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OPENING STATEMENT OF HON. DONALD BEYER JR., CHAIRMAN, A U.S. REPRESENTATIVE FROM THE COMMONWEALTH OF VIRGINIA

Chairman Beyer. This hearing will come to order. And I would like to welcome everyone to the Joint Economic Committee's Hearing entitled “Building Back Better: Raising Revenue to Invest in Shared Prosperity.” I want to thank each of our truly distinguished witnesses for sharing their expertise today, and now let me offer my opening statement.

The Biden Administration Build Back Better Plan will cut taxes for working families, help small businesses, and invest in America's long-term economic prosperity, all while asking the wealthy and big corporations to pay their fair share. Today, Federal revenue is just 16.4 percent of the economy, and asking the wealthy and big corporations to contribute more Federal revenue is consistent with supporting long-term economic growth.

The Build Back Better Plan will help provide American small businesses with a level playing field to compete with multinational corporations. The Treasury Department projects that 97 percent of small businesses will be protected from increased taxes, and many will get a tax cut from reducing the corporate tax rate to 18 percent for incomes under $400,000.00.

The Build Back Better Plan promotes global competitiveness by working to end the race to the bottom on corporate taxes, letting American businesses compete on the basis of bringing the best
products to market at the lowest price, instead of competing on who can avoid paying taxes.

As a small businessman for almost five decades I know that paid family leave will help small businesses retain workers. When I had workers who got sick, or needed to care for a sick child, we provided paid leave to our employees because we would never want to leave our workers to choose between a paycheck or taking care of themselves or a loved one.

At some point during their lives all workers are going to need to take time away from work. By establishing a Federal paid leave program, Build Back Better helps small businesses cover those inevitabilities and reduces the cost of turnover, which is why so many small businesses have come out in support if it.

Small businesses will also benefit from expanding the work opportunity tax credit, which would give businesses up to $5,000.00 to hire qualified individuals, including eligible veterans. Asking the wealthy and big corporation to pay their fair share is consistent with supporting long-term economic growth.

After the Obama-Biden Administration allowed the Bush tax cuts for the very wealthy to expire in 2013, the economy added 8 million jobs in President Obama’s second term. Job growth slowed under President Trump as the Trump taxes delivered a windfall for the wealthy, creating record stock buybacks, and adding hundreds of billions to the deficit.

Although friends across the aisle will likely claim that asking the wealthy and big corporations to pay their fair share will hurt economic growth, the evidence just doesn’t back them up. A congressional research service report found that “both labor supply and savings and investment are relatively insensitive to tax rates.” In addition, improving IRS enforcement will increase revenue without raising rates, while ensuring that businesses cannot gain advantages over their competitors by cheating on their taxes.

We know that investing in working families, communities and innovation is the key to broadly shared economic growth, and that’s exactly what the Build Back Better Plan would do. An analysis by the Tax Policy Center shows that the Build Back Better Revenue provisions passed out of the House Ways and Means Committee would abide by President Biden’s pledge not to raise taxes on those making under $400,000.00 a year.

So in 2022, households making under $500,000.00 will get their direct taxes cut on average. Middle income parents will get a tax cut of about $3,000.00 on average. Extending the enhanced child tax credit, and expanded child and dependent care tax credit that is proposed under Build Back Better, would help families to access affordable childcare and paid family leave.

These two supports are both critical to helping parents, particularly mothers, remain engaged in the labor market. And we know that increased labor force participation is key, driving long-term and sustainable economic growth.

Under President Biden, almost four and a half million people have returned to work, and unemployment has dropped to 5.2 percent. In the first few quarters of 2021, real GDP grew at over 6 percent. In fact, the second quarter was just revised upward again, and the Federal Reserve projects 5.9 percent real GDP growth this
year. Core CPI inflation grew just 0.1 percent. That’s 1 over 1,000 in August, even as real wages grew at .4 percent—four times faster.

So passage of Build Back Better and the bipartisan infrastructure bill will cement these economic gains, improved productivity, lower inflationary pressures and create long-term growth. Louisiana Analytics projected that passing both bills will increase GDP growth in 2022 to 5.3 percent.

Similarly, the Economic Policy Institute projects that the two bills would support 4 million jobs per year, including 556,000 manufacturing jobs and 312,000 construction jobs. For too long the wealthy and big corporations have avoided paying their fair share. You have an opportunity now to rebalance the scale and invest in America’s future to create long-term broadly shared economic growth.

We have been waiting for our Vice Chair, Senator Lee to show up, but while he’s not here yet let me go ahead with the introductions of our speakers, and then we will slot Senator Lee as soon as he shows up.

So in the order of their witness testimony our four distinguished witnesses. Dr. Kimberly Clausing. Dr. Kimberly Clausing is the Deputy Assistant Secretary for Tax Analysis in the Office of Tax Policy at the U.S. Department of the Treasury. Prior to that Dr. Clausing was the Eric M. Zolt Professor of Tax Law and Policy at UCLA School of Law. And before that, she joined UCLA from Reed College where she worked as the Thormund Miller and Walter Mintz Professor of Economics.

Dr. Clausing has published numerous articles on taxation with a particular emphasis on the taxation of multinational companies, and she is the author of an amazing, excellent book called Open: The Progressive Case for Free Trade Immigration and Global Capital. She’s a long-time friend of many of us and advisor.

She received her BA in Economics from Carleton College, and an MA and PhD in Economics from Harvard University.

Ms. Chye-Ching Huang is the Executive Director of the Tax Law Center at NYU Law. Before joining the Tax Law Center Ms. Huang was Senior Director of Economic Policy at the Center on Budget and Policy Priorities where she worked on the analysis and design of a wide range of Federal tax fiscal and economic policy proposals in collaboration with tax academics, practitioners, analysts and advocates.

Previously Ms. Huang was a Tax Academic at the University of Auckland in New Zealand, where she published research in tax law, policy and regulation, and taught graduate and under-graduate tax law. Ms. Huang holds an LLM from Columbia Law School where she was a Sir Wallace Rowling/Fullbright and James Kent Scholar, and a Bachelor of Law and a Bachelor of Commerce in Economics from the University of Auckland in New Zealand.

Dr. Wendy Edelberg is the Director of the Hamilton Project and a Senior Fellow for Economic Studies at the Brookings Institution. She’s also a Principal at WestExec Advisors, and prior to Brookings, Dr. Edelberg was Chief Economist at the Congressional Budget Office, something near and dear to all of us.
Previously Dr. Edelberg was the Executive Director of the Financial Crisis Inquiry Commission which reported on the causes of the 2008 Financial Crisis. Dr. Edelberg also worked on issues related to macroeconomics, housing, and consumer spending at the White House Council of Economic Advisers and the Federal Reserve Board.

Dr. Edelberg received a BA in Economics from Columbia, and MBA from the University of Chicago, and a PhD in Economics from the University of Chicago.

Finally, Dr. William McBride is the Vice President of Federal Tax and Economic Policy at the Tax Foundation. Dr. McBride previously served as a Manager in the National Economic and Statistics Group at PricewaterhouseCoopers. Dr. McBride has experience researching and modeling the economics of taxation and issues related to tax reform at the State, Federal and international levels.

From 2011 to 2014 Dr. McBride served as the Chief Economist at the Tax Foundation. Dr. McBride holds a BS in Physics from the University of the South, a BS in Electrical Engineering from Washington University in St. Louis, and a PhD in Economics from George Mason University.

And with that, let me turn the floor over to the Vice Chair of the Full Committee and the distinguished senator from Utah, Senator Michael Lee.

[The prepared statement of Chairman Beyer appears in the Submissions for the Record on page 28.]

OPENING STATEMENT OF HON. MIKE LEE, RANKING MEMBER,
A U.S. SENATOR FROM UTAH

Senator Lee. Thank you so much, Mr. Chairman. I really appreciate it. Before the pandemic disrupted American’s work lives and social connections, tax cuts and deregulation supported a thriving economy that delivered broad benefits to families and workers.

The Tax Cuts and Jobs Act of 2017, which provided historic relief to working and middle class American families, and led to higher wages, better benefits, and new employment opportunities across the country, was crucial to that prosperity.

Our booming economy provided some of the largest benefits to those Americans who needed it most. Unemployment for Hispanic Americans, Black Americans, and Asian Americans fell to the lowest rates on record. Unemployment for women dropped to a near 65 year low, and low income workers saw their wages rise at some of the fastest rates.

All told the wealth of the bottom 50 percent of all Americans increased by over 70 percent in the three years prior to the pandemic. In early 2020, more than 80 percent of working age Americans were employed, and wages continued to rise. Pro-growth policy reform brought the economy roaring to life in a way that few forecasters thought might be possible.

That success demonstrates an important truth. Americans benefit from lower taxes, less regulation, and more freedom. Unfortunately, we’ve come here today because the Biden Administration and Democrats in Congress want to squeeze the American people with higher taxes and more regulation.
They’ve proposed a 3.5 trillion dollar tax and spend blowout, one that would increase American’s taxes by over 2 trillion dollars. It would be the largest tax increase in my lifetime, and it would substantially expand the Federal Government’s footprint into our homes, our businesses, and across our economy.

Now let’s be clear the major winners from the Democrat’s plan are special interests and beltway bureaucrats. Our economy is still recovering from the pandemic. Now is one of the worst times to saddle our economy with higher taxes. The recovery has stopped accelerating and American families are being hit by higher prices for essential goods.

Things like everything from groceries to housing to gasoline keep getting more expensive. Inflation is rising at its fastest pace in three decades, and it’s making it harder to make ends meet. Wage increases are being swamped by higher prices and job growth is stalling. Democrats reckless tax and spend boondoggle will only make things worse.

