3	8.7	10.1	7.7	44.4

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

Real estate developers who provide rental housing to people with low income may qualify for low-income housing tax credits (LIHTCs), which are designed to encourage investment in affordable housing. The credits, which can be used to reduce the federal tax liability of the developer or an investor in the project over a period of 10 years, cover a portion of the costs of constructing new housing units or substantially rehabilitating existing units. For a property to qualify for the credits, developers must agree to meet two requirements for at least 30 years. First, they must set aside a certain percentage of rental units for people whose income is below a certain threshold. Second, they must agree to limit the rent they charge on the units occupied by low-income people.

This option would repeal the LIHTC, although real estate investors could continue to claim credits granted before 2021 until their eligibility expired.

RELATED CBO PUBLICATION: *Federal Housing Assistance for Low-Income Households* (September 2015), www.cbo.gov/publication/50782

Revenues—Option 23

Increase All Taxes on Alcoholic Beverages to $16 per Proof Gallon and Index for Inflation

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Increase tax	6.1	8.3	8.4	8.5	8.6	8.5	8.6	8.7	8.8	8.9	39.9	83.4
Increase tax and index for inflation	6.1	8.3	8.7	9.1	9.6	9.8	10.2	10.7	11.3	11.8	41.8	95.6

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

Alcoholic beverages are not taxed uniformly: The alcohol content of beer (including other malt beverages and hard seltzers) and wine is taxed at a lower rate than the alcohol content of distilled spirits. The tax rates are currently governed by temporary provisions in place through December 31, 2020. After those provisions expire, distilled spirits will be taxed at a flat rate of $13.50 per proof gallon. (A proof gallon is a liquid gallon that is 50 percent alcohol by volume.) A tax rate of $13.50 per proof gallon translates to about 21 cents per ounce of pure alcohol. The tax on beer will be equivalent to about 10 cents per ounce of pure alcohol, and the tax on wine that is no more than 14 percent alcohol will be about 6 cents per ounce of pure alcohol. (Wines with high volumes of alcohol and sparkling wines face a higher tax per gallon.) Other factors affect how alcoholic beverages are taxed. Specific provisions of tax law can lower the effective tax rate on small quantities of beer and nonsparkling wine for certain small producers. Additionally, small volumes of beer and wine that are produced for personal or family use are exempt from taxation.

This option consists of two alternatives. The first alternative would standardize the base on which the federal excise tax is levied by using the proof gallon as the measure for all alcoholic beverages. The tax rate would be raised to $16 per proof gallon, or about 25 cents per ounce of pure alcohol. That alternative would also eliminate the provisions of law that lower effective tax rates for small producers, thus making the tax rate equal for all producers and quantities of alcohol. The second alternative would also raise the tax rate to $16 per proof gallon and eliminate the provisions that lower effective tax rates for small producers, but it would adjust, or index, the tax for the effects of inflation each year.

RELATED OPTION: Revenues, "Increase Excise Taxes on Tobacco Products" (page 81)

RELATED CBO PUBLICATION: *Raising the Excise Tax on Cigarettes: Effects on Health and the Federal Budget* (June 2012), www.cbo.gov/publication/43319

Revenues—Option 24

Increase Excise Taxes on Tobacco Products

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Outlays	*	*	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.3	-0.8
Change in Revenues	3.1	4.1	3.8	3.8	3.8	3.6	3.6	3.5	3.5	3.4	18.6	36.2
Decrease (-) in the Deficit	-3.1	-4.1	-3.9	-3.9	-3.9	-3.7	-3.7	-3.6	-3.6	-3.5	-18.9	-37.0

Data sources: Staff of the Joint Committee on Taxation; Congressional Budget Office.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

* = between -$50 million and zero.

The federal government taxes tobacco products, including cigarettes, cigars, pipe tobacco, and roll-your-own tobacco. The federal excise tax on cigarettes is just over $1.00 per pack. Large cigars are taxed at 52.75 percent of the manufacturer's sales price, with a maximum tax of 40.26 cents per cigar. Pipe and roll-your-own tobacco are taxed at $2.83 and $24.78 per pound, respectively.

