



Senator Van Hollen's Working Americans' Tax Cut Act

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Key Takeaways

1

The proposal would be budget-neutral over the next decade, with the \$1.6 trillion cost of the alternative maximum tax approximately offset by the AGI surtax.

2

Tax cuts would be largest near the middle of the income distribution, where households pay enough in tax to benefit from a new tax cut but do not earn too much to qualify. The surtax would steeply reduce after-tax incomes for those at the very top of the income distribution.

3

The alternative maximum tax results in a more uniform distribution of tax rates for filers in the middle of the income distribution.

Background

On March 12, Senator Chris Van Hollen released legislation titled the Working Americans' Tax Cut Act. This bill contains two provisions: a "cost of living exemption" structured as an alternative *maximum* tax, paid for by introducing a new surtax on high-income filers.

In this report, we estimate the budgetary, distributional, horizontal-equity, time-burden, and incentive impacts of this proposal.

Alternative Maximum Tax

The bill would establish an alternative maximum tax for low- and middle-income filers. Rather than adjusting the existing tax base, as deductions and exemptions do, this provision places a new ceiling on taxes: a qualifying filer's income tax liability cannot exceed 25.5 percent of modified adjusted gross income (MAGI) above a cost-of-living

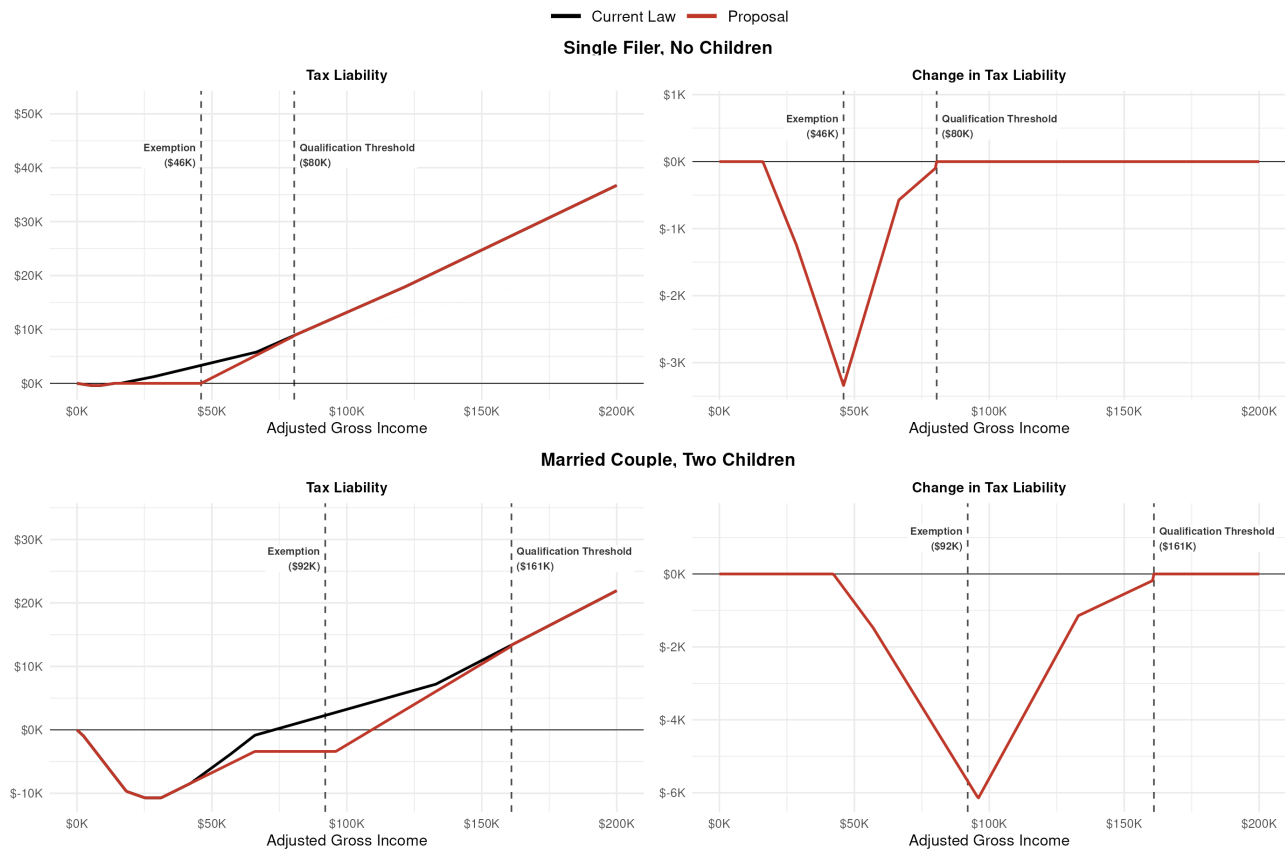
exemption. Under the provision, a filer would compute their tax under both the standard tax schedule and the alternative maximum. If the alternative produces a lower figure, they pay that amount instead.