Here’s what we know this tax plan would do to American families and workers and businesses. It would raise taxes on American families despite President Biden’s pledge to the contrary. The nonpartisan Joint Committee on Taxation, and the left leaning Tax Policy Center both agree that the plan would hike taxes on low and middle income families making less than $400,000.00 a year.

The Democrats tax plan would also drive jobs for American workers overseas. It would raise the Federal corporate tax rate to 26.5 percent, making the cost of doing business in the U.S. higher than in Canada, Mexico, Japan, the United Kingdom, Germany, France and China.

American workers would pay the price. They’d pay for it in lost jobs and slower wage growth and less investment in things like domestic manufacturing and innovative research and development. In 10 years two-thirds of the tax burden from this corporate tax increase would be shouldered by low and middle income workers, and perhaps worst of all the Democrats tax plan would embolden Washington to pick winners and losers, rather than allowing entrepreneurs to meet the needs of American consumers.

This is about so much more than penalizing successful Americans with even higher taxes. This is about putting more of American’s resources under the control of Washington politicians. Democrats tax plan would cost American families and workers and businesses. It would mean less innovation, lower wages, and fewer jobs.

It would increase the size and scope of the Federal Government. It would make our country less prosperous, less fair, and less free. We know what works—keeping taxes low helps to support a thriving economy. It benefits all Americans. We should return to the policies that made the pre-pandemic economy so successful for so many Americans.

Congress should keep taxes low and predictable by making the reforms in the Tax Cuts and Jobs Act permanent. And then we should restrain government spending. It’s on a runaway path right now, by setting clear and enforceable rules for fiscal discipline.

Look, we simply can’t, as in it simply won’t work. We can’t succeed at taxing and spending our way into shared prosperity. Instead, we need to stop spending indiscriminately and make Amer-
ica the best place in the world to do business, pursue happiness and earn success. Thank you.

[The prepared statement of Senator Lee appears in the Submissions for the Record on page 29.]

Chairman Beyer. Senator Lee thank you very much. Now we will recognize Dr. Clausing for your testimony.

STATEMENT OF DR. KIMBERLY CLAUSING, DEPUTY ASSISTANT SECRETARY FOR TAX ANALYSIS, U.S. DEPARTMENT OF THE TREASURY, WASHINGTON, DC

Dr. Clausing. Thank you Chairman Beyer. Chairman Beyer, Ranking Member and members of the committee. Thank you so much for inviting me to share my views on the relationship between tax policy and the economy.

The present moment is a very consequential one for the future of tax policy. We have an opportunity in front of us to create a modern, efficient, and fair tax system, capable of funding investments that are essential to the creation of prosperous U.S. business environment, and to the sort of inclusive economic growth that can benefit all Americans.

First off, raising adequate government revenue is important for funding the Nation’s priorities, and for shoring up the fundamental economic strengths that are central to job creation. We need revenue to build roads and bridges, to fund education, training and research, to mitigate climate change, and to support families from tackling child poverty to maintaining support to the elderly.

These investments are important to all of us, including those in the business community. Right now however, the United States raises less revenue than we need. We are in the bottom fifth of all OECD countries in terms of revenue raised relative to the size of our economy across all levels of government.

We raise particularly low levels of revenue taxing of capital and corporations. The Joint Committee on Tax reports that U.S. multinationals pay an average tax rate of only 8 percent on their income. In contrast, companies located in our top trading partners pay 18 percent.

We collect far less corporate income tax revenue than our trading partners, and we only collect about half what we collected before the Tax Cut and Jobs Act, when we collected 2 percent of GDP. Our corporate tax revenues are low despite the fact that U.S. companies show very high corporate profits, both in historic and comparative terms.

Indeed, the United States’ corporate sector is the most profitable in the world, dominating every measure of corporate success. Beyond revenue, tax reform is also essential to address the offshoring and profit shifting incentives that are embedded in current law.

Under current, law foreign income is sometimes tax exempt, and sometimes taxed at half the rate of domestic income, providing very strong incentives to locate both activity and profit offshore. Although the Tax Cuts and Jobs Act included a global minimum tax called GILTI, it did not stop profit shifting. Indeed, the very large share of U.S. multinational income in very low tax jurisdictions did not change after 2015.
Unfortunately, current law creates an America last tax system. Even high- or medium-taxed foreign income is preferred to U.S. income because it can be blended with low—tax income and taxed at a 50 percent discount. This is why a country by country minimum tax system is so crucial.

These reforms will also create a fairer tax system. The past four decades can be characterized by three related trends—large, troubling increases in income and inequality, multiple reductions in tax rates for those at the top, and difficulty making ends meet for many lower and middle income families.

Under current proposals, large expansions in the child tax credit, the earned income tax credit and the child dependent care tax credit will help address the needs of typical Americans. In short, asking for somewhat larger tax contributions from the country’s wealthiest households, and from the most profitable corporations will help us raise the revenue that is needed to support the long-term competitiveness of the U.S. economy and the well-being of American families.

Finally, there are many ways that our tax system needs to be modernized to suit the 21st century. The mobility of capital means that the taxation of multinational companies is subject to large tax competition pressures.

The existential threat posed by climate change makes it critical to make changes in the tax code that incentivize clean energy. In both areas, cooperation with other countries pursuing the same goals yields double dividends, encouraging them to take firm actions of their own in solving long-standing collective action problems.

A crucial way to modernize our tax system is to also ensure that we collect the tax that is due. The tax gap, which is forecast to total about 7 trillion over the coming decade, creates both inefficiencies and inequities. Honest businesses who pay their tax obligations in full compete with businesses whose owners shirk their tax responsibilities.

Workers who earn solely wage or salary income fully report their income accurately, but face higher tax burdens than taxpayers using evasion to hide opaque sources of income. Those at the top of the income distribution are disproportionately responsible for the tax gap. Providing the IRS with the resources and information they need will give us a more progressive tax system.

American taxpayers will benefit across many dimensions: improved taxpayer service, better targeted audits toward those that evade, and hundreds of billions of dollars of revenue that allow lower taxes elsewhere, less debt, and better government.

In conclusion, the tax reforms that we will discuss today are essential for encouraging U.S. job creation, economic growth and inclusive prosperity. Thank you for inviting me.

[The prepared statement of Dr. Clausing appears in the Submissions for the Record on page 31.]

Chairman Beyer. Thank you, Dr. Clausing very much. We’ll next hear from Ms. Chye-Ching Huang for your testimony.
STATEMENT OF MS. CHYE-CHING HUANG, EXECUTIVE DIRECTOR OF THE TAX LAW CENTER, NEW YORK UNIVERSITY LAW, NEW YORK, NY

Ms. Huang. Chairman Beyer, Ranking Member Lee and members of the committee. I am honored to testify about an opportunity to meet the Nation’s most pressing economic needs. Sound tax policy can lift the living standards of low and moderate income Americans, and support economic growth with shared benefits for workers, families and businesses.

And that is because it can raise revenues to support investments in areas like infrastructure, education, scientific research and worker training that are known to deliver long-term benefits. And this can also reduce the costs of challenges like climate change.

Further, lawmakers are considering proposals, including a stronger child tax credit, and those are also true in these folks because they deliver longer benefits for the trajectories of children and the broader economy.

Research shows that such credits increase the likelihood that children grow up healthier, do better in school, attend college, and earn more as adults. And these long-term benefits can be large. Nobel research also suggests that financial stability can help more children develop and apply their talents for research, innovation, and entrepreneurship and the country is currently losing out on so much of their potential.

Seventeen Nobel Laureate economists have explained that the package that lawmakers are considering will ease long-term inflationary pressures, and that’s because it combines investments that improve growth with revenues to financial those investments without adding to long-term deficits.

Furthermore, sound tax policy can scale back on inefficient tax breaks, and can help it slow to where it’s most productive, rather than where the tax savings are the most lucrative. It can also reduce complex and wasteful tax planning games. And in doing so tax policy can level the playing field for small, domestic and honest businesses so they can fairly compete with businesses that use tax avoidance, profit shifting to tax havens, or even outright tax evasion is a business strategy.

The revenue raising proposals before Congress meet those goals. They would first ensure that companies of wealthy filers pay what they already are. Second, they would reverse some of the 2017 tax law’s corporate rate cuts that would even cover what businesses asked for, and also address subsidies for locating profits and investments offshore.

Third, they would scale back tax breaks that allow some of the wealthiest people in the country to pay a little or no income tax on very large sources of income. Such tax policies are far more likely to strengthen the economy than tax cuts concentrated at the top of the income distribution.

Careful research finds no evidence that the 2017 tax law increased investment or wages above trends already in place. In the fact of that disappointing track record, some proponents of the tax cut strategy have instead cited predictions from paid studies that are deeply flawed, or inaccurately described current proposals.
Another response has been to promote a view of competitiveness that misattributes America’s economic success very narrowly to its willingness to subsidize multinationals tax avoidance, rather than the quality of American ideas, people and infrastructure.

Those have already accumulated large profits and are seeking to protect their tax preferences, can afford to push this short-sighted view of America’s competitive potential. An investment supported by good tax policy can ensure that more children can be part of the next generation of innovators who may generate new breakthroughs in businesses with widely shared benefits.

And of course successful business and individuals will continue to benefit from America’s infrastructure. Finally, some may try to frame the tradeoffs that will make us now face, as requiring them to choose between areas of deep need, including reducing child poverty, broadening access to community college and paid leave, addressing climate change, filling homes with Medicaid and more.

But the actual tradeoff is much broader. It’s between those investments and to what extent policy maintains the status quo of very wealthy taxpayers and corporations not paying taxes that they owe, and keeping provisions of law that allow them to pay very low tax rates. Thank you for inviting me, and I would be glad to take your questions.

[The prepared statement of Ms. Huang appears in the Submissions for the Record on page 38.]