This option would make several changes to the federal excise taxes on tobacco products. It would raise the federal excise tax on all tobacco products by 50 percent. In addition, it would raise the tax on pipe tobacco to equal that for roll-your-own tobacco and set a minimum tax rate on large cigars equal to the tax rate on cigarettes. This option would also reduce mandatory outlays, mainly because of reduced spending for Medicaid and Medicare due to improvements in people's health status.

RELATED OPTION: Revenues, "Increase All Taxes on Alcoholic Beverages to $16 per Proof Gallon and Index for Inflation" (page 80)

RELATED CBO PUBLICATION: *Raising the Excise Tax on Cigarettes: Effects on Health and the Federal Budget* (June 2012), www.cbo.gov/publication/43319

Revenues—Option 25

Increase Excise Taxes on Motor Fuels and Index for Inflation

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Increase the tax rates by 15 cents	9.6	21.9	23.0	23.9	24.8	25.2	25.8	26.8	27.7	28.6	103.2	237.3
Increase the tax rates by 35 cents	22.2	50.0	51.6	52.9	54.1	54.2	54.9	56.2	57.5	58.7	230.8	512.3

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

Since 1993, federal excise tax rates on traditional motor fuels have been set at 18.4 cents per gallon of gasoline and 24.4 cents per gallon of diesel fuel. The revenues from those taxes are credited to the Highway Trust Fund to pay for highway construction and maintenance as well as for investment in mass transit. (A portion of the fuel tax—0.1 cent per gallon—is credited to the Leaking Underground Storage Tank Trust Fund.) Those tax rates are not adjusted for inflation.

This option consists of two alternative increases in the excise tax rates on motor fuels. Under the first alternative, federal excise tax rates on gasoline and diesel fuel would increase by 15 cents per gallon. Under the second alternative, those tax rates would increase by 35 cents per gallon. Under each alternative, the tax would be indexed for inflation each year using the chained consumer price index.

RELATED OPTION: Revenues, "Impose an Excise Tax on Overland Freight Transport" (page 83)

RELATED CBO PUBLICATIONS: *Reauthorizing Federal Highway Programs: Issues and Options* (May 2020), www.cbo.gov/publication/56346; *Issues and Options for a Tax on Vehicle Miles Traveled by Commercial Trucks* (October 2019), www.cbo.gov/publication/55688; *Approaches to Making Federal Highway Spending More Productive* (February 2016), www.cbo.gov/publication/50150; *How Would Proposed Fuel Economy Standards Affect the Highway Trust Fund?* (May 2012), www.cbo.gov/publication/43198

Revenues—Option 26

Impose an Excise Tax on Overland Freight Transport

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	17.2	32.0	35.6	36.4	37.1	37.2	37.7	38.5	39.2	39.9	158.3	350.9

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

Under current law, federal taxes related to overland freight transport by truck consist of a tax on diesel fuel; excise taxes on new freight trucks, tires, and trailers; and an annual heavy-vehicle use tax. Rail carriers pay a small per-gallon assessment on diesel fuel. There is no existing per-mile federal tax on freight transport.

This option would impose a new tax on freight transport by truck and rail. Freight transport by heavy-duty trucks (Class 7 and above in the Federal Highway Administration's classification system) would be subject to a tax of 30 cents per mile and freight transport by rail to a tax of 12 cents per mile (per railcar). The tax would not apply to miles traveled by trucks or railcars without cargo.

RELATED OPTION: Revenues, "Increase Excise Taxes on Motor Fuels and Index for Inflation" (page 82)

RELATED CBO PUBLICATIONS: *Issues and Options for a Tax on Vehicle Miles Traveled by Commercial Trucks* (October 2019) www.cbo.gov/publication/55688; David Austin, *Pricing Freight Transport to Account for External Costs*, Working Paper 2015-03 (March 2015), www.cbo.gov/publication/50049

Revenues—Option 27

Impose a 5 Percent Value-Added Tax

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues												
Apply a 5 percent VAT to a broad base	0	200	290	300	320	320	330	340	360	370	1,110	2,830
Phase in a 5 percent VAT to apply to the same broad base	0	40	100	160	230	290	330	340	360	370	530	2,220
Apply a 5 percent VAT to a narrow base	0	120	190	200	200	210	210	220	230	240	710	1,820

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2022.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

A value-added tax (VAT) is a type of consumption tax that is levied on the incremental increase in value of a good or service at each stage of the supply chain, up until the final point of sale. Currently, the United States does not have a broad consumption-based tax. Most states impose sales taxes, but, unlike a VAT, those are only levied at the final point of sale.

