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Where the Rubio Tax Plan Falls Short

The child credits and new rates pit groups against one another in a way that across-the-board rate cuts do not.

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Can a technical debate over tax plans trigger an identity crisis in the Republican Party? Apparently, yes. Sens. Marco Rubio of Florida and Mike Lee of Utah recently launched their "Economic Growth and Family Fairness Tax Reform Plan." Within a few days former presidential candidate Steve Forbes fired back with a flat-tax plan. In policy circles the big question is whether Jeb Bush and Scott Walker will back "Rubio-Lee" or "flat tax."

The Rubio-Lee plan takes a different approach in the name of achieving the old Republican goal of growth. But the approach is so different that it can hurt the viability of the Republican Party and even set in train changes that may slow future growth.

Signaling opportunity throughout the tax code has long been the basis of the philosophy known as supply-side economics, or "Reaganomics." Reaganomics treats even individual wage earners as entrepreneurs. The marginal rate to which a worker is subject under the progressive tax schedule is crucial.

A higher rate on the next dollar a worker earns discourages him from working more. The highest tax bracket is especially important as top earners produce the most and innovate the most. Incentivized by a low top rate, they will increase earnings more than those further down the income scale. That top marginal rate also functions as a symbol of how society rewards enterprise.

Of course, Republicans have also long routinely backed targeted tax devices for groups: the child credit, education credits and so on. But such mini-entitlements were add-ons to build political coalitions that could support the main cause: dramatic across-the-board rate reductions.

Broadly speaking, the evidence from the Reagan years supports the traditional Republican emphasis on the top marginal rate. A stream of revenues stronger than the Treasury had predicted, $11 billion more, followed Reagan's 1981 cut in the top rate to 50% from 70%.

The topmost earners responded especially vigorously, working and earning more. As economist Lawrence Lindsey pointed out years ago (Journal of Public Economics, 1987), about 40% of the extra revenue collected came from the top taxpayer group. As Mr. Lindsey noted in his 1991 book, "The Growth Experiment," the top 0.1% of taxpayers paid 14% of the taxes in 1986, compared with only 7% in 1981.

The Rubio-Lee plan lowers the marginal rate on the corporate income tax significantly, to 25% from 35%. But on the personal side their proposal drops the top marginal rate on individual income by a puny 4.6 percentage points, to 35% from 39.6%.

By comparison the top rate in the 1986 tax law was 28% (down from 50%); 33% in George W. Bush's 2000 proposal, and 28% in Mitt Romney's 2012 proposal. Mr. Forbes's flat tax is 17%.

What's more, Rubio-Lee lowers tax thresholds drastically. Singles with taxable income as low as $75,000 find themselves entering the 35% top bracket; for couples the top rate applies after $150,000. Currently, individuals don't hit the 35% bracket until $411,501, and the same holds for couples. The very top current rate, 39.6%, doesn't set in for individuals until $413,201 and for couples until $464,851 in taxable income. It is no wonder that Democratic and liberal strategists have singled out the Rubio-Lee plan for praise.

Rubio-Lee also raises the child credit to an unusually generous $2,500 per child, available even to wealthy families. Current child credits feature restrictions on use, and income limits. In short, the senators are flipping traditional GOP priorities. Add-ons for groups trump pro-growth cuts.

Since Rubio-Lee taxes income below the $75,000 and $150,000 thresholds at a low 15%, it is unclear how many Americans would end up paying more in taxes overall than they do at present. But the plan pits groups against one another in a way that across-the-board cuts do not. Couples with several children who live in low-tax states with lower-cost housing are entitled to breaks. Couples who live in high-tax states and are childless are not. Businesses enjoy lower rates than wage earners.

The nonpartisan Tax Foundation recently estimated that Rubio-Lee would increase economic growth so that by 2025 the economy would be 15% larger than otherwise, almost entirely due to business tax cuts. The effect of the child credit on growth is reckoned at zero. Dan Mitchell of the Cato Institute notes that if Rubio-Lee dropped all the preferences it contains, old and new, the plan could drop its top income-tax rate to 20% or lower.

Growth fueled by corporate tax cuts may suffice to offset costly items like the child credit on paper. But the Tax Foundation's scoring doesn't capture the cost of resentment between groups, or that of a tax code that emphasizes families over individuals. Rubio-Lee does not make enough effort to encourage that group of top income earners to strive.

A Republican plan that emphasizes "fairness" to this extent risks establishing a trend. Rubio-Lee sets the stage for greater tax gifts to particular groups in the future, with eventual hikes to the top marginal rate. If the self-styled party of enterprise does not emphasize the individual, no one will.

The overall seriousness of the Rubio-Lee plan is commendable. But to make the plan worth endorsing requires a major change: scrapping the child credit and replicating the business side cuts on the individual side.