Looking Close to Home:
How Jeb Bush's Tax Plan Would Affect Three Taxpayers

2 of 3 taxpayer scenarios could see tax savings from plan,
but questions still remain to understand full potential impacts to tax returns

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Ahead of Wednesday's Republican debate, there has been plenty of analysis in the news on Jeb Bush's tax proposal, the latest of the plans to be announced. While much of the analysis has focused on the plan's possible macro-effects on the U.S. economy and government debt, there has been little analysis done on the impact to the average taxpayer. The Tax Institute at H&R Block has developed three scenarios showing how two different families would see a tax savings, while a third taxpayer would pay more under the Bush plan, which seeks to make the tax code "simple, fair and clear" for individuals and businesses by:

- Condensing tax brackets from seven to three, with a top marginal rate of 28 percent
- Reducing or eliminating many kinds of deductions (such as capping the mortgage interest deduction, and eliminating state and local income tax deductions)
- Eliminating some types of taxes altogether (such as the estate tax and alternative minimum tax, or AMT)
- Eliminating some loopholes for high-wealth individuals and corporations

That, of course, isn't the whole story, and many key questions remain.

The real plan is in the details

Overall, it's difficult to assess – without details – just what impact the proposal would have on various income categories. But much of the recent commentary published indicates that middle- and lower-income earners may have a less-favorable tax outcome under the Bush plan than high-income taxpayers. Here are some possible reasons.

Tax brackets

For higher-income filers, the condensing of tax brackets means that more income would be taxed at a lower rate. But for people in the lower brackets, this change could mean that more income would be taxed at a higher rate.

Itemized deductions

Some middle-income filers – especially in high-tax states – could be affected by the loss or reduction of some itemized deductions under the Bush plan. And these filers may not be able to make up for the losses with the higher standard deduction and flattened tax brackets.

The Bush plan also doesn't outline how middle-income taxpayers in high-cost parts of the country would fare if their deductions for mortgage interest and real property taxes are reduced or eliminated in favor of a higher standard deduction.

Under current law, the highest-income taxpayers are subject to a limit on itemized deductions. Also, the AMT sometimes ensures that the highest-income taxpayers are taxed at a base tax rate, so those taxpayers wouldn't be as affected by the changes.

Credits

Lower-income and some middle-income taxpayers often rely on family and individual credits to reduce or eliminate their tax bill and/or provide a refundable credit. Although the Bush plan will expand the refundable Earned Income Tax Credit (EITC) for childless workers, it's unclear whether an expanded EITC would come at the expense of other family-friendly tax breaks, such as the Child Tax Credit (CTC), child and dependent care credit, and education tax credits. If those credits are reduced or eliminated, lower- and middle-income filers could face a higher bill or refund reduction.

Under current law, higher-income taxpayers may not qualify for these credits, so they wouldn't be affected.

Three real-life examples

Despite the lack of details about credits, it's possible to construct several examples based on the Bush tax plan. Consider these three taxpayer scenarios, which demonstrate how varying fact patterns could result in tax savings and tax increases under the plan:

Scenario 1: Middle-income family of four living in Missouri
Saves $2,913

- Family of four (married couple with two children under 17)
- Homeowners in Kansas City, MO
- Combined wages of $100,000
- Itemized deductions totaling $17,500 ($5,000 state/local tax; $2,500 real property tax; $1,000 personal property tax; $7,000 mortgage interest; $2,000 charitable contributions)

What would change under the Bush tax plan:

- *Itemized vs. standard deduction*. Under the Bush plan, the deduction for state and local income tax would be eliminated, and the deductions for real property tax and mortgage interest would be capped at 2 percent of adjusted gross income (AGI) – reducing available itemized deductions to $7,000. The expanded standard deduction of $22,600 is therefore more advantageous.
- *Tax rate*. Under current law, this family is in the 15 percent marginal tax bracket. Under the Bush plan, they are in the 10 percent bracket.
- *Tax credits*. Under either system, the family is out of EITC range. Under current law, this family is eligible for a CTC of $2,000. It is not clear whether the Bush plan would retain or modify the CTC.

Results:
This family would save $2,913 under the Bush plan compared with current law. The savings are due to an increased standard deduction and lower tax bracket. However, if the CTC is eliminated, their savings would be reduced to $913.