The exemption is \$46,000 for single filers, \$92,000 for married couples filing jointly, and \$64,400 for heads of household, indexed for inflation. Eligibility is limited to filers with MAGI below 175 percent of their exemption (approximately \$80,500 for single filers and \$161,000 for married couples filing jointly) and is binary: filers below the threshold receive the full benefit of the cap, while those above it receive none.

Figure 1 illustrates visually how taxes would work under the proposal compared to current law for two representative taxpayers.

Figure 1. Alternative Maximum Tax: Illustrative Tax Liability (2026)

All income from earnings; standard deduction



Source: The Budget Lab calculations.

AGI Surtax

The bill also introduces a surtax on high-income filers, applied to three inflation-indexed brackets:

- 5 percent on AGI above \$1 million for unmarried filers (\$1.5 million for married filing jointly)
- An additional 5 percent (10 percent total) above \$2 million (\$3 million married)
- An additional 2 percent (12 percent total) above \$5 million (\$7.5 million married)

Note that this tax is assessed on AGI rather than the ordinary taxable income, meaning that it applies to a broader measure of income than the ordinary rate schedule—it is not reduced by below-the-line deductions like itemized deductions or the qualified business income deduction, and it applies to preferred-rate capital gains.

Budgetary Effects

Table 1 presents estimated budget impacts of the proposal, broken down by provision. We estimate that the alternative maximum tax provision would cost about \$1.6 trillion, a cost that would be offset by the AGI surtax over the next ten years. In the longer run, the net budget impact would be positive, as revenue from the AGI surtax grows faster than the costs from the alternative maximum tax.

These numbers are “conventional” estimates, meaning that they account for tax avoidance behavior (e.g., changes in how much taxable income is reported to the IRS) but not macroeconomic feedback (e.g., changes in investment or interest rates). The Budget Lab expects that there would be two main sources of behavioral feedback in response to the AGI surtax. First, capital gains realizations would decline, as investors tend to [delay or reduce asset sales](#) when facing higher rates. Second, some business income would shift from pass-through entities to C corporations, since business owners tend to [reorganize legal entity type](#) when changes in relative tax treatment make one form more advantageous.

Table 1. Estimated Conventional Budgetary Effects, FY2026-2055

Billions of dollars

Provision	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035
Alternative Maximum Tax	-96	-128	-132	-153	-163	-167	-173	-177	-183	-188
AGI Surtax	108	137	140	146	153	160	168	175	183	190
Total	11	9	8	-7	-11	-7	-6	-1	0	2

Table: The Budget Lab • Source: The Budget Lab Calculations • Created with [Datawrapper](#)

Distributional Effects

Figure 2 plots the proposal's impact on after-tax income by income group, showing how each provision contributes to the total effect. It also shows “winners and losers” under the policy—the fraction of taxpayers in each group with a tax cut or a tax increase of at least \$100.

- As a share of income, average tax savings from the alternative maximum tax provision would be largest for middle-income households. Lower-income households often have no tax liability to begin with and so do not benefit from this provision, and higher-income households earn above the maximum qualifying income level.
- At very high income levels, the surtax kicks in and imposes progressive increases in tax liability, with the top 0.1 percent seeing a drop in after-tax income of about 12 percent.

Figure 3 shows the same concept but for age instead of income. Younger taxpayers, who tend to have lower incomes, would see a net tax cut on average, whereas older taxpayers would see a net average increase. These figures are averages and reflect large, concentrated tax increases on a small number of filers; within each age group, one percent or fewer of taxpayers would face the AGI surtax.