Chairman Beyer: Ms. Huang, thank you very much. We’ll now hear from Dr. Edelberg. Dr. Edelberg the floor is yours.

STATEMENT OF DR. WENDY EDELBERG, DIRECTOR OF THE HAMILTON PROJECT AND SENIOR FELLOW FOR ECONOMIC STUDIES AT THE BROOKINGS INSTITUTION, WASHINGTON, DC

Dr. Edelberg: Chairman Beyer, Ranking Member Lee, and members of the committee. My name is Wendy Edelberg, and I am the Director of the Hamilton Project and the Senior Fellow at the Brookings Institution. Before coming to Brookings I was Chief Economist at the Congressional Budget Office.

As we discuss the tax provisions contained in the reconciliation package, and other ambitious policy proposals, I’d like to focus on three points. First, investments in the social insurance system are vital for ensuring broad access to opportunities in advancement, and for making our economy more resilient.

There’s extensive evidence demonstrating how effectively these programs work and why they should be expanded. Second, adopting the ambitious policies included in these packages would not create worrying inflation risk, and those packages effect on the long-term fiscal trajectory would be modest.

Finally, although the contemplated tax increases would have a small negative effect on incentives to work and invest, other policies in the package would increase incentives to work and invest. You know everyone in the United States directly benefits from the social insurance system at some point in their lives.

Moreover, everyone indirectly benefits from it, either from knowing the system would be there during some time of unexpected hardship, or simply because it helps to support the overall econ-
omy. During the pandemic-induced economic downturn, some of these programs have proven particularly effective.

As a result of the enormous fiscal support provided to households in 2020, the percentage of the U.S. population in poverty fell from 12 percent to 9 percent. There is more to do. Implementing new policies with regard to childcare and paid leave would lower barriers to work among parents and those with caregiving responsibilities, and those policies would improve outcomes for children.

Making permanent the full refundability of the child tax credit would lock in place reductions in child poverty. Making permanent the recent expansion of the EITC for adults without children would reduce poverty and income and equality, and increase labor force participation.

Permanent expansions to health insurance premium tax credits and cost-sharing subsidies would decrease uninsured rates by potentially 14 percent. These are not the only improvements to the social insurance system included in the reconciliation package, but they are illustrated examples of how strengthening this system would improve well-being, and make our economy more resilient.

At the same time the ambitious policies included in the packages being considered would not creating a worrying inflation risk and their effect in the long-term fiscal trajectory would be modest.

Policymakers have stated their goal is to include increases in tax revenues and decreases in spending that would decrease revenues and increase spending. If something close to a full offset is achieved, the reconciliation package would do little to the project debt trajectory.

To be clear, policymakers still have long-term challenges with regards to the Federal budget, however this reconciliation package even if the estimates end up showing it would modestly increase the cumulative deficit over the next decade would not worsen those challenges in a notable way.

Although many of the changes being considered would increase people’s incentives to work and invest, the revenue raising policies would have muted negative effects. For example, the reconciliation package undoes some of the reduction the corporate tax rate put in place in the 2017 Tax Act.

Consensus projections were that the large reduction in 2017 only boosted the level of investment modestly. Inversely, reversing some of that reduction would have only small, negative effects on investment even as it raised substantial revenue. In addition, the package increases the effect of marginal tax rates on labor income, but only for a small portion of the labor force comprised of the highest income people.

Any negative effect on the aggregate labor supply would likely be hard to identify after the fact. The policies that would increase recipient’s incentives to work, save and invest, could have large positive effects.

For example, access to high-quality and affordable childcare could be a game changer for labor force participation among mothers of young children. With a larger and more productive workforce firms would have greater incentives to work and invest in the United States.
To wrap up, despite headwinds created by the Delta Variant, the economy is recovering. This is the moment to strengthen the social insurance system, and to enact an ambitious Federal investment package. Together those policy changes would make the U.S. economy more resilient and productive over the longer term, and it would broaden the degree to which prosperity in the United States is shared across workers and families, thank you.

[The prepared statement of Dr. Edelberg appears in the Submissions for the Record on page 51.]

Chairman Beyer. Dr. Edelberg, thank you very much. And finally, we will hear from Dr. McBride.

STATEMENT OF DR. WILLIAM MCBRIDE, VICE PRESIDENT OF FEDERAL TAX AND ECONOMIC POLICY, TAX FOUNDATION, WASHINGTON, DC

Dr. McBride. Thank you Chairman Beyer, Ranking Member Lee and members of the Joint Economic Committee. I appreciate the opportunity to speak with you. Today I’ll share the key findings of our analysis about the economic impacts, the revenue provisions of the most recent version of the President’s Build Back Better agenda, the House Ways and Means Committee reconciliation bill.

The House bill relies heavily on corporate tax increases, would raise the corporate tax rate 5 percentage points to 26 1/2 percent, which would be the largest increase in the rate in more than 70 years.

Including the average State corporate tax, combined Federal State corporate tax rate will be almost 31 percent, the third highest corporate tax rate in the OECD. A similar ranking would result in looking at effective corporate tax rates which account for various deductions and other tax preferences.

The bill also raises or introduces several other taxes on U.S. multinationals. Taxes that do not exist in other countries, including the GILTI tax. The result would be to disadvantage U.S. companies and their workers, in favor of companies based in lower tax countries such as Canada, the UK, or just about anywhere in Europe.

It’s important to remember that corporate taxes are not just paid by corporate shareholders. By reducing investment and productivity growth, higher corporate taxes lead to lower wages across the board. This is why the OECD finds that corporate taxes are the most economically damaging way to raise revenue, followed by individual income taxes, consumption taxes and property taxes.

Several studies demonstrate that corporate taxes are borne in part by workers. For example, a recent study found that workers bear about half of the tax burden in the form of lower wages, with low-skilled young and female employees disproportionately harmed.

Our modeling of the House bill indicates that the corporate tax increases alone would reduce long range GDP by about 0.6 percent, shrink the capital stock by 1.2 percent, cut wages by 0.5 percent and eliminate about 120,000 jobs.

The House bill also levies several tax increases on high earning individuals, especially pass-through business owners, causing the top combined tax rate on ordinary and pass-through business income to exceed 52 percent on average. The top combined tax rate
on capital gains and qualifying dividends would reach 37 percent on average. These higher tax rates come with a cost. They will reduce incentives to work, save and invest broadly reducing employment opportunities throughout the economy. In total we estimate that the House plan, including the corporate and individual income tax increases would reduce the size of the economy by about 1 percent in the long run, shrink the capital stock by 1.8 percent, cut wages by 0.7 percent and cost more than 300,000 jobs.

While the plan would raise more than $2 trillion in tax revenue over the next decade on a gross basis, it would give away about half of it in the form of dozens of tax credits, leaving just over $1 trillion in net revenue. After accounting for the smaller economy, the plan raises even less revenue, about $800 billion over the next decade on net.

In other words, the House plan would reduce long-run GDP by more than $2 for every $1 raised, meaning the costs in terms of GDP loss far outweigh the benefits in terms of tax revenue. This occurs for two reasons: the revenue is raised in economically destructive ways, and a large part of that revenue is spent in the form of tax credits with little to no benefits for long-term economic growth.

The tax credits are aimed at a variety of issues that deserve attention, including childcare, clean energy, housing and broadband development. However, cluttering up the tax code with more tax credits comes with many downsides, including increased complexity and compliance costs for taxpayers as well as additional administrative burden for the IRS, which is ill-equipped to take on so many extra duties unrelated to tax collection.

The bulk of the tax credits are aimed at providing temporary relief to families with children—a worthy goal, but likely better administered by a spending agency such as the Social Security Administration. In general, tax policy should be focused on how to raise revenue in the least economically harmful manner, and other goals should be handled as public spending subject to the appropriations process.

It is important to address the escalating costs of childcare, healthcare, housing and other concerns, but it should be done in a sustainable way that does not greatly add to the deficit or reduce job opportunities, wage growth, or people’s ability to succeed and attain a higher standard of living. Thank you for your time and attention.

[The prepared statement of Dr. McBride appears in the Submissions for the Record on page 70.]

Chairman Beyer: Dr. McBride, thank you very much. We will now begin the round of questions. I will begin followed by Senator Lee. So let me start. Dr. Clausing companies often worry that tax increases will make them less competitive. In fact, I’ve been on many Zooms in the last couple months with corporations complaining about this.

In your judgment, how will reforming the international tax system affect competitiveness?

Dr. Clausing: I’ve got mute button problems, but thank you for that question. There are three really important ways to think...
about competitiveness, and in my view all three of them are much improved because of this set of proposals.

So first if we think about economic fundamentals, like what makes the U.S. economically strong right? These are things like our infrastructure, our workers, our institutions, our business environment of entrepreneurship. Those fundamentals will be strengthened if we have adequate revenue to invest in things like climate change mitigation, like research and education and training.

So in that definition of competitiveness this is definitely helpful. The second definition of competitiveness thinks about the competitiveness of the U.S. location as a place to do things in comparison to offshore locations. Under current law there’s a tax preference for the offshore locations relative to the U.S. locations because offshore income is either exempt from U.S. tax, or taxed at a 50 percent discount.

Under these proposals the tilt in the playing field in favor of foreign income, and away from U.S. income would be dramatically reduced, and that would reduce the incentive—the tax incentive to locate offshore. So this is a very important way that we can improve the attractiveness of the U.S. location for job creation and U.S. activity, as well as buttress the U.S. tax base.

A final notion of competitiveness concerns the competitiveness of U.S. companies when they’re operating offshore relative to their foreign counterparts right, so you could imagine a U.S. company and a foreign company both competing in a low tax rate country.

That type of competitiveness is also improved under the tax policy environment that we see in front of us because there is a historic opportunity to increase tax rates on companies based abroad, and continue ongoing negotiations to end the race to the bottom in corporate taxation.

