Re: How to Fix the Wealth Disparity Gap caused by Trump Administration Tax Plan
To: Kevin Hasset - Assistant to the President for Economic Policy
From: George T. Johnson - Undergraduate B.S Economics & Public Policy, University of Houston

The Problem

The Trump administration has proposed and began implementing a plan to eliminate federal income tax and raise tariffs. This would have significant effects on the United States (U.S.) economy. Since the republicans hold 53 seats in the current senate, I believe it is necessary to prepare possible policy alternatives if this comes to fruition.

My concern is grounded in my academic research as a student. My study conducted following studies of previous economists, Hellman (2022), Steindel (2001), Cornforth (2024), Goss and Chang (2018), and Kogan (2018). These studies that I utilized as a foundation demonstrate that tax and tariff levels significantly impact individuals' economic standing. Data models I produced seem to suggest that these policies will drastically increase the wealth disparity, making the poor poorer.

To mitigate the impact, policymakers must reallocate funding from existing programs to make up for the 50% gap this will leave in the government's spending budget. This will provide a smoother transition into the economic age while maintaining support for social security, Medicare, and national defense.

Changes in Wealth Disparity

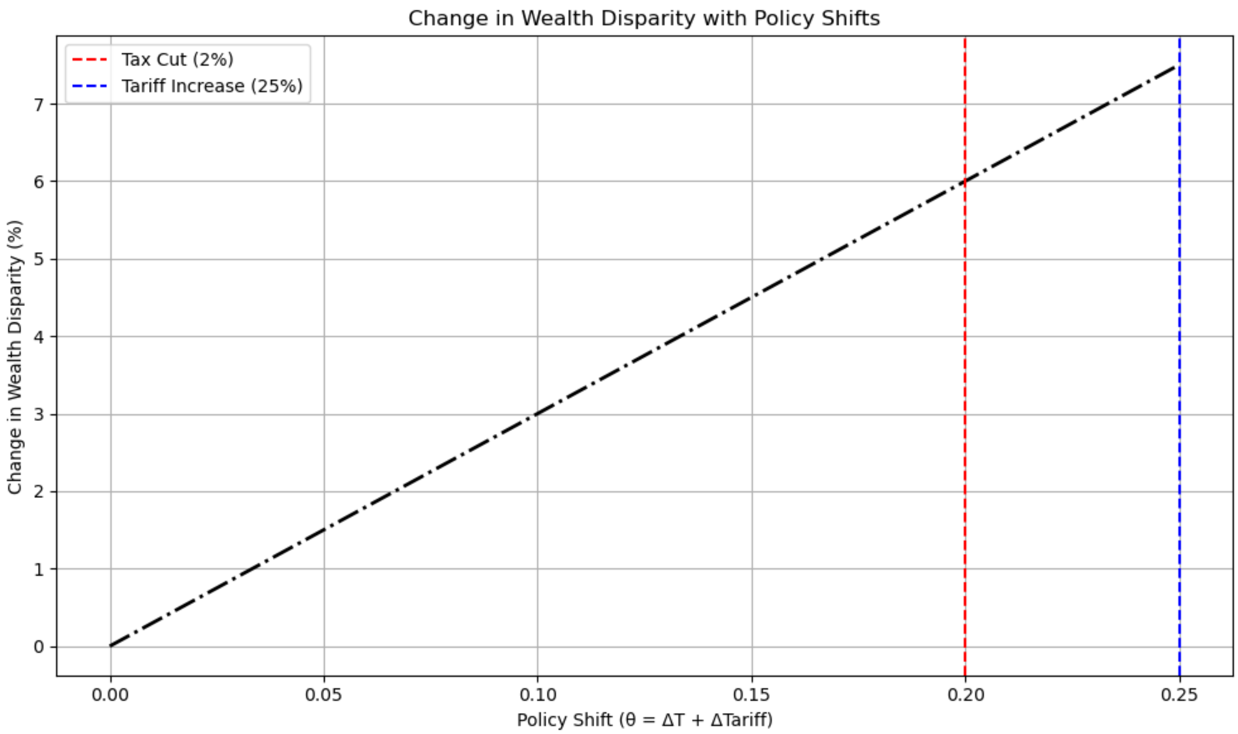
To assess the impact of the proposed tax plan, I implemented a model incorporating new tariff plans as well.

$$\Delta G = (\alpha_y + \alpha_{RR}) * (\Delta T + \Delta T_{tariff}) * G_{current}$$

- **Variables**
    - ΔG represents Wealth Disparity in %
    - α_y (0.4) and α_{RR}(0.1) are the elasticity parameters for wealth disparity
    - ΔT(0.22) is the average income tax rate the most recent completed fiscal year of 2023
    - ΔT_{tariff} (0.25) accounts for new tariffs which models the increase in cost of imported goods under the new administration
    - ΔT_{tariff} and ΔT are the policy shifts
    - $G_{current}$ is the current level of wealth disparity (60%)

