The One, Big, Beautiful Bill Delivering for the American Economy

Testimony for the House of Representatives Committee on Ways and Means
Ronald Reagan Presidential Library

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Chairman Smith, Ranking Member Neal, and members of the committee, thank you for the opportunity to testify on the successes of the recently passed One Big Beautiful Bill Act (OBBBA) and the importance of sound tax policy for the future of economic growth.

Today, I will emphasize four main points:

1. Economic growth is essential to creating opportunities for American families.
2. Sustained economic growth requires a tax code that rewards work, savings, and investment.
3. Key tax provisions in OBBBA will strengthen incentives to work, save, and invest.
4. Additional growth-focused policies are needed to ensure economic dynamism.

The Importance of Economic Growth

A growing economy is essential for expanding economic opportunity for all Americans. It is deeply concerning, then, that in its January 2025 Economic Outlook the Congressional Budget Office (CBO) projected real GDP growth to average just 1.8 percent over the next decade.[1] To put that in perspective, had growth been that low over the last 50 years, the US economy today would be nearly 40 percent smaller.

There is a strong link between a well-performing economy and rising incomes across the income distribution. We've seen this relationship clearly over the last two decades. From 2008 to 2016, the economy grew at an annual real rate of just 1.7 percent. During that time, median real wages rose 0.4 percent per year. In comparison, from 2016 to 2019, real GDP grew at 2.7 percent, leading to median wages rising 1.1 percent per year.[2] The strong growth delivered opportunities across the income spectrum. In fact, the rapid economic growth in the first Trump administration before the pandemic led to more wage growth for the bottom of the income distribution than wage growth for those at the top.[3]

Given its far-reaching effects, strong economic growth is essential. The central challenge for lawmakers is how to reignite the economy.

The Need for a Pro-Growth Tax Code

Pro-growth tax policy is a key ingredient for delivering sustained economic growth. When governments impose high tax burdens, particularly on high earners and businesses, capital moves elsewhere—leading to lower-than-expected revenues and reduced economic growth. In contrast, low marginal tax rates encourage work, savings, and investment. More people working means more growth. More dollars saved or invested means more new businesses, factories, and jobs are created.

My own research at Stanford University has extensively studied how tax policy affects migration and economic activity.

One source of evidence is the state of California. When the state raised tax rates in 2014, my coauthor Ryan Shyu and I found that taxpayers adjusted their behavior in response to the tax hike, significantly reducing their taxable income. Excluding those who left California, for every 1 percent drop in share of income they could keep, high-income earners cut their reported income by 3.0 percent, ostensibly by working less, starting fewer businesses, expanding existing ones less, or engaging in more distortionary tax planning. Overall taxpayer responses eroded 60 percent of the possible revenue gains within the first two years, over 90 percent of which was driven by the reduction in economic activity of the high earners who stayed in the state.[4] This is the Laffer Curve in action.

The effects of sound tax policy were also evident after the implementation of the Tax Cuts and Jobs Act of 2017 (TCJA). With my coauthors Jon Hartley and Kevin Hassett, we found that TCJA's business tax reforms led to substantially higher investment rates—much larger than prior studies had indicated.[5] Notably, the largest increases in investment were in the types of business assets targeted by the TCJA's incentives for growth through faster cost recovery.

Pro-growth tax reforms depend on accurate, trustworthy, and transparent scores from the Joint Committee on Taxation (JCT) and the CBO. These agencies are currently falling short of that standard. For example, the JCT's conventional model remains opaque. It is built on decades-old code and is supplemented by "off-model" calculations that are poorly documented. Key parameters—such as how rate changes affect tax avoidance and evasion—are kept hidden, making it difficult to evaluate their results.

Congress should require that scorekeepers enhance transparency, modernize their outdated models, disclose key assumptions, and publicly benchmark their parameters to relevant scholarship. In addition, the scorekeepers should offer sensitivity analyses of their scores or offer candid, systematic assessments of the confidence they have in specific estimates. These reforms would build trust in the official scores and provide lawmakers with more information, which will facilitate further pro-growth tax reforms.

