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A Triple Whammy in Tax Hikes: How the AMT, Repealing the Bush Tax Cuts, and the Social Security Wage Cap Would Raise Taxes on Millions of Americans

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With the Democratic majority in Congress considering new spending plans, there is renewed concern in Washington about whether Congress will raise revenues to pay for new spending. Speaker of the House Nancy Pelosi has specifically endorsed increasing taxes on wealthy taxpayers, and other potential tax increases have been mentioned. The House leadership is reportedly discussing raising the Social Security wage cap and repealing some of the Bush tax cuts. Meanwhile, millions of Americans will be sucked into the vortex of the onerous Alternative Minimum Tax (AMT).

Each of these would raise taxes on millions of Americans and harm the economy. Taken together, they would create a triple whammy that would subject millions of Americans to three tax hikes at once.

Given the growing appetite for more spending on Capitol Hill and the recent return to pay-as-you-go (PAYGO) budgeting, Congress will likely consider these tax increases. Members of Congress, the national press, and especially taxpayers should understand just how many people would be affected by such legislation.

The Alternative Minimum Tax. The AMT is a pernicious tax that guarantees tax increases for millions more Americans each year. Moreover, it forces taxpayers to calculate their tax liability multiple times. The AMT also prevents some taxpayers from receiving the full value of the Bush tax cuts.[1] Unless Congress enacts another "hold harmless" provision, the AMT would hit the most taxpayers of these tax increases:

- Twenty million more tax filers would be forced to pay on average almost $3,000 more in taxes due to the AMT this year.

The problem with extending the hold harmless provision is that it costs almost $50 billion for one year alone. Congress would have to find a way to pay for this if it is serious about PAYGO discipline. If AMT is not reformed, approximately one in four income taxpayers will be subject to the AMT by 2013.[2] But if an AMT fix is offset by raising other taxes, it would still be a tax increase and a move in the wrong direction.

The Social Security Wage Cap. Another proposal is to raise revenues by increasing the Social Security wage cap. This idea has been promoted by Members of Congress and several influential

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groups.[3] In 2007, the wage cap is scheduled to be $97,500 under current law. Raising the wage cap would impact many Americans:

- An increase in the wage cap would subject 10.3 million American workers to sharply higher taxes.
- On average, those affected would pay over $5,600 more in payroll taxes each year.
- Almost three million small business owners and entrepreneurs would be hit especially hard by this tax increase.
- Many schoolteachers, nurses, police officers, and similar professionals would be hit with higher taxes.[4]

Increasing the Social Security wage cap is the wrong solution to Social Security's long-term financing problem, and it is not the way to achieve retirement security for Americans. This proposal would subject millions of Americans to a painful tax increase that would harm the economy and do little to extend the solvency of Social Security.[5]

Repealing the Bush Tax Cuts. In 2001 and 2003, President Bush signed into law a series of tax cuts that reduced marginal tax rates on income and the taxation of capital and ended the marriage penalty. Speaker Pelosi is the most prominent politician to call for repeal of the Bush tax cuts for the wealthy. However, repealing the Bush tax cuts—especially the lower tax rates on ordinary income, the lower rate and one-year repeal of death taxes, and the lower rates on capital gains and dividend income—would reduce investment, job growth, and the incentives to work for many Americans:

- Approximately 4.7 million tax filers, earning over $200,000, would pay higher taxes if the Bush tax cuts were repealed.[6]
- The average tax increase would be over $14,000 per tax return.

The Triple Whammy. The impact of any of these tax increases alone would be worrisome. But many Americans would be subject to more than one of these tax increases. The majority of taxpayers affected by a repeal of the Bush tax cuts would also be subject to an increase of the Social Security wage cap—a double whammy. Between these two tax increases, over 14 million taxpayers would face over $20,000 more in taxes each year. Their marginal tax rate would increase to almost 50 percent, not including any state or local taxes.

Worse yet, over two million tax filers would be hit by all three tax increases—a triple whammy. These taxpayers earn above $200,000 in adjusted gross income, have earnings above the wage cap, and would start to pay additional taxes as a result of the alternative minimum tax.[7] Some of these taxpayers would face marginal tax rates in excess of 50 percent on earned income—a level not seen in over 20 years.

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1. However, if the Bush tax cuts are repealed, some individuals may no longer be subject to the AMT because their regular tax liability would increase. Their total tax liability will remain roughly the same, but they will pay taxes under the traditional tax system rather than the Alternative Minimum Tax.
2. If the AMT is not fixed, it will affect approximately one out of every seven of the 130 million tax filers projected for 2007. That number will increase as more taxpayers are forced to pay the AMT.
3. Congressman Robert Wexler (D-FL) and the AARP, among others.
4. David John and Rea S. Hederman, Jr., "Raising the Wage Cap: No Painless Solution to Social Security's Fiscal Woes" Heritage Foundation *WebMemo* No. 1319, January 22, 2007, at *www.heritage.org/Research/SocialSecurity/wm1319.cfm*.
5. A 2003 Social Security Administration report found that raising the wage cap would extend solvency by less than a decade. This is because the increased Social Security taxes would generate new future liabilities. Chris Chaplain, Actuary, and Alice H. Wade, Deputy Chief Actuary, Social Security Administration, "Estimated Long-Range OASDI Financial Effects of Eliminating the OASDI contribution and Benefit Base."
6. These numbers are based on the Center for Data Analysis tax model and the following policies: increasing the top two marginal tax rates, raising the tax rate on capital gains to 20 percent, and ending the dividends exclusion.
7. The number of filers was calculated by estimating the number of filers who are affected by the AMT, have wages and salary above the Social Security wage cap, and report adjusted gross income above $200,000. It is assumed that the 20 million new AMT filers would have roughly the same characteristics as current AMT payers and others with earnings and income that meet the above specifications.