So when we look at the typical tax burden faced by U.S. companies, relative to the typical tax burden faced by foreign companies that will be narrowing rather than widening. And I should point out that even if we ignore changes in foreign laws and if we assume that there are none of them, a recent Reuter’s study found that even if you adopted the full-fledged Biden proposals on corporate and international tax, that U.S. companies would still have a tax advantage relative to their peers.

They looked at the 52 largest multinational companies, and they found that our current tax advantage is about 8 percentage points relative to their own competitors cited in financial statements, and that that advantage would still be at least 3 percentage points. And that’s ignoring all of these investments in things like clean energy and also ignoring any possible changes to our foreign tax laws.

So we think that this set of proposals enhances every type of competitiveness.

Chairman Beyer. Thank you very much. Dr. Edelberg as the former Chief Economist of the Congressional Budget Office you’re probably better equipped to understand than anyone the impact of this legislation on our fiscal health, so do you worry about the long-term fiscal trajectory of the Nation if we pass any of this reconciliation in the Infrastructure Bill, and specifically do you worry about inflation?
Dr. Edelberg. I don’t think that the packages that are currently being contemplated would have a notable effect on the fiscal trajectory over the next decade. Policymakers have stated that their goal is to fully offset any tax decreases or spending increases with when you have tax increases and spending decreases.

But even if those weren’t fully offset, I don’t see that this would notably increase the fiscal trajectory in a worrying way. Financial markets have made it very clear that they are not perturbed by the level of fiscal debt, with the level of Federal debt. I mean they’re not perturbed by the projection of Federal debt over the next decade under current law, and this wouldn’t do much to that projection over time.

And so you also asked about inflation. I don’t see that the packages currently being considered would have notable—would create notable, in any kind of worrying inflation risk, and that’s for two main reasons. One, the Committee Commission on Taxation estimates in their score that the policies would essentially be deficit neutral over the next two years, which is to say that all of any spending increases would be offset by spending decreases or tax increases.

So we would see a little economic effect from those policies over the next two years, and other policies would take years to stand up. So inflation risk is a thing that we should be worried about, but it has nothing to do with the policy discussions at hand. The Chairman. Thank you Dr. Edelberg very much. My time is up. I’ll recognize my friend from Arizona, Mr. Schweikert, with the shout out that the President appointed an Arizonan to be the new Chair of the National Endowment of the Humanities, and an Arizonan to be the new Chair of the National Endowment of the Arts. Dave you were left out, but you get to ask questions now.

Representative Schweikert. And a Native American from our State, so it’s wonderful. Mr. Chairman and just as an aside, but an incredibly important one, as you’ve heard the democrat, the left’s witnesses all throw the caveat that the democrats have a stated commitment. Majority Leader Steny Hoyer even, after I gave a floor speech came and reaffirmed right after my discussion that the left has made a commitment. They will pay for every dime of the spending in this package, whether it be the transfer payments, whether it be the subsidies to the rich, and so we look forward to the left keeping their commitment that this will be fully paid for.

Because without doing that much of the economic discussion we’re having here is intellectually vacuous and dishonest. So Mr. McBride I want to first thank you, Tax Foundation, for doing the only intellectually credible analysis of the proposals we’ve seen so far, but I wanted to go a bit further.

I’m one of those that has a fixation on how you make the working poor less poor, and we’ve seen some of the success of economic expansion providing resources and ability and making labor wages more robust. When Tax Foundation did their modeling I know you worked through the capital stock, the actual revenues, those things you came up with what was it 880 billion dollars of probably true, actual increase in revenues.
Was there any attempt to model a society that moves to almost a social welfare transfer payment model, and what that will actually do to labor stock and labor participation incentives?

Mr. McBride. Well we follow the empirical literature on the well run impacts of transfer payments, and you know studies from the IMF for instance, and other major organizations indicate that it’s very small, it’s close to zero. Some studies indicate it’s actually it has a negative impact on long-term economic growth. And so we’ve adopted the assumption of a zero impact at those type of transfer payments.

Representative Schweikert. Okay. And my reason Dr. McBride for the discussion is we have a couple articles and Chairman Beyer we’re going to submit them for the record that basically focus on social stratification and freezing of social mobility in the societies that do almost the identical model to the Left’s proposal that people find themselves trapped in their quartiles.

And we were struggling, to figure out how you would even model such a thing.

Dr. McBride. Well it’s interesting. I mean the idea of mobility and movement you know from one income quintile to the next over one’s lifetime, or you know from one generation to the next, is a very interesting topic.

Representative Schweikert. Yes.

Dr. McBride. That’s no doubt that there’s actually a great deal of movement across income quintiles within ones lifetime, an average person’s lifetime that the millionaires, or the top 1 percent are not monolithic. They are actually changing from year-to-year. You can look at the list of the richest people in the U.S. or any other list.

It’s changing. It changes quite a lot over the course of you know 10 or 20 years, and you know essentially that’s because wealth is episodic, and you know someone can really hit it big with a very successful business, and that doesn’t last forever. Very often the good times lasts only a few years and then end.

Representative Schweikert. Dr. McBride, and the tyranny of the clock because some of this would be actually very interesting, if our ultimate goal was we wished to deal with child poverty, but we also want a society that closes income inequality. There’s good literature that shows transfer payments give you a nice pop, and then freeze your society.

And I have a fixation of how do we help with child poverty, but then also maximize economic expansion? And even some of the details in everything—even from some of the other witnesses, that looks like long-term capital stock economic growth opportunity, particularly for the working poor will be actually fairly severely damaged by the end of the decade by the democrat proposal. And with that Mr. Beyer I yield back.

[The articles referred to by Representative Schweikert appear in the Submissions for the Record on page 84.]

Chairman Beyer. Thank you Congressman Schweikert very much. I now recognize the Congressman from Madison, Wisconsin Mr. Pocan.
Representative Pocan. Thank you very much Mr. Chairman. I appreciate it and thanks to all the witnesses. Ms. Huang, I hope I'm saying it right, Huang.

Ms. Huang. Huang, thank you.

Representative Pocan. Thank you. Let me ask you this question because I think there's a lot of Halloween-like behavior going out, people trying to scare the average person about taxes, scare small businesses. I'm a 33 year's small business owner, over half of my lifetime.

I'm curious when you said this is about leveling the playing field between small business and big business. And I know there's some provisions in particular I think, you know for example, about corporation's first five million et cetera. Can you just talk a little bit about what you meant in a little more detail as if you were explaining it to a local Wisconsin chamber group?

Ms. Huang. Yeah. Well when I talk to small business people, I really prefer not to think that much about taxes. They'd rather be thinking about their products, their customers, their supply chains, or the real world things that really sort of drive business growth and productivity.

But that sort of falls down when they have to compete with big businesses that are shifting profits offshore and using complex tax havens to undercut them, or they have another person that's down the street, that they know is kind of taking in cash and not reporting it to the IRS.

So there are a range of proposals that would help these other productive small businesses by leveling the playing field for them, and allow really both them and other businesses to focus more on the core things that make American productive as opposed to playing games with taxes. And I think that's one of the biggest things.

The other part of course is the investment part. Small businesses, I think would also like to not have to think about potholes in the roads that they are using to get their product to market or other sort of relaxed infrastructure skilled workforce that make it hard to run a business.

Representative Pocan. And I agree with you on the supply chain issues. If you ask my husband who's spending many extra hours every night trying to find the same stuff that he used to be able to find, he would vote for whoever figured that issue out. That's absolutely a huge issue in the small business side.

You know another question is you know we talk about how I think it was referred to as you know the average person is going to pay more in taxes. Again, I like to do it with you know people I might run into. So the median income in Wisconsin for a family is $81,829.00. If they have two children, let's say one's at childcare age, and one's in elementary school.

You know I looked at what the child tax credit does for that family, and that's going to be $3,600.00 a year for one of their kids and $3,000.00 for another kid they're going to benefit from. The childcare provisions, if they're paying 7 percent of their income, that's going to be $5,700.00 instead of the median $12,597.00— again I'm only counting one child.

You know I'm already up to $13,500.00 savings, I'm not even counting the prescription drug savings, I'm not counting the paid
leave if they need that. Can you just address that as well a little bit about the reality is for that median family in Wisconsin, are they paying more like it's been inferred by some of the crypt keepers—I'm trying talk about Halloween, and scare people, or are they actually going to be benefiting pretty well.

Ms. Huang. Yeah. They will be benefiting. And to your point I've seen some numbers that sort of average out the tax increase that a hedge fund manager will pay with the tax cut that a teacher or one of the small business people would get. And in fact, the vast majority of working families and small businesses will be benefiting from these costs and tax cuts, that's really only the very top of the income scale that faces those tax increases.

Representative Pocan. Great thank you. And then one last one. I'm going to throw out a little wild ball here, hopefully our Chairman doesn't care. I find it amazing that Jeff Bezos pays virtually nothing in taxes, that between 2006 and 2018 his wealth grew by 127 billion, and he only paid 1.1 percent of his income, or 1.1 percent of that in Federal taxes.

That year he claimed—one year he claimed a $4,000.00 child tax credit. In 2018 he paid no Federal income taxes. You know for a guy who has his employees having to carry bottles with them when they're on the road to urinate in, tell me what do I say to that average person in my district who is saying why is it our tax code rewards someone like him?

What can we do to go after someone with that kind of wealth in the long-term?

Ms. Huang. There's a major hole in the tax code that is real income and that is income that just Bezos or anyone else that's making 100 billion dollars in gains in their stock prices can use to fund a pretty Huxtable lifestyle, and it doesn't make sense that they face a lower tax rate their income, but a teacher or a professional that's earning a salary. So I completely agree we should be addressing that, and that is one of the things a number of the proposals would do.

Representative Pocan. Thank you. I'm out of time. I appreciate Mr. Chairman.