Effects on Horizontal Equity

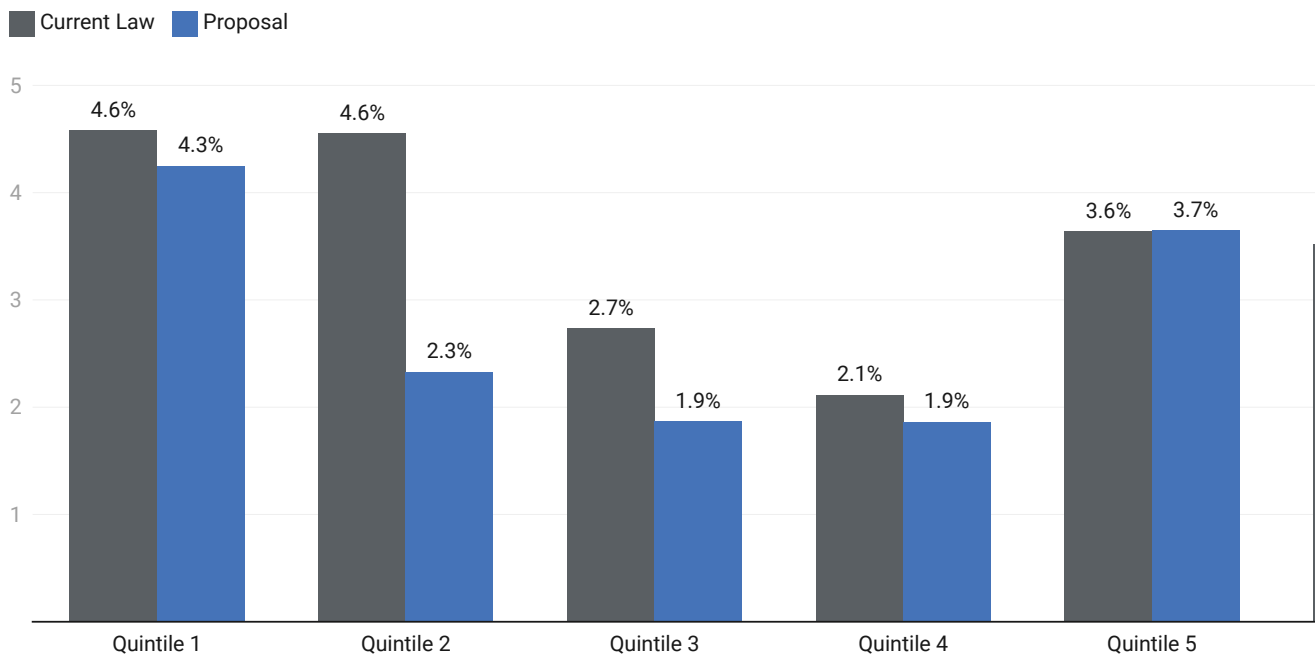
Horizontal equity is the notion that taxpayers with similar economic resources should face similar tax burdens. When the tax code offers special treatment for specific types of income or spending, taxpayers with identical incomes will pay different tax rates based solely on the source of their income or their spending patterns. In addition to any intrinsic concern about horizontal inequity, this kind of within-group dispersion in tax burdens can lead to economically inefficient tax avoidance.

We measure horizontal equity by isolating dispersion in tax rates that cannot be explained by income, marital status, or number of dependents. Figure 4 shows the interquartile range, a measure of variance, of within-group effective tax rates under current law and under the proposal.

We find that tax rate dispersion would fall across most of the income distribution. The alternative maximum tax caps liability at a flat rate, which compresses the upper tail of the effective tax rate distribution within each group. The result is a more uniform distribution of tax rates.

Figure 4. Within-Group IQR of Effective Tax Rate, 2026

Estimate universe is nondependent tax units, including nonfilers. 'Income' is measured as AGI plus: above-the-line deductions, nontaxable interest, nontaxable pension income (including OASI benefits), nondeductible capital losses, employer-side payroll taxes, and inheritances.



Source: The Budget Lab calculations • Created with [Datawrapper](#)

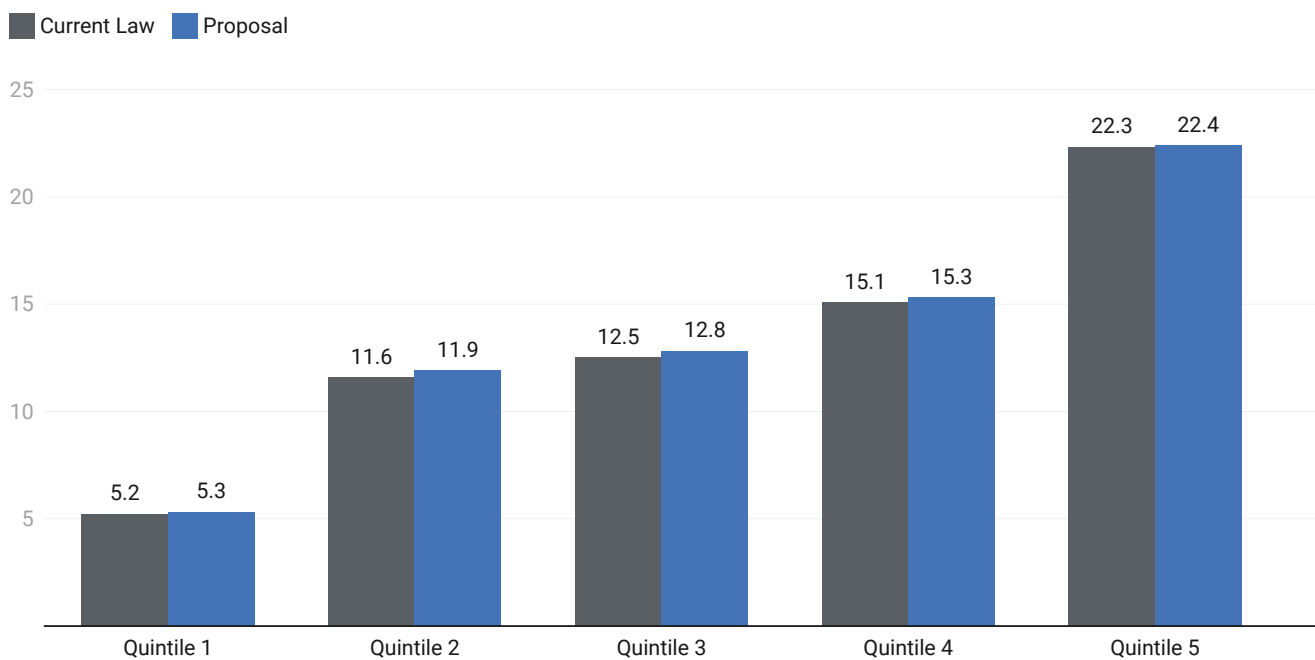
Effects on the Time Burden of Filing Taxes

