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Individual Income Tax Rates Under the Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16)

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Summary

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) reduces marginal income tax rates for individuals. The Act creates a new 10% marginal income tax bracket and reduces the four top marginal tax rates to 25%, 28%, 33% and 35%. The Act also widens the 15% marginal income tax bracket for married couples filing joint returns. These changes are phased in over a period of several years.

The EGTRRA tax cuts are scheduled to expire at the end of calendar year 2010. In the 107th Congress, the House passed several bills that would have extended the EGTRRA tax cuts beyond 2010. The Senate did not adopt these bills. It is likely that the 108th Congress will revisit the issue of making the EGTRRA tax cuts permanent.

Additionally, in response to continued sluggish economic performance, President Bush unveiled a new tax stimulus plan in early January 2003. As part of his stimulus plan, President Bush has proposed accelerating the phase-in of some of the EGTRRA tax cut provisions. The President's proposal includes accelerating all of the EGTRRA tax rate cuts to 2003 and accelerating the expansion of the 10% marginal income tax bracket to 2003. The Treasury Department estimates that the 10-year revenue cost of these two changes would be $112 billion.

This report will be updated as legislation action warrants.

Since 1986, individual income tax rates have been changed on four occasions. The number and level of marginal income tax rates were significantly reduced under the Tax Reform Act of 1986 (P.L. 99-514). The 1986 Act reduced the number of statutory marginal income tax rates from 14 to two. The two new marginal income tax rates were 15% and 28%. The Omnibus Budget Reconciliation Act of 1990 (P.L. 101-508) added a new statutory marginal income tax rate of 31%. The Omnibus Budget Reconciliation

Act of 1993 (P.L. 103-66) added two new marginal income tax rates, 36% and 39.6%, to the tax rate schedule.[1]

On May 26, 2001, the House and Senate approved The Economic Growth and Tax Relief Reconciliation Act of 2001 (H.R. 1836). The Act was signed into law (P.L. 107-16) by President George W. Bush on June 7, 2001. The Act makes three major changes to the individual income tax rate structure. It creates a new 10% marginal income tax bracket for a portion of taxable income that had been taxed at a 15% marginal rate, it reduces the four top marginal income tax rates over the 2001 to 2006 time period, and it widens the 15% tax bracket for married couples filing joint returns.

The new 10% marginal income tax rate bracket will apply to the first $12,000 of taxable income for married couples filing jointly, the first $10,000 of taxable income for heads of households, and the first $6,000 of taxable income for single individuals. In 2008, the $6,000 amount for single individuals will increase to $7,000 and the $12,000 amount for married taxpayers filing joint returns will increase to $14,000. Starting with tax year 2009, these marginal tax rate bracket amounts will be indexed for inflation.

In practice, the new 10% tax rate bracket will be implemented in tax years beginning after December 31, 2001. For the 2001 tax year, instead of an actual 10% tax rate bracket, the Act created a 10% rate reduction credit.[2] The credit was used as a means of providing immediate tax reductions in hopes of stimulating the economy.

Under prior income tax law, the marginal tax rate structure for individuals consisted of five rates: 15%, 28%, 31%, 36% and 39.6%. The 2001 Act reduces the top four marginal income tax rates over a 6-year period to 25%, 28%, 33% and 35% respectively. The schedule for these phased-in rate reductions is shown in the following table.

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[1] For more information on these tax rate changes, see CRS Report RL30007, *Individual Income Tax Rates: 2001*, by Gregg Esenwein.

[2] For a description of the rate reduction tax credit and a discussion of its distributional effects, see CRS Report RS20939, *The Rate Reduction Tax Credit (the "Tax Rebate") in P.L. 107-16*, by Gregg Esenwein and Steve Maguire.

The Schedule of Marginal Income Tax Rate Reductions Under P.L. 107-16

	--------------------Prior Law Rates------------------			
	28%	31%	36%	39.6%
	-------------------New Law Rates------------------			
2001[3]	27%	30%	35%	38.6%
2002	27%	30%	35%	38.6%
2003	27%	30%	35%	38.6%
2004	26%	29%	34%	37.6%
2005	26%	29%	34%	37.6%
2006	25%	28%	33%	35%

The Act also increases the width of the 15% tax bracket for married couples filing joint returns to twice the width of the 15% tax bracket for single returns. This provision is phased-in over a four year time period starting in 2005. The end point of the 15% tax bracket for joint returns is scheduled to be 180% of the end point of the 15% tax bracket for single returns in 2005, 187% in 2006, 193% in 2007, and 200% in 2008 and subsequent years.

The widening of the 15% tax bracket for joint returns was included as a means of mitigating the marriage tax penalties that can occur in the individual income tax.[4]

However, all of the changes in the Economic Growth and Tax Relief Reconciliation Act of 2001(including the tax rate changes) will expire (sunset) after 2010. Congress included the sunset in EGTRRA to avoid a Byrd rule violation in the Senate. The Byrd rule prohibits "extraneous matter" in reconciliation legislation. Under the rule, extraneous matter includes, among other things, language that would cause an increase the budget deficit (or reduce budget surpluses) in a fiscal year beyond those covered by the reconciliation legislation. As a result of the Byrd rule, EGTRRA contained language providing for the expiration of all of its provisions at the end of calendar year 2010.

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[3] Since this change is implemented on July 1, 2001, the effective marginal income tax rates for the entire year are 27.5%, 30.5%, 35.5%, and 39.1%.

[4] The Act also increases the standard deduction for joint returns to twice the size of the standard deduction for single returns. This change is scheduled to be phased in over the 2005 to 2009 time period. For more information on marriage tax penalties and bonuses under the individual income tax see CRS Report RL30800, *The Federal Income Tax Treatment of Married Couples: Background and Analysis,* by Gregg Esenwein.