Chairman Beyer. Mr. Pocan thank you very much. We'll now turn to a professional tax collector, the former Treasurer of Kansas Mr. Estes.

Representative Estes. Well thank you Mr. Chairman. And thank you for all of our witnesses for being here today. Congress should be concerned more with the economic crisis that's unfolding before us, an unprecedented worker shortage, coupled with rising inflation and energy prices.

But still this bill forces through trillions of new spending and is fixated on raising taxes. So much so that President Biden will break his promise and raise taxes on those who make less than $400,000.00. The Joint Committee on Taxation found that two-thirds of Biden's corporate tax hike will be felt by middle income taxpayers, including small businesses that file taxes as individuals.

It's not honest to say this legislation, which the New York Times describes as touching virtually every American at every point in life from conception to old age, won't cost a dime. That's clearly not true.
The many new social spending programs in this plan won’t create economic growth. The Joint Committee on Taxation estimates it will actually lower Federal revenues by around 1.2 trillion dollars over the next decade. The administration’s budget even acknowledges that growth isn’t a priority for them in an ideal world.

It only forecasts a meager 2 percent GDP growth by 2023 with it dropping even lower until 2029. Any inside Washington seem to think that just because a bill spends lots of money it’s automatically a good investment, but Washington has a lousy track record of spending taxpayer money.

Out in the real world spending money doesn’t magically make money. A so-called good investment gets worse when you dig into the actual details under the hood. Much of it will go to force Americans to do what a bureaucrat in Washington decides to do for them, like what car to drive.

The Green New Deal provisions would make working class families across the U.S. pay more in taxes so the millionaires in California can write off a new electric vehicle. The bottom line of the agenda is not based on reality. It’s going to crush small businesses, even though it’s got a pull tested slogan like Build Back Better.

I hope that we get serious about the dire financial situation our country faces. The U.S. took in more than 3.4 trillion dollars in revenue last fiscal year. If we took time to prioritize spending that could very well be more than enough to support the United States Government.

Dr. McBride, as you know the evidence shows that higher tax rates do not always yield higher increases in revenue. For example, despite the wide variation in Federal marginal tax rates over the years in the ’60s they were even as high as 90 percent. The share of Federal revenues remained relatively steady in the post-World War II era, ranging between 15 and 20 percent of GDP.

Indeed, scholars at your organization have pointed out that many studies show income reported by taxpayers falls as marginal tax rate rise. Punitive high tax rates, not only increase the insidious to shift or underreport income, they also have a high economic cost. How should policymakers think about the tradeoff between high tax rates, raising revenue and economic performance?

Dr. McBride. Thank you. That’s certainly a very important thing to remember that it’s like you said it’s not that simply raising rates, it leads to more revenue in every case. Primarily the most extreme example demonstrating that is capital gains, and this is why they’re recognized from the history of changing tax rates on capital gains that there’s a sort of a revenue maximizing tax rate of about 28–29–30 percent in that range, and that’s what the Joint Committee on Taxation assumes as well. And this is widely understood among revenue estimators.

So for instance, that is well below the 37 percent average capital gains tax rate that would apply when factoring in the State capital gains rate under the House bill. So another example there is corporate taxes, and so here we can look at across the developed world, countries that have generally been lowering their corporate tax rates quite a lot in the last 40 years roughly in half, have come down you know from around you know 40–50 percent corporate tax rates in most countries down to closer to 20 percent on average.
And what has been the impact on revenue? You might think that revenues would have collapsed across all of these countries. In fact they have been fairly stable as a share of GDP, and actually increased moderately in many cases, and that's over this very long period of time.

So there's something going on there along the lines of what you're talking about. Reported income goes down, the production of income and incentives to generate income go down as marginal tax rates increase. And it can be a very large effect.

Representative Estes. Thank you. I wish I had more time because I want to talk a little bit about the budget deficit, and the increase there, but thank you for enlightening us on some of that, and Mr. Chairman I yield back.

Chairman Beyer. Thank you Mr. Estes, and hang in there if we have time. It would be great to do a second round. But now let me recognize the gentleman from southern California Congressman Peters.

Representative Peters. Thank you Mr. Chairman. First of all I just want to say when I was a student at NYU Law School, I took a couple tax classes. I thought it was so fascinating that I actually went into tax law while in practice, and that was a huge mistake. So I'm saying that the academics are a lot more fun than the practice, so my free advice is don't leave.

But I had a question on this topic which is about taxing the wealthy. One of the objections I had to the Trump tax cuts, I didn't disagree with every part of it, because I thought the corporate rate needed to be adjusted, and I thought we had to fix some international tax things, but to give all that money to wealthy people who didn't need it.

And we saw that it did not increase wealth according to the President's projections. We saw also that the inequality has continued to rise. And I just want to know what's your take on the long-term economic impact on economic growth or job creation if we were to increase taxes on capital gains for high income earners?

It seems to be just to set that up is that wealthy people have all the stuff that they need to buy right? They got their fancy refrigerator, they got the cars that they need, they might have a second house. There's no stimulative effect to giving them money. How should we tax them, and what's wrong with raising the capital gains rate along the lines that the President suggested?

Ms. Huang. It's a great question because it comes up over and over again the idea that this would damage investment which is just simply not worn out by the reality. But the model, the sort of trickle down idea that increasing taxes on very high end, high wealth people would somehow sort of make it square down to workers, that model can break down on each and every link.

There's not that much that tax cuts are very effective at spurring private investment. Cutting taxes can increase tax opportunity for investment, but that can also mean that people need to save and invest less to sort of meet their savings goals. And also if the taxes are following on excess returns from market power rates, and other sort of special returns, there's not going to be a hit to the overall size of investment.
So you see pretty small private investment changes in response to tax changes, and that can be overwhelmed by the effect on public saving and investment because there is a very large fiscal cost.

**Representative Peters.** And I think also that the CBO does assess that even after all the growth projections haven’t been met, the add to the deficit from that was 1.9 trillion dollars, which has a real drag effect on the investment as you know.

Dr. Clausing, I want to just talk to you a little bit about corporate tax revenues. I would have definitely agreed with Mr. McBride that 35 percent was too high. I thought we were uncompetitive. At the time the business roundtable was asking for 25 percent, so was Dave Camp, who was then the Chairman of the Ways and Means Committee, and President Trump took it down to 21 percent.

Now there’s talk about raising it back up to 25 say, and business community is saying that the effective rate would be a lot higher because there’s been base broadening. Can you tell me how we should analyze that? Is that true? And how should that matter as we analyze what the appropriate corporate tax treatment is?

**Dr. Clausing.** Well I think there’s a general principle, it’s very useful to have a broad base in part because you don’t need to raise the rate as high if you’re taxing all the income. If you tax some of the income at a high rate and some of the income at a low rate, right, then the income kind of rushes over to the place where the rate is lower.

So in several aspects of these tax proposals we’ve tried to even the tax treatment of different types of income. So whether it’s for capital or labor; for a multinational company, whether it’s foreign or domestic income; for a small business, whether they’re paying their taxes, or whether they’re evading taxes. And so I think that this is a very important feature.

It’s certainly the case that if the base is broader all things equal, at any particular tax rate that more tax will be paid. The question is whether that is a bad thing. You know I think that the corporate taxes——

**Representative Peters.** Wouldn’t it be just—I’m going to run out of time, so can you assess what the effective rate would be if we were looking at 25 percent before, now there’s base broadening. What if we raise it up to nominally 25 percent, what are we talking about for an effective rate?

**Dr. Clausing.** Yes I think part of the difficulty there is that the actual statutory rates doesn’t bear a lot of resemblance to the true tax rate paid by companies. So, for instance, the Joint Committee on Tax is telling you right now that U.S. companies are paying about 8 percent, the big multinationals right.

If you ask them to pay more it will be more than 8 percent, but 8 doesn’t really reflect current law which is 21 for domestic, and 10 and 1/2 for foreign right? So while the Biden proposals would certainly raise effective rates, they would still remain competitive with those of peer countries. Right now we’re way below the effective rate in peer countries.

**Representative Peters.** Thank you. My time has expired. I want to just commend your testimony from 2017 about carbon taxes, maybe we have time to do that later.
Chairman Beyer. Thank you Congressman Peters very much. If the Senator Cruz is with us, you will be recognized next.

Senator Cruz. Thank you Mr. Chairman. Thank you to the witnesses who are here. Dr. McBride, President Biden and the democrats so-called Build Back Better Act, as reported by Ways and Means is estimated to reduce long-run GDP by .98 percent, which in today’s dollars amounts to about 332 billion dollars of lost output annually each and every year.

It’s also estimated that the plan would in the long run raise about 152 billion in new tax revenue. That being said for every dollar of revenue raised economic output would fall by $2.18. Your team has done extensive work analyzing these proposals. What are your thoughts on the potential impact of the democrat’s plan on the U.S. budget deficit on America’s long-term fiscal health?

Dr. McBride. Thank you for that question. It’s very difficult to pinpoint the impact on the deficit when we don’t have estimates from the CBO or anyone else on all of the spending programs that are being discussed in this reconciliation bill.

What we have assumed for our purposes of estimating the impact of the deficit is we have assumed the top line number of 3 and 1/2 trillion, and there’s actually deficits over the 10 year budget window, and in the out years no impact on the deficit based on compliance with the Byrd Rule of the Senate.

And but event there due to the impacts on the economy, the reduction in wages, which is a major tax base for the Federal Government, and other tax bases, that so-called dynamic revenue, that accounts for all this reduction in the size of the economy, falls to only about 800 billion over the 10 year window.