The Importance of the OBBBA for Growth

Given the pessimistic growth projections, policymakers had a clear mandate this year to pursue pro-growth tax reforms that would improve the nation's economic outlook. Fortunately, Congress recognized this imperative. The tax provisions included in the recently enacted One Big, Beautiful Bill Act (OBBBA)—particularly for business—are precisely the kind of policies needed to expand opportunities for American workers and families.

The bill includes many growth-focused provisions, but I want to highlight three that are focused on increasing investment and improving productivity in the United States.

First, the OBBBA made permanent the TCJA's full expensing of equipment and temporarily expanded the tax measure to include qualified production facilities. Under the TCJA, full expensing provisions began to phase out in 2023. This was deeply unfortunate as few parts of the TCJA were more impactful on growth. Full expensing gives businesses strong incentives to invest in new equipment and expand operations. In addition, unlike other rate reductions, which may apply to past investments, full expensing disproportionately rewards new investment. Renewing full expensing for capital and temporarily extending it to new factories will provide a powerful boost to new investment and economic productivity.

Second, the OBBBA provides permanent full expensing for domestic research and development. Similar to full expensing of capital, this TCJA provision was temporary. Beginning in 2022, firms were required to amortize these costs over multiple years. Research by my Stanford colleague Rebecca Lester and others shows that the change led to a $12 billion drop in R&D expenditures in the first year after full expensing expired.[6] The permanent extension of R&D expensing will mean new inventions and more innovations for Americans in the future.

Third, the OBBBA returns the business interest deduction limit to 30 percent of earnings before interest, taxes, depreciation, and amortization (EBITDA). Since 2022, the limit had applied to an income base that excluded depreciation and amortization. This shift had increased business tax burdens, particularly in a rising interest rate environment, and especially for businesses that wanted to invest to replace depreciating capital. The impact was especially severe for businesses relying on short-lived capital assets.

Basing the interest deduction limit on EBIT, rather than EBITDA, also departed from international norms.[7] The OBBBA's reversion to EBITDA brings U.S. tax treatment more in line with other developed countries and reduces the tax penalty on investment. More broadly, combining limitations on interest deductibility with lower tax rates and full expensing, as initiated under the TCJA, remains sound policy. This approach supports investment while reducing the bias toward debt financing. However, unless full expensing is expanded to cover all types of capital, some interest deductibility should remain, just as the OBBBA preserves. An even better alternative would be to eliminate the asymmetry altogether, by allowing full expensing for all types of capital and further limiting or eliminating interest deductibility, as I describe further in the following section.

The economic effect of these provisions is substantial. The Tax Foundation estimates that these three measures alone will increase long-run GDP by 0.8 percent—equivalent to roughly $250 billion in today's economy.[8] By comparison, the JCT's conventional score projects that these three provisions will reduce revenue by an average of just $56 billion per year over the next decade.[9]

Beyond these three provisions, the OBBBA renewed several other pro-growth tax reforms.

The most important is the extension of the TCJA's individual income tax rate reductions. My research on California's tax changes shows just how responsive taxpayers are to changes in their rates. California's experience illustrates how higher tax rates clearly depress economic activity. Allowing federal rates to return to their pre-TCJA levels would have produced harmful effects nationwide.

Similarly, the OBBBA's qualified business income (QBI) tax deduction was made permanent. This provision strengthens incentives for pass-through businesses—LLCs, S-corps, partnerships, and sole proprietors—to hire, invest, and expand. Pass-throughs, many of which are small businesses, account for over 95 percent of all businesses in the US and generate nearly 60 percent of reported business profits.[10] The OBBBA made important changes to the deduction to further improve incentives. Most notably, the act reduces the steep QBI phaseout that created high marginal tax rates for some small-business owners.

Importantly, lawmakers did not merely extend or expand many of the pro-growth provisions—they made many of them permanent. This provides long-term certainty to taxpayers, allowing business owners to plan, invest, innovate, and grow with confidence. Congress should extend this long-term approach to other provisions that shape economic decision-making. A clear candidate is the full expensing of owner-occupied production facilities, which, if made permanent, would provide lasting incentives for businesses to invest in new factories and production capabilities.