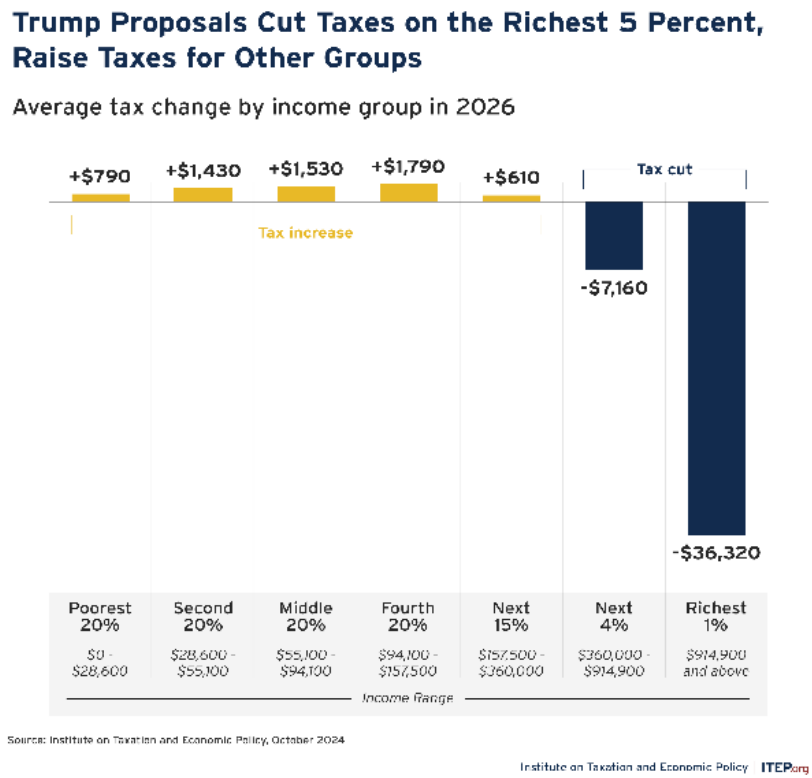
The data here is sourced from the U.S Treasury, IRS, and Tax foundation. From this equation I was able to model the equation using a mix of MATLAB and R to cross reference my results. In both cases I was given the same graph. The graph has two key elements.

1. Black dashed line
    a. Shows the trend of an increase in wealth disparity as the tariffs increase and income tax decreases
    b. The positive slope suggests that the policy change here may exacerbate the wealth disparity.
2. Red vertical lines at (0.22 and 0.25)
    a. First red line at 0.22: This marks the original average income tax at current.
    b. Second red line at 0.25: This shows the increase in tariffs
    c. These lines highlight policy thresholds, showing the analysis of these key changes in tax and tariffs.



- **Interpretation**
    - As policy shifts increase (higher tariffs and possibly other forms of tax) wealth disparity will rise
    - Suggest that these policy adjustments disproportionately affect different economic groups and increasing inequality.
    - This means that cutting income tax and raising tariffs will worsen the wealth gap significantly.

This graph shows evidence that wealth disparity will increase with the cutting or cutting of income tax. I however am not the only one who has studied this trend. Studies as recent as January 2025, have shown that most of the burden will be held by the lower income population.



This graph is directly sourced from the institute of taxation and economic policy (ITEP). ITEP's study shows that only the top 5% of earners will be benefiting this tax cut that Donald Trump is proposing. This further supports my research and my table below. As the policy shifts the probability of wealth disparity rising increases (Witten 2024).

- **Interpretation**
  - When policy shifts are between **0** and **0.094** there is only a 50% chance that wealth disparity will rise – uncertainty remains
  - When policy shifts are equal to **0.188** the risk is 80% - high risk and noticeably regressive
  - When the policy shift is greater than **0.282,** wealth disparity *will* increase if the policy reaches or grows past this point
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Wealth Disparity Response to Policy Shift

Policy Shift (θ)	Change in Wealth Disparity (%)	Probability of Wealth Disparity Increasing
0.0	0.0	0.5
0.094	2.82	0.5
0.188	5.64	0.8
0.282	8.46	1.0
0.376	11.28	1.0