And so you can tell that is considerably lower than the top line spending numbers that are being discussed on the order of 2 trillion plus. And so we do find it does increase deficits in the 10 year window, and those deficits do matter. In our modeling the deficits means that if we continue with a historical pattern of a lot of our national debt is bought up by foreigners, and assuming that continues to hold, that means foreigners own a larger and larger share of U.S. assets, and a larger amount of income in the form of interest payments goes to foreigners, as a result of the increase in the debt. There’s a reduction in U.S. income that’s measured by sort of gross national product.

Senator Cruz. So Dr. McBride a minute ago you just described the cost of the Bernie Sanders socialist budget as 3.5 trillion. President Biden rather remarkably has claimed the cost of it is zero dollars. I’m reminded of what Nobel Prize winning economist Milton Friedman said, which is “there’s no such thing as a free lunch.”

How can you possibly reconcile this administration’s claim that a 3.5 trillion dollar bill costs zero dollars?

Dr. McBride. Right. I think that the charitable interpretation there is that it has no impact on the deficit, but as I’ve just discussed it does have an impact on the deficit when you account for the reduction in the size of the economy, the reduction of the tax bases—the big tax bases.

Senator Cruz. But so you found that if I heard your number correctly a little bit over 2 trillion dollars of impact, is that right?

Dr. McBride. Thereabouts.
Senator Cruz. Okay. Let me ask you also President Biden has repeatedly pledged that the democrats would not increase taxes on anyone making less than $400,000.00 a year, and yet this Bernie Sanders socialist budget does exactly that, and in fact Congress’s own Joint Committee on Taxation—so not a republican organization. The Joint Committee on Taxation shows that all these promises are unequivocally false, and that tax rates will increase on virtually every income level—taxpayers earning $40,000.00 a year, $50,000.00, $50,000.00 to $75,000.00, $100,000.00.

Pretty much everyone earning $40,000.00 a year or more will see their taxes go up. Can you explain why that is, and we’re talking about 85 percent of taxpayers that either see no impact, or see their taxes increase. Is that right?

Dr. McBride. That’s right. Right. In particular for instance, the group earning between $100,000.00 and $200,000.00, most of those taxpayers would see a tax increase over the course of the next decade as a result of this, that’s according to——

Senator Cruz. But how? Please explain how.

Dr. McBride. The main reason is the corporate tax. While it’s being depicted as paid only by the wealthy or shareholders, neither of those are completely true. First of all let’s just stick to the idea that it’s paid by shareholders. The first thing to know about that is not all shareholders are rich. Many of them are retirees earning considerable less than $400,000.

So as a result the Joint Committee finds that even in 2023, very early in the budget window, although that year they assume that all of the corporate taxes are paid by shareholders, they find that even there in all income groups, all of those deciles all the way down the scale, there are shareholders that own U.S. equities, and they own them in all sorts of forms.

But the fact is they are affected by those corporate taxes through that channel. And the second big channel is through worker’s wages. And so that effect takes longer to happen, but it happens through reduced productivity as a result of corporate taxes.

Reduced productivity means lower wages over time. And so that has an effect of further increasing the tax burden ultimately on workers all up and down the income scale.

Senator Cruz. Thank you.

Chairman Beyer. Senator, thank you very much. By the way “there’s no such thing as a free lunch” was actually used by Robert Heinlein in 1966, nine years before the Milton Friedman thing.

Senator Cruz. I stand corrected Mr. Chairman.

Chairman Beyer. In the first century, so pretty cool.

And with that Senator thank you very much. Now recognize my friend from Texas Mr. Arrington for his questions.

Representative Arrington. Thank you Chairman. Thank you witnesses, and I’m driving through God’s country out here in West Texas, and so if I——

Chairman Beyer. I think you just got muted there Congressman Arrington.

Representative Arrington. Can you hear me now?

Chairman Beyer. You’re back.

Representative Arrington. Okay. Look this notion of fairness in the tax code is intriguing to me, and I want to direct this to Dr.
McBride to make sure that I’m using accurate numbers here. But I think some top 1 percent of the income earners who earn 20 percent of the total income in the country pay 40 percent of the taxes doesn’t seem fair to me.

I think some top 10 percent of the income earners pay 75 to 85 percent of the taxes. I guess my point is the tax code is pretty darn progressive, and in fact even though the TCJA, the Tax Cuts and Jobs Act was disparaged for a giveaway to the rich, we actually have a more progressive tax code post Republican tax cuts.

Dr. McBride could you confirm and shape up some of those numbers and percentages I was throwing out there? Do we have one of the most progressive tax systems in the developed world?

Dr. McBride. That is correct. That was an assessment by the OECD a few years ago. I have not seen a new assessment as to how the U.S. compares to other countries, but safe to say the U.S. has not changed the progressivity of the tax code a great deal even after the Tax Cuts and Jobs Act, that’s according to David Splinter at the Joint Committee on Taxation, and found that progressivity did not increase measurably, did not change measurably after the Tax Cuts and Jobs Act.

Redistribution—a separate concept, did change. Taxes came down, it was a tax cut, and so redistribution in the tax code came down, but the actual progressivity as it is measured did not change appreciably as a result of the Tax Cuts and Jobs Act.

Mr. Arrington. I don’t know you know what the definition of fairness in a tax code vis-à-vis the democrat Reconciliation Tax and Spend Bill, but to have 10 percent of Americans paying 80 percent of the freight in terms of the cost of our government doesn’t sound very fair to me, especially if you have 40 percent roughly, or over 40 percent paying zero taxes.

And I think that’s bad policy, not just on the inequity of that ratio, but I want every American to have a stake in the future of our country. I want ownership. I think that’s healthy, it’s good, and I think you can make it so that it’s reasonable to relative to their income.

Same thing on the whole corporate tax rate. I don’t know what the tax rate—I don’t have a magic number. I’m not dogmatic about it. It’s not the gospel to me. I’m not theological about, and religious about this. I just—one place I start is what’s everybody else taxing their job creators and their risk takers, and their businesses?

Because this is a global economy, and I don’t want to hamstring the whole team while we’re competing in away games for customers in markets around the world.

And so that’s kind of where I start. So it seemed pretty reasonable to me to go from the highest corporate tax rate in the free world, the developed world, to something more competitive, not the best. So when we did that we had 4,000 inversions in the United States, the decade leading up to the tax cuts.

We’ve had no inversion since then. If you talk to biotech it’s just one sample of the economy. Three out of four biotech companies in acquisitions were being purchased by foreign biotech companies, or venture capital companies, and today that trend is completely reversed.
So I don't think that's an accident that we're more competitive as a result of reducing the tax burden on our job creators. But here's my question on the corporate tax side because this is disconcerting to me, but it's also because of the effects, but it's also interesting that we can't all see this the same because the Tax Policy Center, which is more left leaning, and the Joint Committee on Taxation, which is supposed to be neutral arbiter of these things—tax policies, and you all have said that the tax increases on corporations, the vast majority—70 percent of it will be borne by working people with higher prices of goods and services in the form of lower wages and benefits.

I mean every think tank, and every expert analyses of the policy left, and right is saying that same thing. Am I getting that right Mr. McBride? And I yield back, I probably went over my time, sorry Mr. Chairman.

Chairman Beyer. I know you don't have the clock in the car, I understand Congressman.

Dr. McBride. That's right. And that's essentially right that the Joint Committee on Taxation, the Treasury Department, all major scoring groups such as ours, the Tax Policy Center, Penn Wharton, they all assume that a significant portion of the corporate tax is borne by workers.

And so that explains why the Joint Committee finds that so many households, some tens of millions of households earning less than $400,000.00 would ultimately bear the burden of corporate taxes.

Chairman Beyer. Because we have gone so far over, let me go to Ms. Huang for her thoughts on this.

Ms. Huang. Just to sort of effect a clarification, it is true that all of the major estimators do assume that ultimately some of the corporate tax is borne by non-shareholders. But mainstream estimates are roughly 20 to 25 percent, not 75 percent. And that's what the JCT estimates.

It's also really important to note that the intuition that sits behind the models that assumes that this happens. ASO assumes that the cost of any corporate tax cut is fully paid for because otherwise any private investment change that you see in those tables would get offset by the public debt going up, and interest rates going up, and therefore national saving and investment going down.

So one of the things that's really important to know is that most tables don't show the ultimate cost of the corporate tax cuts even though they assume they'll be paid for. So when you try and figure out where the workers actually do benefit, you really need to check who ends up bearing the ultimate cost.

And that means taking into account things like in the 2017 tax law, the long-run costs of the permanent cuts was offset by tax changes that increased taxes for individuals across the board after the 10 year budget window, and that would have made more workers worse off as opposed to better off even in those models.

Chairman Beyer. Thank you very much. I wish we could talk about this all afternoon, but many things are going on including missing our seven democrats. So I want to thank each of our witnesses for their expert contributions.
I always marvel how beautifully trained economists with PhD’s can so disagree on the same sets of statistics, but asking the wealthy and the big corporations to pay their fair share is an essential part of the broader package to help small business thrive, cut taxes for working parents and invest in education and healthcare, and policies for the workforce.

So Congress has a real opportunity to level the playing field for American small businesses and workers while also supporting long-term economic growth, and promoting labor force participation. So thank you to each of our panelists for their contributions to this timely and important debate.

This once in a generation investment in America’s future will create long-term broadly shared economic growth, rebalancing the scale to Build Back Better. And as we do this important work, we’re going to rely on your expertise and good faith. So thank you as well to all my colleagues for being a part of this discussion and sharing your wisdom.

The record will remain open for 3 business days, and this hearing is now officially adjourned.

[Whereupon, at 3:51 p.m., Wednesday, October 6, 2021, the hearing was adjourned.]
SUBMISSIONS FOR THE RECORD
This hearing will come to order. I would like to welcome everyone to the Joint Economic Committee’s hearing entitled “Building Back Better: Raising Revenue to Invest in Shared Prosperity.”

