Obama’s Tax Plan Is More Progressive than McCain’s, But Neither Proposes to Increase Revenue

One of the most passionate, and most confused, debates taking place during this election season is the debate over federal tax policy. Unfortunately, both presidential candidates, Barack Obama and John McCain, are proposing enormous tax cuts that would reduce federal revenues that are badly needed to fully fund public services. What is less widely understood is that Obama’s proposed tax cuts would cost less and target more benefits towards the middle-class than McCain’s.

Our analysis shows that McCain’s plan gives its largest benefits to the richest one percent of taxpayers, while Obama’s plan offers more benefits to low and middle-income taxpayers. The nearby table shows figures for 2012, when most of the provisions in both candidates’ tax plans would be fully in effect.

The poorest 60 percent of taxpayers would get a tax cut under both plans, but would receive a larger cut under Obama ($1,017) than under McCain ($823). The average tax change for the richest one percent would be a tax cut under both plans. But the average tax cut received by the richest one percent under McCain’s plan would be forty times the size of the average tax cut received by this group under Obama’s plan.

What the Candidates Propose

There are several parts to each candidate’s tax plans. First, both would extend the Bush tax cuts for most people (in the case of Obama) or for everyone (in the case of McCain). Second, both would change the Alternative Minimum Tax. Obama would keep it from affecting those who are not rich while McCain has indicated a desire to repeal it altogether. Third, both would also offer new tax cuts. Obama’s are targeted towards the middle-class while McCain’s consist mostly of tax cuts for corporations and businesses. Fourth, both propose to close some business loopholes to raise revenue, but not nearly enough to offset the cost of their proposed tax cuts. These loophole-closing provisions could raise taxes overall for some very rich taxpayers. McCain would take an additional step of enacting what he calls an alternative “simplified” tax (AST), which would actually make the tax code more complicated.

The common element one finds in looking at the two tax plans is that Senator Obama proposes to shower tax cuts on all but the very richest Americans, while McCain proposes novel ways to direct tax cuts even to the very richest taxpayers. This is one reason why McCain’s plan would lose even more federal revenue than Obama’s.

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McCain Would Extend the Bush Tax Cuts for Everyone, Obama Would Extend the Bush Tax Cuts for Almost Everyone

Senator Obama proposes to extend the Bush tax cuts for everyone except married couples with adjusted gross income (AGI) over $250,000 or singles with AGI over $200,000. We estimate that only 2.6 percent of taxpayers will have AGI above these levels.

Even these richest few would get to partially keep some of the tax cuts enacted under Bush, since Obama would partially extend Bush’s estate tax reduction and dividend loophole for even the richest Americans.

Senator McCain, on the other hand, would extend all the Bush tax cuts for everyone, regardless of how wealthy they are. The fact that Obama would not make all the Bush tax cuts permanent for the richest 2.6 percent has been falsely described in an ad by the McCain campaign as “painful tax increases on working American families.”

McCain’s proposal to extend the Bush tax cuts for everyone would cost an incredible $216 billion in 2012 alone, while Obama’s proposal to extend them to almost everyone would cost $146 billion in 2012.

Alternative Minimum Tax: Reform or Repeal?

Senator Obama says he supports “fiscally responsible” reform of the Alternative Minimum Tax (AMT), the back-stop tax that is intended to ensure that wealthy Americans pay some income tax no matter how proficient they are at finding loopholes to reduce or wipe out their regular tax liability. It is generally assumed that Obama means he would make permanent the AMT relief that Congress has been enacting periodically to ensure that the AMT’s reach does not expand to more taxpayers who are not so wealthy.

Senator McCain’s staff has said that he would also “reform” the AMT, but the candidate himself has indicated at various times that he would repeal it altogether. Extending AMT relief would ensure that the non-rich don’t have to worry about the AMT, but repealing it altogether would extend the same favor to even the richest Americans, who would then be more able to use loopholes to reduce or wipe out their tax liability.

Both Candidates Propose More Tax Cuts On Top of Extending the Bush Tax Cuts: Obama’s Middle-Class Tax Cuts vs. McCain’s Corporate Tax Cuts

Senator McCain proposes to reduce the statutory tax rate for corporations from 35 percent to 25 percent. (Remember that most corporations pay far less than the statutory rate because of tax loopholes.) He also proposes to enact first-year deduction or “expensing” of equipment, which, along with...
a lower corporate tax rate, will create new opportunities for tax sheltering by corporations and the wealthy. McCain also proposes an increase in the exemption for dependents, which would not benefit those taxpayers (around 40 percent of all taxpayers) who pay federal payroll taxes but don’t pay federal income taxes.