One dimension for evaluating a tax policy reform is how it would affect compliance costs, including the time burden of filing taxes. Complying with the tax law and filing a return involves time-intensive activities like understanding the law, compiling documentation, and filling out a return. A more complicated code with more tax preferences for certain activities will tend to impose a greater time burden on taxpayers, particularly when the tax-minimizing choice for many taxpayers is to exploit those preferences.

Figure 5 shows our estimate of the time burden of filing taxes under current law and under the proposal. We find that average time burdens would increase slightly due to the new alternative maximum tax calculations.

Figure 5. Average Tax Filing Time Burden by Income Group, 2026

Mean estimated filing time burden in hours.



Source: The Budget Lab calculations • Created with [Datawrapper](#)

Incentive Effects

Beyond its effects on average tax burdens (considered above in the “Distributional Effects” section), the proposal would also change the incentives taxpayers face at the margin. Effective marginal tax rates (EMTRs)—the share of an additional dollar of earnings lost to taxes after accounting for deductions and credits—would shift across the income distribution. Figure 6 plots the average effective marginal tax rate on wages across the income distribution for parents and non-parents separately, under both current law and the proposal. Figure 7 decomposes the change from current law into each provision.

The alternative maximum tax generates an oscillating pattern of average EMTR changes across the income distribution reflecting the interaction between the flat cap rate and the current-law progressive bracket structure:

- At low levels of income, households already do not owe tax under current law. Therefore, the proposal does not affect EMTRs.

- At slightly higher levels of income that remain below the exemption amount, the cap eliminates tax liability entirely, reducing EMTRs to near zero.
- Just above the exemption, the pattern reverses. While these filers still benefit from a lower *average* tax burden, the flat 25.5 percent cap rate exceeds the statutory rate of 10 or 12 percent they would otherwise face, pushing EMTRs upward.
- Near the qualification threshold, filers lose eligibility for the cap and revert to their ordinary bracket rates, and the EMTR increase disappears.
- A second, analogous wave of EMTR changes then appears at higher income levels, driven by the shift in filing status composition: as the share of married filers rises across the income distribution, the same exemption-to-threshold dynamics repeat at the higher exemption levels for joint returns.
- At the top of the AGI distribution, surtax effects on average MTRs are muted in figures 6 and 7 because the surtax applies only to a share of even the top bin of filers.

The proposal, by imposing a binary eligibility threshold rather than a phase-out, also creates *notches* for some taxpayers—discrete jumps in tax liability for small changes in income. For example, consider a married couple with two children and whose income is solely wage earnings. Just below the qualification threshold of \$161,000 for married filers, their tax liability would be \$13,195. Just above it, their tax liability rises to \$13,360—an increase of \$165 from just one additional dollar of earnings. Notches are important to study because they represent large effective marginal tax rates and, if large enough, can discourage labor supply and encourage inefficient tax avoidance behavior.

In practice, most notches would be small under the proposal because the flat 25.5 percent cap rate closely approximates the normal effective tax rate for most households near the threshold. We estimate that approximately 82 million tax units have incomes below the eligibility cap in 2026 and thus would face a potential notch at the qualification threshold. But of this group, only 1.7 million have income within \$5,000 of the threshold, and they save an average of just \$181 from the cap.