I want to thank each of our truly distinguished witnesses for sharing their expertise today. Now, I would like to turn to my opening statement.

STATEMENT

The Biden Administration’s Build Back Better plan will cut taxes for working families, help small businesses, and invest in America’s long-term economic prosperity, while asking the wealthy and big corporations to pay their fair share. Today, Federal revenue is just 16.8 percent of the economy, almost an all-time low, and asking the wealthy and big corporations to contribute more to public revenue is consistent with supporting long-term economic growth.

The Build Back Better plan will help provide American small businesses with a level playing field to compete with multinational corporations. The Treasury Department projects that 97 percent of small businesses will be protected from increased taxes and many will get a tax cut from reducing the corporate tax to 18 percent for income under $400,000.

The Build Back Better plan promotes global competitiveness by working to end the race to the bottom on corporate taxes, letting American businesses compete on the basis of bringing the best products to market at the lowest price, instead of competing on who can avoid paying taxes.

As a small businessman for almost five decades, I know that paid family leave will help small businesses retain workers. When I had workers who got sick or needed to care for a sick child, we provided paid leave to our employees because we would never leave workers to choose between a paycheck or taking care of themselves or a loved one.

At some point during their lives, all workers will need to take time away from work. By establishing a Federal paid leave program, Build Back Better helps small businesses cover those inevitabilities and reduces the cost of turnover, which is why so many small businesses have come out in support of it. Small businesses will also benefit from extending the Work Opportunity Tax Credit, which will give businesses up to $5,000 to hire qualifying individuals, including eligible veterans.

Asking the wealthy and big corporation to pay their fair share is consistent with supporting long-term economic growth. After the Obama-Biden Administration repealed the Bush tax cuts for the very wealthy in 2013, the economy added 8 million jobs in President Obama’s second term. Job growth slowed under President Trump, as the Trump tax cuts delivered a windfall for the wealthy, creating record stock buybacks and adding hundreds of billions to the deficit.

While our friends across the aisle will likely claim that asking the wealthy and big corporations to pay their fair share will hurt economic growth, the evidence does not back them up. A congressional Research Service report found that “both labor supply and savings and investment are relatively insensitive to tax rates.” In addition, improving IRS enforcement will increase revenue without raising rates, while ensuring that businesses cannot gain advantages over their competitors by cheating on their taxes.

We know that investing in working families, communities, and innovation is the key to broadly shared, long-term economic growth. And this is exactly what the Build Back Better plan would do.

Analysis by the Tax Policy Center shows that the Build Back Better revenue provisions passed out of the House Ways and Means committee would abide by President Biden’s pledge not to raise taxes on those making under $400,000 a year. In 2022, households making under $500,000 would get their direct taxes cut, on average. Middle-income parents will get a tax cut of about $3,000 on average.

Extending the enhanced Child Tax Credit and expanded Child and Dependent Care Tax Credit, as proposed under Build Back Better, would help families pay household expenses and generate long-term economic benefits. The Joint Economic Committee estimated that advance payments of the CTC will generate $19.3 billion in local economic activity each month, creating jobs in local communities.

Using the revenue raised from making multinational corporations and the wealthiest pay their fair share, Build Back Better would help families access affordable childcare and paid family leave. These two supports are both critical to helping parents—and particularly mothers—remain engaged in the labor market—and we
know that increasing labor force participation is key to driving long term and sustainable economic growth.

Under President Biden, almost 4.5 million people have returned to work and unemployment has dropped to 5.2 percent. In the first two quarters of 2021, real GDP grew at over 6 percent, and the Federal Reserve projects 5.9 percent real GDP growth this year. Core CPI inflation was just 0.1 percent in August, even as real wages grew at 0.4 percent.

Passage of Build Back Better and the bipartisan infrastructure bill will cement these economic gains, improve productivity, lower inflationary pressures, and create long-term growth. Moody’s Analytics projected that passing both bills will increase GDP growth in 2022 to 5.3 percent. Similarly, the Economic Policy Institute projects that the two bills would add 4 million new jobs, including 556,000 manufacturing jobs and 312,000 construction jobs.

For too long, the wealthy and big corporations have avoided paying their fair share. We have an opportunity now to rebalance the scale and invest in America’s future to create long-term, broadly shared economic growth.

PREPARED STATEMENT OF HON. MIKE LEE, RANKING MEMBER, JOINT ECONOMIC COMMITTEE

Before the pandemic disrupted Americans’ work lives and social connections, tax cuts and deregulation supported a thriving economy that delivered broad benefits to families and workers. The Tax Cuts and Jobs Act of 2017—which provided historic relief to working and middle-class American families and led to higher wages, better benefits, and new employment opportunities across the country—was crucial to that prosperity.

Our booming economy provided some of the largest benefits to those Americans who needed it the most. Unemployment for Hispanic Americans, Black Americans, and women, in particular, fell to the lowest rates on record.1 Unemployment for women dropped to a near 65 year low. And low-income workers saw their wages rise at some of the fastest rates. All told, the wealth of the bottom 50 percent of Americans increased by over 70 percent in the three-years prior to the pandemic.2

In early 2020, more than 80 percent of working age Americans were employed and wages continued to rise.3 Pro-growth policy reform brought the economy roaring to life in a way that few forecasters thought possible. This success demonstrates an important truth—Americans benefit from lower taxes, less regulation, and more freedom.

Unfortunately, we have come here today because the Biden Administration and Democrats in Congress want to squeeze the American people with higher taxes and more regulation. They have proposed a $3.5 trillion tax-and-spend blowout, one that would increase Americans’ taxes by over $2 trillion. It would be the largest tax increase in my lifetime and would substantially expand the Federal Government’s footprint into our homes, into our businesses, and across our economy.4

Let’s be clear—the major winners from the Democrats’ plan are special interests and beltway bureaucrats.

Our economy is still recovering from the pandemic; now is one of the worst times to saddle our economy with higher taxes. The recovery has stopped accelerating and American families are being hit by higher prices for essential goods—things like groceries, housing, and gasoline keep getting more expensive.

Inflation is rising at its fastest pace in three decades, and it is making it harder to make ends meet. Wage increases are being swamped by higher prices and job growth is stalling. Democrats’ reckless tax-and-spend boondoggle will only make things worse.

Here’s what we know this tax plan would do to America’s families, workers, and businesses.

It would raise taxes on American families—despite President Biden’s pledge to the contrary. The nonpartisan Joint Committee on Taxation and left-leaning Tax Policy Center both agree the plan would hike taxes on low- and middle-income families making less than $400,000 a year.

1 https://www.bls.gov/cps/
2 https://www.federalreserve.gov/releases/z1/dataviz/dfa/distribute/chart/
#range:2006.1,2021.1
3 https://fred.stlouisfed.org/series/LNS12300060
4 https://www.heritage.org/taxes/commentary/8-things-you-need-know-about-democrats-tax-increase-bill
The Democrats’ tax plan would also drive jobs for American workers overseas. It would raise the Federal corporate tax rate to 26.5 percent, making the cost of doing business in the U.S. higher than in Canada, Mexico, Japan, the United Kingdom, Germany, France, and China.

American workers would pay the price—they would pay in lost jobs, slower wage growth, and less investment in things like domestic manufacturing, and innovative research and development. In 10 years, two-thirds of the tax burden from this corporate tax increase would be shouldered by low- and middle-income workers.5

Perhaps worst of all, the Democrats' tax plan would embolden Washington to pick winners and losers rather than allowing entrepreneurs to meet the needs of American consumers. This is about so much more than penalizing successful Americans with even higher taxes; this is about putting more of Americans' resources under the control of Washington politicians.

Democrats’ tax plan would cost American families, workers, and businesses. It would mean less innovation, lower wages, and fewer jobs. It would increase the size and scope of the Federal Government. It would make our country less prosperous, less fair, and less free.

We know what works. Keeping taxes low helps to support a thriving economy that benefits all Americans. We should return to the policies that made the pre-pandemic economy so successful for so many Americans. Congress should keep taxes low and predictable by making the reforms in the Tax Cuts and Jobs Act permanent, and restrain runaway spending by setting clear and enforceable rules for fiscal discipline.

We cannot tax and spend our way to shared prosperity. Instead, we need to stop spending indiscriminately and make America the best place in the world to do business, pursue happiness, and earn success.

Thank you.

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5 https://www.finance.senate.gov/ranking-members-news/analysis-biden-tax-hikes-hit-middle
Chairman Beyer, Ranking Member Lee, and Members of the Committee: Thank you for inviting me to share my views on the relationship between tax policy and our economy. Changes in our tax system are vital for encouraging U.S. job creation, economic growth, and inclusive economic prosperity.

**Building a Solid Foundation for Job Creation**

Simply put, raising adequate government revenue is a prerequisite for funding the nation’s most urgent priorities and shoring up the fundamental economic strengths that are central to job creation. Resources are needed to build roads and bridges, to invest in education and training, to fund research, to mitigate climate change, and to support families throughout their lives, from tackling child poverty to maintaining a support system for the elderly.

These investments are important to all of us, including the business community, and business leaders have consistently advocated for a robust response to the problems of climate change as well as substantial funding commitments to infrastructure, research, education, and training. At present, however, the United States raises less revenue than required to fund our government: after the tax cuts of recent years, federal tax revenues are equal to only about 17 percent of GDP. (The last time the U.S. balanced the federal budget, receipts were about 20 percent of GDP.) We are in the bottom quintile of OECD countries in terms of revenue raised relative to GDP, across all levels of government.¹

We raise particularly low levels of revenue on capital income. The Joint Committee on Taxation (JCT) reports that, in 2018, U.S. multinational companies (MNCs) paid an average tax rate of

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only 7.8 percent on their worldwide income. In contrast, JCT finds that our top ten trading partners levied an average tax rate of 18.1 percent. Even before the Tax Cuts and Jobs Act (TCJA) was enacted in 2017—when the U.S. corporate tax rate was 35 percent—U.S. MNCs still paid an average tax rate (16.0 percent) that was lower than our top ten trading partners (19.2 percent). Similarly, a recent Reuters study found that U.S. MNCs pay effective tax rates that are much lower than those of MNCs in other countries. For the 52 largest U.S. MNCs, effective tax rates are 8 percentage points below their peers (companies named as competitors in filings) that are headquartered in foreign countries. Adoption of Administration tax proposals would lower, but not eliminate, the U.S. MNC tax advantage to 3 percentage points.