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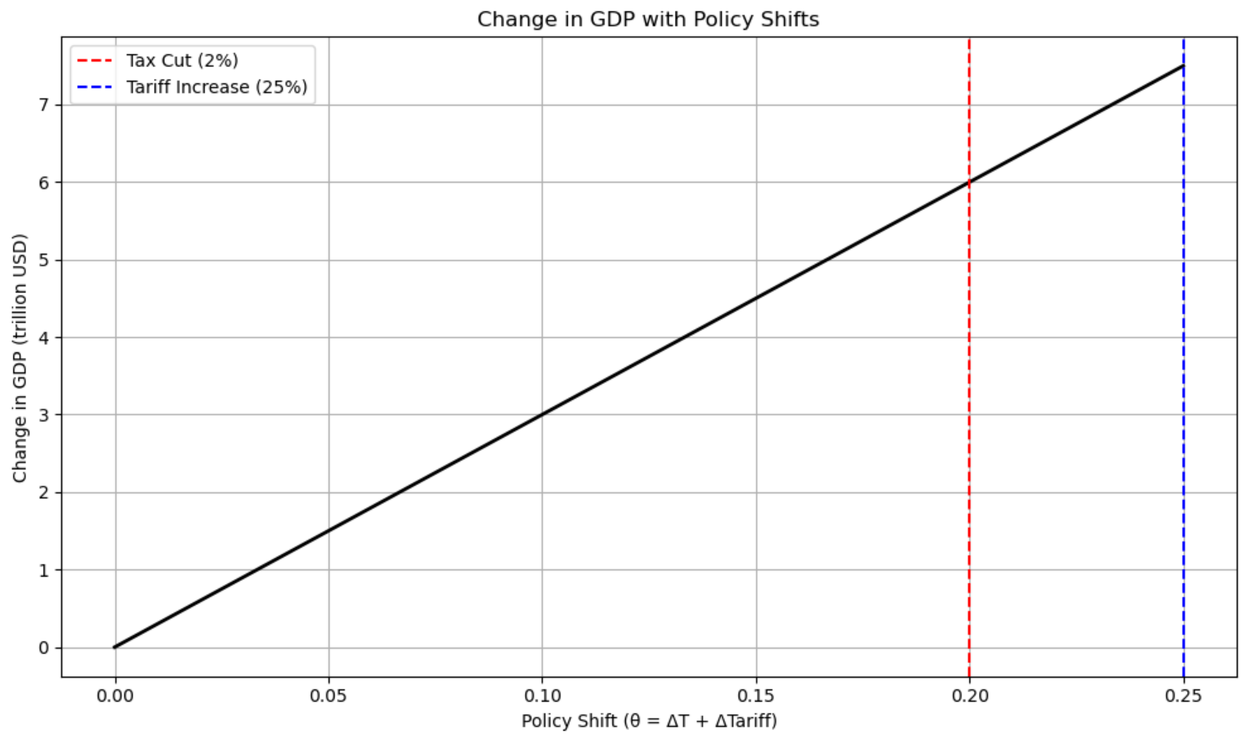
Other Economic Effects

1. **Loss of government revenue** – Income tax roughly provides 50% of federal revenue. No income tax means deficits will rise, weakening public services such as education, healthcare, and infrastructure. Gross and Chang (2018) highlight income tax as the most stable revenue source unlike volatile corporate and sales taxes.
2. **Increased burden on low-income citizens** – States without income tax (Washington) have extremely high sales tax to make up for the loss of revenue. In this state there is a strong notice of wealth disparity with Seattle having one of the highest living costs and a corresponding high homeless population per capita (Hellman, 2022).
3. **Effects on GDP** – Higher tariffs and tax shifts will alter GDP. To visualize this I utilize another equation

$$\Delta GDP = \beta_C + \beta_I + \beta_G) * \left(\Delta T + \Delta T_{tariff}\right) * GDP_{current}$$

- **Variables**

    - β_C = 0.6817 (Consumption)
    - β_I = 0.207 (Investment)
    - $\beta_G = 0.207$ $(Government\ Spending)$
    - ΔT_{tariff} (0.25) accounts for new tariffs
    - ΔT(0.22) is the original tax rate
    - $GDP_{current}$ (2023 GDP) since fiscal (FY) 2024 isn't over yet.



This graph shows that GDP has the potential in the long term to rise to $29.12 trillion. The benefits will, however, accrue to the wealthiest of earners exacerbating inequality. Imports will be lower under this new plan; however, the problem arises where the U.S. has globalized so much, we now lack infrastructure to produce domestically currently. In the long run, however, this may be beneficial in the long run.

Policy Recommendations

Making up for a loss of 50% in government spending and fixing the gap in wealth disparity will be extremely difficult without at least introducing new tax systems or a full reconstruction of government spending. Planning around these two ideas I provided policy reforms that might be able to help ease the blow this plan will have to the nation.