This option consists of three alternatives. The first alternative would impose a 5 percent VAT on a broad base of goods and services that would become fully effective in January 2022. Certain goods and services would be excluded from the base because their value is difficult to measure. Those include financial services without explicit fees, existing housing services, primary and secondary education, and other services provided by government agencies and nonprofit organizations for a small fee or at no cost. Government-reimbursed expenditures for health care—primarily costs paid by Medicare and Medicaid—would also be excluded from the tax base. The second alternative would gradually introduce a 5 percent VAT to the same broad base of goods and services. The VAT would be phased in over five years, starting at 1 percent in 2022 and increasing by 1 percentage point each year. The third alternative would impose a 5 percent VAT on a narrower base and would, like the first alternative, become fully effective in January 2022. In addition to those items excluded under the broad base, the narrow base would exclude certain goods and services that are considered necessary for subsistence or that provide broad social benefits—specifically, new residential housing, food purchased for home consumption, health care, and postsecondary education.

Revenues—Option 28

Impose a Tax on Emissions of Greenhouse Gases

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	58.2	89.9	92.1	96.6	101.8	106.2	111.4	117.9	125.1	133.4	438.6	1,032.5

Data sources: Staff of the Joint Committee on Taxation; Congressional Budget Office.

This option would take effect in January 2021.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

The accumulation of greenhouse gases in the atmosphere—particularly of carbon dioxide (CO_2) released when fossil fuels (such as coal, oil, and natural gas) are burned—contributes to climate change, which imposes costs and increases the risk of severe economic harm to countries around the globe, including the United States. The federal government regulates some emissions in an effort to reduce them; however, emissions are not directly taxed.

This option would impose a tax of $25 per metric ton on most emissions of greenhouse gases in the United States—specifically, on most energy-related emissions of CO_2 (for example, from electricity generation, manufacturing, and transportation) and on some other greenhouse gas emissions from large manufacturing facilities. The tax would increase at a constant real (inflation-adjusted) rate of 5 percent per year.

RELATED CBO PUBLICATIONS: Evan Herrnstadt and Terry Dinan, *CBO's Projection of the Effect of Climate Change on U.S. Economic Output*, Working Paper 2020-06 (September 2020), www.cbo.gov/publication/56505; *Effects of a Carbon Tax on the Economy and the Environment* (May 2013), www.cbo.gov/publication/44223

Revenues—Option 29

Impose a Tax on Financial Transactions

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	-43.3	20.4	67.4	90.1	98.0	99.0	101.1	103.9	106.5	109.0	232.6	751.9

Data source: Staff of the Joint Committee on Taxation.

This option would take effect in January 2022, although some changes to revenues would occur earlier because of an immediate reduction in the value of financial assets.

An offset to reflect reduced income and payroll taxes has been applied to the estimates in this table.

The United States is home to large financial markets with a lot of daily trading. Under current federal tax law, no tax is imposed on the purchase of securities (stocks and bonds) or other financial products. However, the Securities and Exchange Commission charges a fee of approximately 0.002 percent on most transactions.

This option would impose a tax on the purchase of most securities and on transactions involving derivatives (contracts requiring one or more payments that are calculated by reference to the change in an observable variable). For purchases of stocks, bonds, and other debt obligations, the tax generally would be 0.1 percent of the value of the security. For purchases of derivatives, the tax would be 0.1 percent of all payments actually made under the terms of the contract, including the price paid when the contract was written, any periodic payments, and any amount to be paid when the contract expires. The tax would not apply to the initial issuance of stock or debt securities, transactions of debt obligations with fixed maturities of no more than 100 days, or currency transactions (although transactions involving currency derivatives would be taxed). It would be imposed on transactions that occurred within the United States and on transactions that took place outside of the country and involved at least one U.S. taxpayer (whether a corporation, partnership, citizen, or resident).