In contrast, Senator Obama’s plan has a variety of new tax breaks targeting middle- and low-income families. His refundable Making Work Pay Credit would refund $500 in payroll taxes (or $1,000 for a working couple). His refundable American Opportunity Credit would provide up to $4,000 for post-secondary education. He would exempt seniors with incomes below $50,000 from income taxes. His refundable Universal Mortgage Credit would offer a tax break for homeowners who don’t benefit from the current mortgage interest deduction. He would strengthen the Earned Income Tax Credit, which President Reagan called the “the best anti-poverty, the best pro-family, the best job creation measure to come out of Congress.”

The list goes on, but the point is clear. Senator Obama proposes to cut taxes for middle- and low-income families, while McCain proposes to cut taxes for business.

**McCain’s Alternative Simplified Tax Would Make the Tax Code More Complicated and Has Huge Costs**

Senator McCain has proposed enacting an alternative “simplified” tax (which we will call the AST) that taxpayers could file under at their option. There have been several proposals for simpler tax systems that are optional, but one immediately wonders how this can really simplify tax filing. Clearly, anyone who can choose between two different taxes is going to calculate their liability under both (or, for the wealthy, have their accountants calculate their liability under both) and then choose whichever one results in lower tax liability. How can it be simpler to have everyone do their taxes twice?

Even more baffling is that the McCain campaign says that the AST would be revenue-neutral. Proponents of this concept argue that some people will be willing to pay more in return for using the simpler tax. But this is preposterous since filers can already have a simpler tax right now by simply forgoing the various deductions and credits that are offered to them. It’s highly unlikely that many people opt to do this. Thus only those who would pay less under the AST would opt to use it, and the revenue cost is likely to be huge.

While the McCain campaign has not specified the parameters of the AST, it is clearly inspired by similar proposals put forward by former Senator Fred Thompson and a group of Republicans in the House of Representatives. Based on the details of those proposals, and assuming that Americans would behave rationally and opt to file under the AST if it saves them money, CTJ estimates that the AST will cost $98 billion in 2012 alone. About half of the tax cuts provided by the AST in 2012 would go to the richest one percent of taxpayers.

**Loophole-Closing for Corporations and Other Businesses**

Both campaigns claim that their candidates can raise some revenue by closing tax loopholes. McCain’s campaign says he can raise about $30 billion a year by closing corporate tax loopholes, but has not given specifics other than to say that certain breaks for energy companies would be repealed, as well the deduction for domestic manufacturing.
The Obama campaign says that Senator Obama can raise $76 billion in 2009 alone by taking certain steps to close loopholes and crack down on tax evasion. These steps include repealing special breaks for energy companies and imposing a windfall profits tax on them, sanctioning countries that are tax havens (that do not cooperate with U.S. tax enforcement efforts), shutting down certain schemes used in the financial sector to take advantage of the capital gains rate for income that is not really capital gains, and several others.

These provisions could lead to tax increases for some in 2012. We make the standard assumption that any tax increases resulting from closing corporate loopholes will be born by owners of corporate stock (the majority of which is owned by the richest one percent). The other loophole-closing provisions are also likely to affect the very rich.

**McCain's Ads and Statements on Taxes Are Refuted by His Own Chief Economic Adviser**

Senator McCain’s campaign is running ads that say Senator Obama proposes “painful tax increases on working American families.” But clearly Obama is proposing tax cuts for almost all Americans, and even the richest one percent would receive, on average, a tax cut under Obama’s plan. Senator McCain lately has been telling Americans that “Senator Obama will raise your taxes.” Oddly, McCain’s advisers are fully aware that the message the McCain campaign is delivering about taxes is untrue. TIME’s Michael Sherer wrote, back in July:

“Here is Douglas Holtz-Eakin, McCain’s chief economic policy adviser. ‘I used to say that Barack Obama raises taxes and John McCain cuts them, and I was convinced,’ he told me in a phone interview this week. ‘I stand corrected [about Obama’s plans].’”

**McCain Condemns Obama for Refusing to Make the Bush Tax Cuts Permanent for Everyone, Even though McCain Voted Against Enacting the Bush Tax Cuts**

Senator McCain actually voted against the two major components of the Bush tax cuts. He first voted against the 2001 law that cut the personal income tax, mostly benefitting the rich, and phased out the estate tax, which entirely benefits the rich. He then voted against the 2003 law that increased the loophole for capital gains, created a new one for dividends, and sped up or extended other cuts in the personal and corporate income taxes.