What do these pro-growth tax changes mean for the economy? The CBO models GDP growth as a function of capital, labor, and total factor productivity. The key tax components of the OBBBA have been designed to enhance labor supply, increase investment, and raise productivity. For example, full expensing will raise after-tax returns to capital. Permanent reductions in labor taxes will expand labor supply. And full expensing of research and development will improve the efficiency of both labor and capital allocation, improving productivity.

As I noted, my recent academic work suggests that the CBO and the JCT may understate the effects of these provisions on the economy. This could translate into substantial differences in the CBO's assumed GDP growth rate and its deficit effects. Using the CBO's rule of thumb workbook, if annual productivity growth is 0.25 percentage points higher, the annual GDP growth rate over the next 10 years will average 2.1 percent.[11] This contrasts with their current forecast of 1.8 percent. CBO estimates that such a difference in growth would result in an additional $1 trillion reduction in the deficit over the 10-year budget window. If annual productivity growth is 0.5 percentage points higher, annual growth would reach 2.5 percent and deficits would fall by an additional $2 trillion over the 10-year budget window. This would offset more than half of CBO's projected 10-year deficits from the bill and, importantly, fully cover the projected deficit impact in the final years of the budget window. And that is before accounting for any additional tariff revenue raised by the administration.

In addition, I applaud Chairman Smith and this Committee for opposing the attempt by the OECD (with the active encouragement of the EU and the Biden Administration) to impose a Global Tax Code. Although the rules contain incredible complexity and many acronyms, the heart of the issue, as this Committee has recognized and as Treasury Secretary Bessent has testified, is that a Global Tax Code attacks America's sovereignty and violates our Constitution, which allows only Congress to impose taxes on Americans.[12]

The understanding reached at the G7 by the Trump Administration with regards to exempting US companies from the Global Tax Code is an important first step and led Congress to drop from the OBBBA a provision targeting foreign countries imposing discriminatory and extraterritorial taxes on Americans. But this Committee should carefully make sure that this understanding is properly fleshed out and implemented.

Specifically, trying to get other countries to exempt the U.S. on the grounds that the U.S. tax system already imposes sufficiently high taxes would be inadequate and misses the point. The OECD, EU and the countries that have already enacted the Global Tax Code into their laws must change those laws and agree that they will not attempt to tax American companies on income earned in the U.S. regardless of whether Congress lowers U.S. tax rates or makes any other change to U.S. tax law. Any country that fails to do so and has a law on the books that would raise taxes on American companies not just if U.S. law stays the same but also if Congress lowers taxes should be subject to stringent countermeasures.

The Need for Pro-Growth Reforms

Lawmakers should not be content to stop here. Economic dynamism depends on removing barriers that discourage work, saving, and investment.

A comprehensive pro-growth tax reform would aim to eliminate the numerous deductions, exemptions and credits that complicate the tax code. These tax breaks distort economic decision-making and create an inefficient allocation of resources. By broadening the base through removal of these preferences, policymakers would be able to fund substantial rate reductions in both individual and corporate income, while maintaining revenue neutrality. This reform would eliminate advantages that currently favor some sectors and industries and allow the rate of return to capital and the free market to determine the most productive use of capital, rather than tax policy.

Congress has already taken an important first step for comprehensive tax reform by providing full expensing for many capital purchases. The next step should be to explore a permanent overhaul of US business taxes that extends full expensing to all capital purchases while further limiting interest deductions. Such a tax system would reduce distortions in the tax code while giving business owners more incentive to invest in new machinery and production capabilities. Similarly, while the QBI delivers lower rates for business owners, it does little for workers who continue to face high marginal rates on their labor. Broad rate reduction for all taxpayers should be the next aim of policy makers, as high rates stifle the incentive to work and invest. For example, the House's 2016 Better Way proposal included lowering the highest rate to 33%, and that is the sort of goal Congress should strive for. The result would be a simpler tax code that doesn't distort economic decision-making. Such a tax system would unlock substantial economic growth, benefiting all Americans.