1. **Introduction of Value Added Taxes** – Value added taxes or (VAT) taxation set at 15%, this would replace most of the income tax revenue and can ensure fair contributions across income levels

2. **Flat Tax on Top 5% of Earners -** Another option to this could be wealth-based taxation (property tax), this high tax would apply to the top 5% of earners.
3. **Expand Social Safety Programs and implement VAT tax** – Strengthen existing support networks to cushion the impact on vulnerable populations. This will be done by utilizing a VAT system at 15% that will allow for funding to remain the same without income tax.
4. **Implement Targeted Tariff Reforms** – Avoid tariffs that disproportionately harm low-income groups by tariffing high income goods: diamonds, luxury furniture, exotic cars, private jets, yachts, high end electronics, designer, etc.
5. **Reduce Government Spending** – Reduce wasteful spending abandoned military equipment, redundant government programs using the list from Government Accountability Office (GAO) and Department of Government Efficiency (DOGE), and subsidies for large wealthy corporations. An example includes but is not limited to the reform / deconstruction of the Department of Education

Projecting Outcomes and Confronting Tradeoffs

Predicted Economic Effects of Policy Recommendations

Policy	Predicted Wealth Disparity (%)	Predicted GDP (Trillions USD)
1. Value Added Tax (15%)	12.0	39.35
2. Flat Tax on Top 5%	9.0	36.35
3. VAT + Social Safety Expansion	10.5	37.85
4. Targeted Luxury Tariffs	11.1	38.45
5. Reduce Government Spending	7.5	34.85

1. **Introduction of Value Added Taxes** – This plan is estimated to have wealth disparity increase by 2% and an increase in GDP by $12 trillion dollars compared to the current amount of $27.72 trillion. This would mean that the country would be richer, and the U.S. will be most probably operating at a net positive allowing faster debt repayment. The value added tax will affect domestic businesses at the different production levels but allow for an overall increase in GDP with a minimal effect of Wealth Disparity.
2. **Flat Tax on Top 5% of Earners** – This plan is estimated to have the effects of decreasing the wealth disparity gap by 1% and increasing the GDP by $9 trillion. This will not affect anyone outside of the top 5% of earners, however it may cause a trickle-down effect with high-ranking earners move out of the U.S. but leave businesses operating in the U.S.

3. **Expand Social Safety Programs and implement VAT tax** – This plan is estimated to have the effects of an increase in wealth disparity of by 10.5% and an increase in GDP by $10 trillion. This policy has the most minimal increase in wealth disparity, while still maximizing the growth in GDP, and introducing this policy would affect all people equally rather than focusing on one group. Another benefit is by expanding social safety nets with the extra income earned from VAT wealth disparity can be mitigated through expanded social welfare programs.
4. **Implement Targeted Tariff Reforms** – Targeted luxury tariffs cause for an increase in wealth disparity by 11.1% and a corresponding increase in GDP by $11 trillion. This plan targets exporters of luxury goods. This policy would be implemented with the tariff increase that is already planned and would likely not cause much of a change in relations. Most citizens were already not purchasing these luxury goods so by tariffing these goods those who choose to spend lavishly will still be paying a premium that was already expected.
5. **Reduce Government Spending** – This policy has already seen partial implementation with DOGE and has been shown to spark outcry and suspicion. I believe with added transparency this policy could be more effective in causing less of an outrage by showing exactly what the problems are and why rather than just stating there is a problem with certain areas of government, for example being the department of education. This, however, does lead to an estimated decrease in wealth disparity of 2.5% and an increase in GDP by $7 trillion.

Recommendation

The proposed alternatives that are under consideration have different pros and cons. Ultimately the final decision will depend on whether or not they value higher GDP over wealth disparity. For example, the increase in alternative 1 where GDP is increased by $12 trillion and wealth disparity is increased by 2%.

Those who tend to lean towards equality reformation and limiting government spending will most likely propose alternate 6. This alternative should be combined with another however to better assist social programs and the loss of revenue from these policy shifts proposed by the presidency.

VAT already exists in Europe and has proven to be beneficial with the Euro appreciating compared to the current state of the United States Dollar where it has been on a decline since the beginning of 2025. VAT may initially face oppositon but overtime as the quality-of-life increased people's opinions could change due to the increase in access to welfare and improved infrastructure (Cornforth 2024).

I believe the best policy choice at this current time is alternative 3: Expand Social Safety Programs and Implement VAT tax. The overarching goal of providing more access to necessary resources such as healthcare, education, food, and shelter, while also increasing the total GDP is an impressive feat. However, resistance to these taxes persists which is the whole reason this government is trying to do away with income tax, but I suggest this because with proper explanation to the president there may be a way to reason that this tax will equally affect everyone not sparking a big outrage since it would be considered a shared tax. This policy does cause a slight increase in wealth disparity however I believe that with the expansion of safety nets this increase would later become null and void. This is the first of many steps forward in nurturing the United States economy back to a healthy state.

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