Senator McCain was critical of Bush’s tax proposals even before Bush took office. Senator McCain said back in 2000, “Gov. Bush wants to spend the entire surplus on tax cuts. I don’t believe the wealthiest 10% of Americans should get 60% of the tax breaks. I think the lowest 10% should get the breaks.”

**No Evidence that Tax Cuts Will Improve the Economy**

There is no evidence that allowing taxes to revert to the levels in place under President Clinton will harm the economy. It is therefore even less likely that Obama’s plan, which would only do this for the richest 2.6 percent, would harm the economy.

For the best-off 2.6 percent, Obama would extend only part of the Bush tax cuts, specifically a lower estate tax and a tax break for dividends. Otherwise, he would let the rest of the Bush tax cuts for the very wealthy expire.

But even if all Americans faced the tax rules that existed during the Clinton years, it’s hard to see how this would hurt the economy. Real median household income, which grew during the Clinton years, has fallen in the Bush years. The poverty rate, which declined under Clinton, has inched back up during the Bush years. Unemployment, which fell under Clinton, has risen under Bush. And, of course, the Clinton budget surpluses have turned into giant deficits under Bush. As it turned out, wildly cutting taxes was bad fiscal policy and bad economics.♦
The Presidential election isn’t the only forum in which voters will be able to exercise some influence over tax policy this November. Residents of at least five states will be deciding upon ballot initiatives with important consequences for their states’ tax systems.

Unfortunately, most of these proposals either strongly favor the wealthy, or potentially will have a disastrous impact on state revenues (or both). Such criticisms are frequently true of tax-related ballot questions, since all too often such proposals are focused single-mindedly on cutting taxes at any cost, rather than on undertaking the hard work necessary to actually improve our systems of taxation.

Massachusetts: A Proposed 40% Cut in Government

The proposal on the ballot in Massachusetts provides perhaps the most obvious example of the recklessness so often involved in anti-tax ballot initiatives. Massachusetts voters will once again have to decide this November on a proposal to amend their constitution to end the income tax — a move that would reduce government revenues by a whopping 40%, and would undoubtedly have dire consequences in the form of reduced government services.

But while all Massachusetts residents would have to share in the pain of a 40% reduction in their government’s budget, the wealthy would be the primary beneficiaries of the tax cut — as the income tax is the only major progressive tax levied by the state.

Despite the proposal’s fundamental flaws, as well as the existence of a formidable opposition, there is still good reason to be concerned about its potential passage. In 2002, a similar measure was supported by over 45% of voters.

North Dakota: A Typo-Plagued Income Tax Giveaway For the Rich

North Dakota voters will also be taking a look at their income tax this fall. Backers of an income tax rate cut there are enthusiastically pushing a plan that offers an average tax cut of just $83 to the lowest and middle 60% of taxpayers statewide. What’s the big deal? Well, the wealthiest 1% of North Dakotans, for one thing, would save an average of over $11,000 per year! Seem fair? And those numbers don’t even include the corporate income tax cuts, which are sure to also disproportionately benefit the wealthy. And to make matters worse, the proposal would cost the state over $200 million annually.

But just as interesting as the unfair lopsidedness of this initiative is the amateurish way in which it was drafted. As a result of errors in the proposal’s language, including confusion by the authors in their use of commas and periods, the proposal provides tax cuts for a few families that differ significantly from what was intended, and for other families could even result in a net tax increase! Oops!

Oregon: $15,809 for Each of the Richest 1% ... $0 for 78% of Families

A proposal to be voted on in Oregon seeks to allow taxpayers to deduct (in full) their income tax payments to the federal government for state income tax purposes. Currently, only the first $5,600 one pays to the federal government is allowed to be deducted on Oregon state income tax forms. This arrangement already has regressive results, and by uncapping the deduction limit completely, those wealthy individuals who owe the most in federal income taxes will be allowed to slash their Oregon tax payments substantially.

Though the workings of the Oregon proposal may seem a bit confusing, its results most certainly are not. The vast majority (78%) of Oregonian families will get nothing, the wealthiest 1% will enjoy a nearly $16,000 annual tax cut, and the government of Oregon will have to make due with between $500 million and $1 billion less in revenues each year. Six other states: Alabama, Iowa, Louisiana, Missouri, Montana, and North Dakota currently allow for some deduction of federal income taxes. Each of these states would be wise to end this regressive and costly practice.
Arizona: A Proposal to Effectively End All Tax Increases Forever

Proposition 105 seeks to amend Arizona’s constitution to require that any tax increase be approved by a majority of registered voters. This might sound reasonable to someone who doesn’t take a moment to think about what it means. This would replace the existing requirement that all tax increases done through the ballot be approved by a majority of those who vote in the relevant election. There’s something that Arizonans should remember: No ballot initiative in the last decade (tax related or otherwise) has received approval from a majority of registered voters in Arizona.

