

Unpacking the Consequences of the New US Tax and Budget Legislation

Peterson Institute for International Economics
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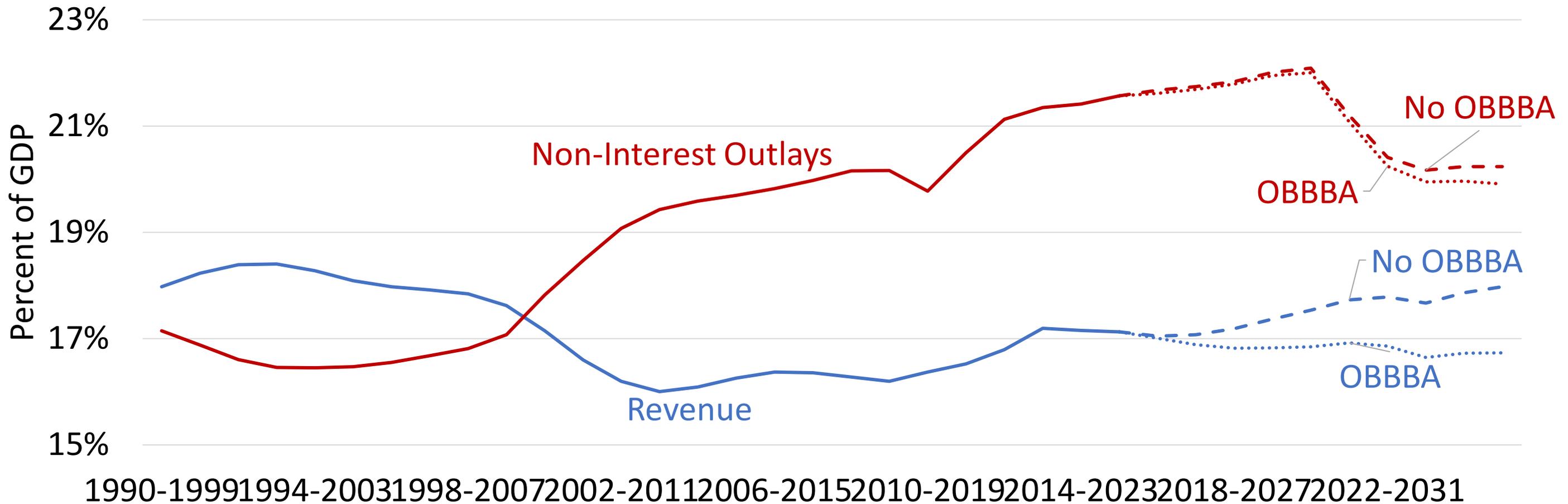
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The Fiscal Picture Before OBBBA and CBO Projections After

Revenue and Non-Interest Outlays: 10-Year Rolling Average



Notes: Historical data are from OMB's *Historical Tables*. Budget projections without the OBBBA are based on CBO's *Budget and Economic Outlook: 2025 to 2035* (January 2025). Budget projections with the OBBBA are the author's calculations using CBO's *Estimated Budgetary Effects of Public Law 119-21, to Provide for Reconciliation Pursuant to Title II of H. Con. Res. 14, Relative to CBO's January 2025 Baseline* (July 21, 2025).

