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Replacing the personal exemption with a tax credit

Our data base for addressing this question is 1979 preliminary returns and the summary data on years prior to 1979. This allows estimates of the impact on historical revenues of proposed changes such as the one considered. Projecting the revenue impact of proposed changes into the future is normally based on the revenue forecast for the existing law which are not available to us. For example an interest exemption in 1979 would have reduced revenue by about \$80 million or 10.6 percent of total revenue. Applying the 10.6 percent to forecast 1981 revenue would be a much better estimate than using the \$80 million amount.

In this case we are in a little better shape because the personal exemption is a fixed dollar amount (indexing ignored) and both the number of exemptions and the number of credits are related not to income but to the number of exemptions (dependent and over 65). Raising incomes will still affect marginal tax rates,

but revenue impact is limited because most taxpayers are already at the highest rate. Projections to futures can reasonably be made based on growth in the number of exemptions rather than growth in income or revenue.

The personal exemption remained at \$750 between 1975 and 1978. Over this period we averaged a 5 percent per year increase in the number of personal exemptions (only 3.2 percent in 1978). I assume no increase in 1979 because of the increase in the personal exemption to \$1,000. Thereafter, I assume 5 percent per year.

A rough calculation from preliminary 1979 data indicates the following increased revenues per exemption on taxable returns:

| Credit Amount | Revenue Increase \$ |
|---------------|------------------------|
| 50. | 41. |
| 60 | 31. |
| 70 | 21. |
| 80 | 11. |

This provides the following estimate of 1981-83 revenue impact

| YEAR | Number of Exemptions | Credit Amount | | | |
|------|----------------------|---------------|-------------|-------------|-------------|
| | | 50 | 60 | 70 | 80 |
| 1980 | 2,486,000 | 101.9 | 77.1 | 52.2 | 27.4 |
| 1981 | 2,610,000 | <u>107.0</u> | <u>80.9</u> | <u>54.8</u> | <u>28.7</u> |
| | | 2089 | 158,0 | 107,0 | 56.1 |