Under this new proposal, if a tax increase was on the ballot and only a little over half the registered voters took the time to vote (which would not be unusual) then every single one of them would have to vote in approval of the tax measure for it to become law. Needless to say, Proposition 105 is a sneaky way of blocking any and all tax increases — a very irresponsible arrangement, given the recent budget troubles in the state.

Colorado: A Move Towards More Responsible Governance?

Colorado is the lone exception to the norm of ill-conceived ballot proposals this year. For over a decade, Colorado revenues were strictly suppressed by the so-called “Taxpayer Bill of Rights” (TABOR). This posed a serious problem given the inflationary nature of the cost of government services, especially since another constitutional amendment requires regular increases in education spending. Reconciling these two competing demands proved impossible, and in 2005 Colorado voters temporarily suspended a significant portion of the TABOR requirement.

This year, it appears many Coloradans have finally had enough with having to deal with inadequate government services under the unrealistic TABOR requirements. Voters will have the opportunity to decide on Amendment 59, which would end the automatic refunds to taxpayers used to suppress state revenues, in favor of diverting that money toward education. Passage of Amendment 59 would amount to a bold statement that lower taxes are not always better, a message that would mean a lot coming from a state that so recently embraced the opposite philosophy.

Other Good News: Numerous Anti-Tax Plans Fail to Make the Ballot

Florida: The Florida Supreme Court struck from the ballot a measure seeking to repeal a substantial portion of state property taxes for schools. The property tax cut would not only have hurt Florida’s children, but would also have required an increase in the state’s sales tax. The measure was removed from the ballot for being both confusing and misleading. Further debate in Florida regarding their property tax can be expected in the near future.

Nevada and Montana: Proposition 13-style efforts to limit annual increases in a home’s value for tax purposes fell short in both Nevada and Montana. Such a cap would have created an unworkable situation in both states for schools and other services dependent on the property tax, since such programs generally increase in cost much faster than the amounts allowed by the cap. The Montana provision fell well short of the number of signatures needed, while in Nevada, proponents of the cap only fell short after 8,000 signatures were invalidated as a result of election law violations.

Arizona: After a startling 47% of signatures were found to be invalid, an Arizona measure seeking to increase the sales tax to pay for transportation was stripped from the ballot. While Arizona is undoubtedly in need of additional transportation funding, the sales tax is arguably the worst way to go about raising that money. Sales taxes are a regressive source of revenue that also does a poor job of raising funds from those commuters and travelers who benefit the most from the roadways. With a transportation network paid for by sales taxes, the poor end up paying the most (as a share of income) regardless of how much they drive.
No. Anyone looking at Senator Obama’s actual tax plan can see that’s not the case. (See front page article.) But the McCain campaign has gone through all sorts of contortions to make the argument that Obama wants to raise taxes on middle-income people. During the first presidential debate, Senator McCain dug up an old vote cast by Senator Obama on a budget resolution and twisted its meaning to say Obama supports tax increases for people at this income level.

The vote McCain referred to was for a non-binding budget resolution that actually called for cutting taxes. President Bush and his allies in Congress enacted tax cuts that expire at the end of 2010. Obama voted to approve a non-binding budget resolution calling for extending some of the Bush tax cuts for the middle-class past 2010. Republican leaders said this was a “tax increase” since it did not call for extending all the tax cuts, and apparently McCain has adopted this notion.

But even if you accept that fiction, and even if you put aside the fact that the budget resolution is not binding law and cannot by itself raise taxes, you would still be hard-pressed to find anything true in what McCain has been saying lately about Obama’s tax plan.

Several of McCain’s ads say that Obama’s vote (for the budget resolution) would result in higher taxes for people making just $42,000, and the visual images that accompany the message clearly indicate that the ads are referring to people with children. But that is blatantly misleading, because even if the budget resolution was binding law this year, no one at that income level would lose a dollar of their Bush tax cuts unless they were single — and even then they would only lose $15.

But all of this is entirely irrelevant anyway, because the budget resolution vote simply indicates the senator’s preference between two budget plans that were available at that time (a Democratic version and a Republican version). The more relevant question is what Senator Obama wants to do as president. That can only be answered by looking at his current tax proposal which showers tax cuts on almost all Americans.
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