State-by-State Impact of Three Proposed Tax Hikes

State	Workers Affected by Raising the Wage Cap: Number	Workers Affected by Raising the Wage Cap: Percent of Total Affected	Tax Filers Impacted by AMT Increase: Number	Tax Filers Impacted by AMT Increase: Percent of Total Affected	Tax Filers Impacted by Bush Tax Cuts Repeal: Number	Tax Filers Impacted by Bush Tax Cuts Repeal: Percent of Total Affected
Alabama	119,760	1.16%	88,902	0.46%	44,056	0.94%
Alaska	22,583	0.22%	15,066	0.08%	8,498	0.18%
Arizona	153,031	1.48%	195,482	1.00%	75,097	1.61%
Arkansas	48,039	0.47%	78,447	0.40%	22,421	0.48%
California	1,623,053	15.74%	3,836,511	19.66%	721,927	15.45%
Colorado	215,438	2.09%	202,749	1.04%	81,040	1.73%
Connecticut	184,892	1.79%	508,094	2.60%	112,393	2.40%
Delaware	31,189	0.30%	40,909	0.21%	13,012	0.28%
District of Columbia	44,160	0.43%	74,399	0.38%	17,459	0.37%
Florida	667,428	6.47%	749,715	3.84%	302,550	6.47%
Georgia	279,585	2.71%	462,131	2.37%	127,286	2.72%
Hawaii	40,238	0.39%	61,655	0.32%	16,504	0.35%
Idaho	36,570	0.35%	52,180	0.27%	12,782	0.27%
Illinois	449,804	4.36%	709,198	3.63%	229,696	4.91%
Indiana	129,598	1.26%	184,040	0.94%	62,065	1.33%
Iowa	82,537	0.80%	107,820	0.55%	27,513	0.59%
Kansas	69,242	0.67%	121,627	0.62%	32,103	0.69%
Kentucky	104,539	1.01%	150,778	0.77%	36,727	0.79%
Louisiana	95,120	0.92%	114,745	0.59%	37,998	0.81%
Maine	36,129	0.35%	73,729	0.38%	13,966	0.30%
Maryland	311,234	3.02%	650,150	3.33%	121,549	2.60%
Massachusetts	363,424	3.52%	734,441	3.76%	164,845	3.53%
Michigan	304,934	2.96%	439,077	2.25%	121,685	2.60%
Minnesota	181,893	1.76%	363,514	1.86%	87,105	1.86%
Mississippi	60,948	0.59%	49,682	0.25%	18,383	0.39%
Missouri	149,557	1.45%	219,099	1.12%	63,154	1.35%
Montana	16,000	0.16%	38,392	0.20%	8,480	0.18%
Nebraska	42,179	0.41%	83,886	0.43%	18,313	0.39%
Nevada	79,773	0.77%	85,544	0.44%	39,397	0.84%
New Hampshire	52,337	0.51%	70,813	0.36%	23,628	0.51%
New Jersey	532,785	5.17%	1,441,160	7.38%	247,892	5.30%
New Mexico	57,848	0.56%	55,633	0.29%	16,123	0.34%
New York	719,999	6.98%	2,763,862	14.16%	390,680	8.36%
North Carolina	225,583	2.19%	440,430	2.26%	105,832	2.26%
North Dakota	16,977	0.16%	14,895	0.08%	5,865	0.13%
Ohio	282,730	2.74%	763,061	3.91%	125,830	2.69%
Oklahoma	95,689	0.93%	100,654	0.52%	30,600	0.65%
Oregon	110,650	1.07%	234,241	1.20%	44,702	0.96%
Pennsylvania	366,547	3.55%	724,473	3.71%	177,716	3.80%
Rhode Island	37,641	0.36%	85,246	0.44%	16,484	0.35%
South Carolina	75,280	0.73%	164,787	0.84%	41,960	0.90%
South Dakota	17,985	0.17%	13,541	0.07%	7,747	0.17%
Tennessee	146,752	1.42%	111,463	0.57%	44,056	0.94%
Texas	698,894	6.78%	748,558	3.84%	302,133	6.46%
Utah	70,741	0.69%	87,061	0.45%	24,500	0.52%
Vermont	17,726	0.17%	37,209	0.19%	153,424	3.28%
Virginia	394,372	3.82%	563,335	2.89%	7,840	0.17%
Washington	270,168	2.62%	223,337	1.14%	103,421	2.21%
West Virginia	21,745	0.21%	39,018	0.20%	11,089	0.24%
Wisconsin	144,694	1.40%	328,361	1.68%	66,228	1.42%
Wyoming	13,143	0.13%	13,333	0.07%	6,386	0.14%
Total	**10,313,162**		**19,516,430**		**4,592,142**	

Source: Center for Data Analysis calculations
Note: AMT distribution by state assumes that the new AMT payers will follow the current distribution of AMT payers. Taxpayers outside the fifty states and the District of Columbia are excluded.

This group of taxpayers is especially important to economic growth because it includes many entrepreneurs and investors who create jobs and growth. Thus, the triple tax whammy would also harm the economy and opportunities for all Americans.

Conclusion. While many in Congress have publicly espoused the laudable goal of restraining spending, which would slow the growing financial burden on current and future generations, they should not pay for new spending by raising taxes. Instead, Congress should focus on limiting federal spending and restraining the growth in entitlement costs. The three tax increases would harm the economy and subject too many taxpayers to significantly higher marginal tax rates, with millions suffering the triple whammy.

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