The Daily Dish

How Not to Reform the TCJA

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What will be the elements of the tax legislation that must pass next year to avoid a complete sunset of the 2017 Tax Cuts and Jobs Act (TCJA)? It is far from obvious, but one popular element is the child tax credit (CTC). Indeed, both presidential campaigns favor not just preserving the TCJA version of the credit but increasing the credit further. In addition to the social welfare impacts, advocates point to evidence that such an increase would improve outcomes for children, increase educational attainment, raise future productivity, and increase earnings of future workers. What's not to like?

There is the issue of how to pay for such a program, but conveniently enough, the left is fully in favor of raising the corporate rate up to, say, 28 percent. Big corporations are sufficiently out of step with the populist times that even some on the right are comfortable advocating for a higher corporate rate. In this worldview, the 21-percent rate is simply a giveaway and raising the rate would have little economic consequence.

You can see where this is going. Expand the CTC permanently and pay for it by raising the corporate rate. The policy's economic virtue outweighs any minor economic damage and, somehow, the United States has a more productive economy. At least that is how the argument goes.

But is this argument true? AAF retained EY's Quantitative Economics and Statistics Group to examine the macroeconomic impacts of permanently expanding the CTC, paid for by raising the corporate tax rate. We learned three key things. First, making permanent the American Rescue Plan version of the CTC would cost approximately $1.4 trillion over the 2025–2034 budget window. Second, financing the expanded CTC with a hike in the corporate tax rate would require a full 10-percentage-point increase. That is a lot more than Eakinomics had expected.

But it is worth it, right? Having the big CTC creates enough good news that the higher corporate rate does not matter. Turns out, this is not even close to true.

EY finds that even in the best-case scenario for impacts of the CTC, in the long run, labor supply would fall by 0.4 percent, after-tax wages by 0.3 percent, consumption by 0.1 percent, investment by 1.2 percent, and GDP by 0.4 percent. It is just macroeconomic bad news. Sure, in the near term a bigger CTC can prop up household spending, but the investment and GDP impacts are negative.