Major Growth Provisions

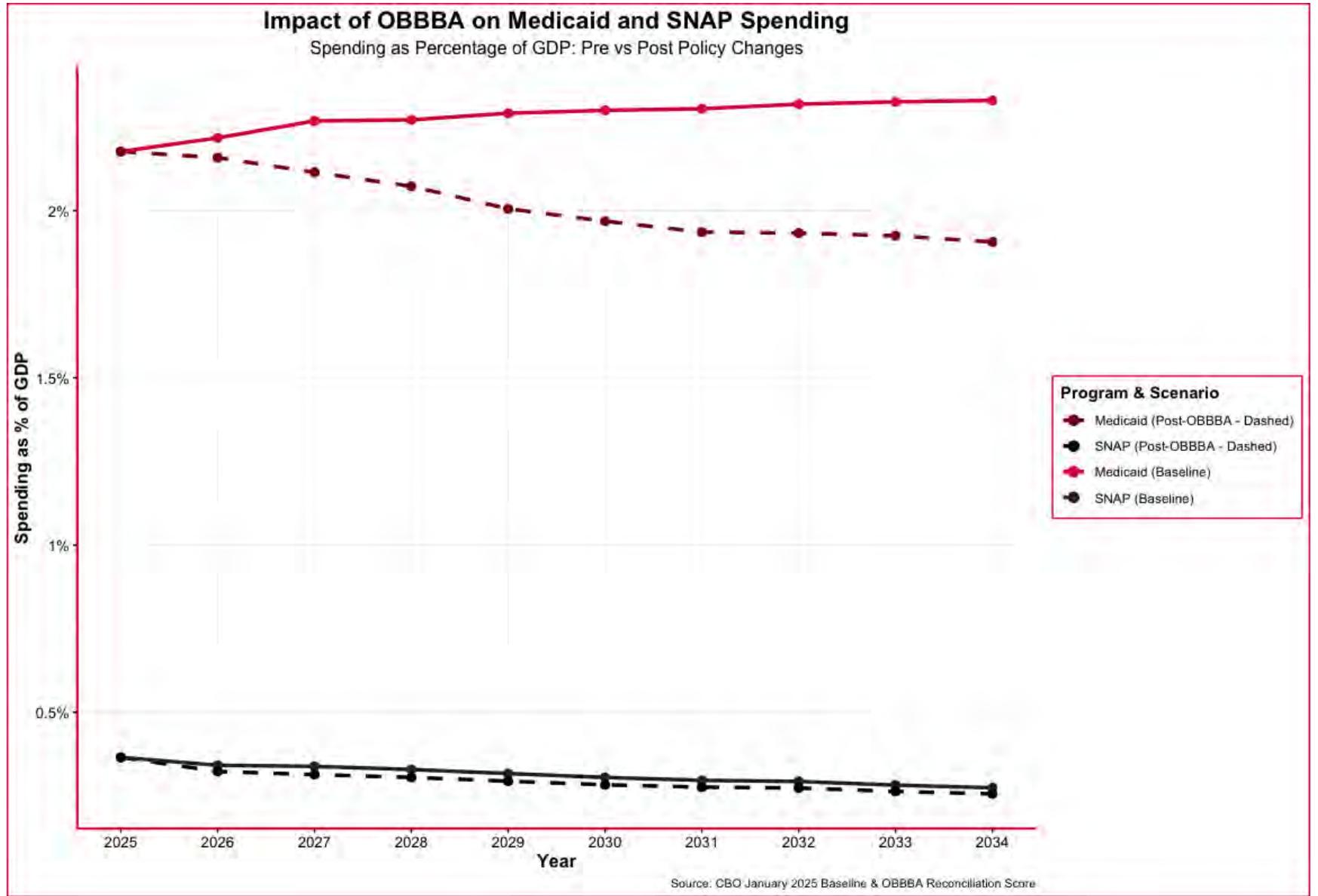
Provision	10-Year Revenue Effect	Long-Term GDP Effect
Permanent Full Expensing of Equipment	\$363	0.60%
Permanent Full Expensing of R&D	\$141	0.10%
EBITDA	\$61	0.10%
Rate Reductions	\$2,192	1.10%
Qualified Business Income Deduction (199a)	\$737	0.50%

Notes: Revenue effects are based on conventional estimates in JCT's *Estimated Revenue Effects Relative To The Present Law Baseline Of The Tax Provisions In "Title VII – Finance" Of The Substitute Legislation As Passed By The Senate To Provide For Reconciliation Of The Fiscal Year 2025 Budget* (July 1, 2025). Growth effects from the Tax Foundation's *One Big Beautiful Bill Act Tax Policies: Details and Analysis* (July 4, 2025).

- Taxes have large effects on business investment and household taxable income
 1. Firm Investment and the User Cost of Capital: New U.S. Corporate Tax Reform Evidence (Hartley, Hasset, and Rauh, 2025)
 - Examines TCJA variation across BEA asset classes
 - Uses Auerbach and Hasset (1991), Cummins et al (1994, 1995, 1996) specifications
 - Findings consistent with user cost elasticities of investment of -1.8 to -3.5, vs. CBO's 0.7
 2. Behavioral Responses to State Income Taxation of High Earners: Evidence from California (Rauh and Shyu, 2024):
 - California saw 30% increase in top bracket marginal tax rate
 - Elasticity of taxable income (ETI) of 2.6-3.0 for top bracket taxpayers
- Effects are much larger than Congressional scorekeepers (JCT/CBO) assume
- Individual ETI effects may work not only through GDP but also avoidance/evasion

Spending Reforms in OBBBA

- Congress reduced the rate of expenditures for Medicaid, SNAP, and green energy subsidies.
 - SNAP cut by \$68.6 billion from 80 hours/month work requirements for able-bodied adults
 - Medicaid cut by \$950 billion from community engagement requirements, provider taxes, and state directed payments (15% reduction); combined \$1.02 trillion in reductions over 10 years.
 - Main reductions in SNAP and some in Medicaid from Work/Volunteer/School requirement-80 hours/month for able bodied



Pre-OBBBA (Baseline): Congressional Budget Office. (2025, January). *The Budget and Economic Outlook: 2025 to 2035*. Retrieved from <https://www.cbo.gov/data/budget-economic-data#3>

Post-OBBBA: Congressional Budget Office. (2025, July 21). *Cost Estimate: Public Law 119-21, to Provide for Reconciliation Pursuant to Title II of H. Con. Res. 14* (Publication No. 61570). Retrieved from <https://www.cbo.gov/publication/61570>

- Under behavioral responses consistent with recent studies, revenue impacts of OBBBA tax cuts will be considerably smaller than CBO/JCT projections
 - Due to effects in both conventional and dynamic scores
 - Plus: these are pro-growth tax cuts which do increase long-run GDP
- Exactly how much? Need CBO and JCT to fully publish their models and source code
 - CTC and other non-growth provisions still will be costly
- Material spending cuts are primarily in Medicaid, ~0.3% of GDP
- Relative to 2026 CBO pre-OBBBA projection of 5.5% of GDP deficit, the deficit remains very substantial
- Congress should be very concerned about interest cost burden
 - I calculate 2035 interest as share of non-Social Security revenue at 30%
 - Tax increases will be counterproductive due to elasticities and growth effects, need increased focus on spending