Beyond tax reform, today's lawmakers have many additional opportunities to grow the economy.

A key priority for lawmakers should be to reduce the regulations that stifle productivity, entrepreneurship, and innovation. Congress should do all it can to eliminate regulations that make it harder for employers to hire and grow. That includes cumbersome permitting rules, incumbent-protecting licensing requirements, and rigid labor regulations that raise the cost of hiring. Similarly, lawmakers should seek to remove the regulations and taxes that weaken competition and hurt consumers.

There are signs that there may be bipartisan support for permitting reform, such as the bipartisan ePermit Act that would digitize the US permitting process and reduce processing times for all federal permits including National Environmental Policy Act (NEPA) reviews. Republicans in Congress could also seek Byrd Rule compliant provisions that reduce regulatory burdens, such as the OBBBA's ingenious Section 60026, which allows applicants to pay somewhat higher fees for significantly expedited NEPA reviews. While ideally both the fees and the associated regulations would be reduced, the 25% higher fee for a fast-track review allowed the measure to pass the primary Byrd Rule test (changes federal receipts or outlays). Ultimately, Section 60026 will still significantly reduce the overall cost of the regulation, since the economic cost of delay and uncertainty surrounding NEPA reviews dwarfs the review fees.

Finally, and perhaps most importantly, future growth depends on spending restraint. The primary fiscal challenge facing the United States is not insufficient revenue, but excessive spending. According to the CBO, federal revenues in 2025 are projected to reach 17.1% of GDP, very close to the historical average of 17.3% from 1974 to 2024. In contrast, federal spending is expected to be 23.3% of GDP, more than two percentage points above its historical average, and is projected to rise further in the coming decade.

Without serious and immediate efforts to rein in federal spending, tax cuts that are labeled permanent will prove not to be. Future taxpayers will inevitably face the cost of today's deferred obligations whether through higher explicit taxes, draconian spending cuts, or the monetization of today's debt through inflation. Any of these outcomes will undermine growth and jeopardize future prosperity.

Four decades ago, President Ronald Reagan spoke to the nation about the risks of growing federal deficits. His words remain just as relevant today:

> I'm asking all of you—Democrats, Republicans, and independents—to give me your help to put our financial house in order so that our tax, spending, and monetary policies will not hinder growth, but encourage it; not send inflation and interest rates shooting back up, but keep them heading down; and not drown us under a tidal wave of debt, but protect us in the safe harbor of financial stability, with a sound and powerful economy.[13]

Today, as we gather at the Ronald Reagan Presidential Library, the fiscal challenge is far greater, but the call to action remains the same. We must pursue policies that improve incentives and rein in borrowing to preserve prosperity for future generations.

Thank you for your time, and I look forward to your questions.

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[1] Congressional Budget Office. *The Budget and Economic Outlook: 2025 to 2035.* January 17, 2025. https://www.cbo.gov/publication/60870

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[6] Cowx, Mary, Rebecca Lester, and Michelle L. Nessa. "The Consequences of Limiting the Tax Deductibility of R&D." *Stanford University Graduate School of Business Research Paper No. 4998845*. *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4998845#*.

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[10] Li, Huagan, *How the TCJA Affected Legal Business Forms*. June 19, 2024. https://taxfoundation.org/blog/tcja-pass-through-business-tax-reform/.

[11] These estimates are based on the January 2025 CBO Budget Outlook. See Congressional Budget Office, *Workbook for How Changes in Economic Conditions Might Affect the Federal Budget: 2025 to 2035*. March 13, 2025. https://www.cbo.gov/publication/61183.

[12] See United States House Committee on Ways and Means. *Six Key Moments: Hearing with Treasury Secretary Scott Bessent.* June 13, 2025. https://waysandmeans.house.gov/2025/06/13/six-key-moments-hearing-with-treasury-secretary-scott-bessent/.

[13] Reagan, Ronald. *Address to the Nation on the Federal Budget and Deficit Reduction.* April 24, 1985. https://www.reaganlibrary.gov/archives/speech/address-nation-federal-budget-and-deficit-reduction.