RELATED OPTION: Revenues, "Raise the Tax Rates on Long-Term Capital Gains and Qualified Dividends by 2 Percentage Points" (page 60)

Revenues—Option 30

Increase Federal Civilian Employees' Contributions to the Federal Employees Retirement System

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Revenues	1.4	2.7	4.0	5.3	5.2	5.1	5.0	4.9	4.7	4.5	18.6	42.8

This option would take effect in January 2021.

The federal government provides most of its civilian employees with a defined benefit retirement plan through the Federal Employees Retirement System (FERS). The plan provides retirees with a monthly benefit in the form of an annuity. Those annuities are jointly funded by the employees and the federal agencies that hire them. Employees' contributions are counted as federal revenues. Over 95 percent of federal employees participate in FERS, and most of them contribute 0.8 percent of their salary toward their future annuity. However, the contribution rates for employees hired in 2013 or later generally are higher: Most employees hired in 2013 contribute 3.1 percent, and most hired in 2014 or later contribute 4.4 percent.

Under this option, most employees enrolled in FERS would contribute 4.4 percent of their salary toward their retirement annuity. The increase in the contribution rates (of 3.6 percentage points for employees who enrolled in FERS before 2013 and 1.3 percentage points for those who enrolled in 2013) would be phased in over four years. The dollar amount of future annuities would not change under the option, and the option would not affect employees hired in 2014 or later who already contribute 4.4 percent. Agencies' contributions would remain the same under the option.

RELATED CBO PUBLICATIONS: Justin Falk and Nadia Karamcheva, *Comparing the Effects of Current Pay and Defined Benefit Pensions on Employee Retention*, Working Paper 2018-06 (June 2018), www.cbo.gov/publication/54056; *Options for Changing the Retirement System for Federal Civilian Workers* (August 2017), www.cbo.gov/publication/53003; *Comparing the Compensation of Federal and Private-Sector Employees, 2011 to 2015* (April 2017), www.cbo.gov/publication/52637

Revenues—Option 31

Increase Appropriations for the Internal Revenue Service's Enforcement Initiatives

Billions of Dollars	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Total 2021–2025	Total 2021–2030
Change in Outlays	0.5	1.0	1.5	2.0	2.5	2.5	2.5	2.5	2.5	2.5	7.5	20.0
Change in Revenues	0.3	1.5	3.3	5.1	6.8	8.1	8.8	9.0	8.9	8.8	17.1	60.6
Increase or Decrease (-) in the Deficit	0.2	-0.5	-1.8	-3.1	-4.3	-5.6	-6.3	-6.5	-6.4	-6.3	-9.6	-40.6

This option would take effect in October 2021.

Because of the budget scorekeeping guidelines used by the Congress, the revenue changes attributable to this option would not be counted for budget enforcement purposes. However, if an appropriation bill or another bill providing funding for this option was enacted, the Congressional Budget Office's next projection of the budget deficit would incorporate its effects on revenues.

The Internal Revenue Service (IRS) undertakes a variety of enforcement activities (including audits) to improve compliance with the tax system. Increasing funding for enforcement (often referred to as a program integrity initiative) would, in the Congressional Budget Office's estimation, boost federal revenues.

This option would gradually increase the IRS's funding for enforcement. Funding would rise by $500 million each year for the first five years and then remain at an additional $2.5 billion per year from 2026 to 2030. Each infusion of new funding would result in the start of new enforcement initiatives—expansions of audits and other activities that could improve compliance with the tax system. All the new initiatives would continue to be funded at the same level and would remain in effect through 2030 and beyond.

RELATED CBO PUBLICATIONS: *Trends in the Internal Revenue Service's Funding and Enforcement* (July 2020), www.cbo.gov/publication/56422; Janet Holtzblatt and Jamie McGuire, *Factors Affecting Revenue Estimates of Tax Compliance Proposals*, Working Paper 2016-05 (November 2016), www.cbo.gov/publication/52199; *Estimating the Revenue Effects of Proposals to Increase Funding for Tax Enforcement* (June 2016), www.cbo.gov/publication/51699