Scenario 2: Lower-income family of four living in Missouri
Saves $1,000

- Family of four (married couple with two children under 17)
- Renters in Kansas City, MO
- Combined wages of $45,000

- Use standard deduction of $12,600

What would change under the Bush tax plan:

- *Standard deduction*. Because this family uses the standard deduction to begin with, the biggest change for them is the higher standard deduction of $22,600 under the Bush plan.
- *Tax rate*. Under both systems, this family is in the 10 percent tax bracket. However, because of the higher standard deduction under the Bush plan, their income would be subject to tax decreases.
- *Tax credits*. The only EITC change outlined in the Bush plan is an expansion of the credit for taxpayers without children. Since this family has two children, we assume the EITC would remain the same for them under either system. As explained in Scenario 1, it's not clear whether the family would retain their $2,000 CTC.

Results:
This family would save $1,000 under the Bush plan compared with current law, because of the increased standard deduction. However, if the CTC is eliminated under the Bush plan, this family would see their refund go down $1,000, compared with current law. In that case, the expanded standard deduction would not make up for the loss of the credit.

Scenario 3: Middle-income single filer living in New York
Pays additional $1,089

- Single filer
- Owns co-op in Queens, NY
- Wages of $80,000
- Itemized deductions totaling $18,300 ($6,800 state/local tax; $4,000 real property tax; $6,000 mortgage interest; $1,500 charitable contributions)

What would change under the Bush tax plan:

- *Itemized vs. standard deduction*. Under the Bush plan, the deduction for state and local income tax would be eliminated, and the deductions for real property tax and mortgage interest would be capped at 2 percent of AGI – reducing available itemized deductions to $4,700. The expanded standard deduction of $11,300 is therefore more advantageous.
- *Tax rate*. This filer is in the 25 percent marginal rate bracket under either system.

Results:
This single filer would have a $1,089 increase in taxes under the Bush plan. Unlike in Scenario 1, the higher standard deduction does not make up for the loss of more than $13,000 in itemized deductions. In addition, the elimination of the 15 percent bracket means that more of this filer's income is taxed at 25 percent.

Stay tuned

The details are crucial when it comes to any tax plan. As presidential campaigns progress and additional tax plans are made available, The Tax Institute will analyze the impact using real-life scenarios to determine the potential effects of candidates' plans on taxpayers of varying income levels, filing status, and family makeup.

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Side-by-side comparisons

Scenario 1: Middle-income family of four living in Missouri:

	Current law	Bush plan	Comments
Wages / AGI	100,000	100,000	
Itemized deductions			
State/local income tax	5,000	-	S/L income tax ded eliminated
Real estate tax	2,500	2,000	Capped at 2% of AGI
Property tax	1,000	1,000	
Mortgage interest	7,000	2,000	Capped at 2% of AGI
Charitable	2,000	2,000	
Total itemized	17,500	~~7,000~~	
Standard deduction	~~12,600~~	22,600	Increased std ded > itemized
Personal exemptions (4)	16,000	16,000	
Taxable income	66,500	61,400	
Tax before credits	9,053	6,140	
Child tax credit	2,000	2,000	
Tax liability	7,053	4,140	
Tax saving if CTC remains		2,913	
Tax saving if CTC eliminated		913	

Scenario 2: Lower-income family of four living in Missouri

	Current law	Bush plan	Bush plan/no CTC	Comments
Wages / AGI	45,000	45,000	45,000	
Standard deduction	12,600	22,600	22,600	Increased std ded
Personal exemptions (4)	16,000	16,000	16,000	
Taxable income	16,400	6,400	6,400	
Tax before credits	1,640	640	640	
Child tax credit	2,000	2,000	-	
EITC	1,042	1,042	1,042	
Tax liability (refund)	(1,402)	(2,402)	(402)	
Tax saving (refund incr)		1,000		
Refund decrease if CTC eliminated			(1,000)	

Scenario 3: Middle-income single filer

	Current law	Bush plan	Comments
Wages / AGI	80,000	80,000	
Itemized deductions			
State/local income tax	6,800	-	S/L income tax ded eliminated
Real estate tax	4,000	1,600	Capped at 2% of AGI
Mortgage interest	6,000	1,600	Capped at 2% of AGI
Charitable	1,500	1,500	
Total itemized	18,300	~~4,700~~	
Standard deduction	~~6,300~~	11,300	Increased std ded > itemized
Personal exemption	4,000	4,000	
Taxable income	57,700	64,700	
Tax liability	10,219	11,308	32,450 @ 10%; balance @ 25%
Tax increase		(1,089)	