At present, corporate income tax revenue as a share of GDP is about 1 percent, far lower than the share raised by our trading partners. For many years, the typical Organization for Economic Cooperation and Development (OECD) country has raised about 3 percent of GDP from corporate taxation, whereas in 2018 and 2019 (before the pandemic occurred), the United States raised only 1 percent of GDP from the corporate income tax. Even before the 2017 TCJA, the United States was below peer nations, collecting only 2 percent of GDP from the corporate income tax. Indeed, corporate income tax revenues as a percentage of GDP have been trending downwards in the United States since the 1950s.

<table>
<thead>
<tr>
<th>Table 1: Corporate Income Tax Revenues Relative to GDP</th>
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<tbody>
<tr>
<td>Post TCJA: 2018/2019</td>
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<tr>
<td>5 Years before TCJA: 2013-2017</td>
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<tr>
<td>2000-2012</td>
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</tbody>
</table>

Source: OECD Revenue Statistics.

Corporate income tax revenues are low despite the fact that U.S. companies produce very high corporate profits, both in historic and comparative terms. Indeed, the United States’ corporate sector is the most profitable in the world, dominating every common metric of company success. In 2019, U.S. corporations accounted for 37 percent of the profits that accrued to the world’s 2,000 largest companies, despite having a much lower share of world GDP (see Figure 1 below). The outsized role of the U.S. corporate sector has been apparent for decades: over the prior 15 years, U.S. profit shares were at similar levels although they moved with exchange rates (since values are all measured in U.S. dollars).

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^2 This is the most recent year for which they have reported data.

^3 For the JCT study, see Table 3 on page 58 here: https://www.jct.gov/publications/2021/jcs-16-21/. The Reuters study was reviewed by outside academics; it ignores tax subsidies for manufacturing and clean energy as well as tax increases affecting foreign MNCs. See https://www.reuters.com/world/us/even-after-bidere-tax-bates-us-firms-would-pay-less-than-foreign-rivals-2021-06-22/.


^5 The average for G7 countries is very similar.

^6 The United States also has a large pass-through business sector, but the U.S. economy also shows robust corporate profits, both in comparative and historic terms.

^7 The second most dominant country on the Forbes Global 2000 list is China.
In addition to large corporate profits, the United States has experienced very strong income growth at the top of the income distribution even as average tax rates for this group have fallen. According to Congressional Budget Office data, the share of aggregate income (before taxes and transfers) earned by the top 5 percent of the income distribution increased from 20.6 percent in 1980 to 30 percent in 2018 (the most recent year with data), while the average federal tax rate faced by those in the 96th to 99th percentile dropped from 27.1 percent to 24.2 percent over the same time period.\(^8\)

In short, raising adequate government revenue is essential for the long-term competitiveness of the U.S. economy because it finances the public investments that are needed to maintain the considerable strength of America’s business environment. Asking for somewhat larger tax contributions from the country’s wealthiest households and most profitable companies will help meet that important long-term goal.

**Levelling the Playing Field**

Under current law, a global intangible low-taxed income (GILTI) minimum tax applies to the foreign income of U.S. multinational companies. Unfortunately, offshore investment is encouraged by a feature of the GILTI minimum tax that exempts the first 10 percent return on foreign tangible assets. Under GILTI, owning greater foreign tangible assets (referred to as “qualified business asset investment” or “QBAI”) increases the amount of foreign profit that is tax-free. There is already some limited evidence that U.S. companies are responding to these

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\(^8\) Congressional Budget Office. 2021. *The Distribution of Household Income*, 2018. Report No. 57061. The tax rate of the top 1 percent in the CBO data is somewhat higher, but it also drops over this period.
incentives by increasing their offshore investment.\textsuperscript{9} Foreign activities are also encouraged by a GILTI tax treatment that allows a 50 percent deduction relative to domestic income. So foreign income is sometimes tax exempt, and sometimes taxed at half the rate of domestic income.\textsuperscript{10}

In addition to incentivizing offshore investment and business activity, current law also strongly encourages profit shifting outside of the United States, shrinking the U.S. corporate tax base. Although the 2017 Tax Cuts and Jobs Act included a global minimum tax, it was not a sufficient incentive to counter other aspects of the law that increased profit shifting, such as the complete exemption of some foreign income from U.S. tax. As illustrated on Figure 2, the already large share of U.S. multinational income booked in low-tax jurisdictions is unchanged post-TCJA.

**Figure 2: Share of U.S. MNC Income in Seven Key Low-Tax Jurisdictions, 2000-2019**

Note: Data are foreign investment earnings from the U.S. Bureau of Economic Analysis (see \url{https://www.bea.gov/international/diasedba}). The seven most important low-tax jurisdictions in these data are Bermuda, the Caymans, Ireland, Luxembourg, the Netherlands, Singapore, and Switzerland. These shares are mechanically higher than they would be in some data sources since the data are reported on an after-tax basis.

\textsuperscript{9} For example, Beyer et al. (2021) find that for U.S. MNCs subject to higher GILTI inclusions, higher levels of pre-TCJA foreign cash are associated with increased post-TCJA foreign property, plant, and equipment investments. They do not find a similar increase in domestic property, plant, and equipment. Atwood et al. (2020) find the GILTI provisions introduced new incentives for U.S. MNCs to invest in foreign target firms with lower returns on tangible property so that they might shield income generated in havens from U.S. tax liability under the GILTI minimum tax. See \url{https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3381449} and \url{https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3009978}.

\textsuperscript{10} Depending on the countries of operation, the tax rate applied to this income for some firms can be somewhat higher than half the U.S. corporate income tax rate (rising up to 13.125 percent) due to limits on foreign tax credits.
Perversely, current law creates an “America last” tax system, since even high- or medium-taxed foreign income is tax-preferred to domestic income because it can be blended with low-tax income and taxed at a 50 percent discount relative to U.S. tax rates. That is why a “country by country” GILTI system is so crucial; if the minimum tax can no longer be avoided by blending the incentives to report income in both high-tax foreign countries and havens are greatly reduced. Under the OECD/G20 inclusive framework agreement reached in July, 134 countries (and all members of the G20) have agreed to a “country by country” administration of a minimum tax.

Current U.S. corporate and international tax reform proposals have the potential to end offshoring incentives found in current law and dramatically reduce profit shifting incentives for both U.S. and foreign MNCs. These measures will considerably reduce the tilt in the playing field that favors foreign business activity relative to U.S. business activity, encouraging U.S. job creation and investment.

In addition to reworking the parts of our tax code that favor foreign business activity over domestic business activity, these proposed reforms would also reduce the ways in which our tax system favors large MNCs relative to small businesses. Large multinational companies have profit shifting opportunities that lower their tax burdens relative to those of purely domestic businesses, which makes it difficult for smaller businesses to compete with their larger competitors and further increases the market concentration of U.S. industry. Of note, market concentration has also played an important role in the shrinking labor share of income, since larger, “superstar” firms tend to use less labor than their smaller counterparts. Thus, a competitive economy goes hand in hand with U.S. job creation.¹¹

Creating Inclusive Economic Growth

Most scholars agree that increases in income inequality over the prior four decades have been both large and troubling, although scholars disagree on the magnitudes of these trends.

Over the same time period, those at the top of the income distribution have benefitted from multiple reductions in tax rates: several steep cuts in the top income tax bracket (particularly in the 1980s), large cuts in the top income tax rates applied to dividend income and long-term capital gains, reductions in the reach of the estate tax, and sharp reductions in the corporate income tax rate in 1986 and 2017, which also mostly benefit those at the top of the distribution. While there have also been some instances of tax increases borne by those at the top of the income distribution, those households who have most benefitted from economic growth in recent decades can afford to contribute more to financing urgent fiscal priorities.

At the same time, many workers and families have struggled to make ends meet. Under the American Rescue Plan (ARP) and current proposals, large expansions of the child tax credit (CTC), the earned income tax credit (EITC), and the child and dependent care tax credit (CDCTC) will help address the economic needs of typical Americans. Expansions in the CTC are already pushing childhood poverty to historically low levels and benefitting millions of children. The EITC expansion rewards work for those workers without children or at or near the poverty line. And the CDCTC makes childcare more affordable, incentivizing parents’ labor force participation and strengthening the financial position of working families.

A 21st Century Tax System Architecture

There are many ways that our tax system needs to be modernized to address the needs of the 21st century. The mobility of capital means the taxation of MNCs is subject to large tax competition pressures. The existential threat posed by climate change makes it critical to both remove features of our tax code that subsidize fossil fuel production and consumption and to add tax incentives for the production and consumption of clean energy. In both areas, cooperation with other countries pursuing the same goals can yield double dividends. Our actions encourage other countries to take firm actions of their own, solving longstanding global collection action problems including mitigating greenhouse gas emissions and tax base erosion.

One crucial element of tax reform in this area is ensuring that the tax base is as broad as possible. Broadening the tax base allows us to efficiently raise revenues to meet U.S. fiscal needs without relying on high tax rates. In the international tax arena, that means substantially reducing the discrepancy between the tax treatment of domestic and foreign income. By raising the GILTI rate that applies to foreign income, we can reduce the erosion of the corporate tax base due to
international profit shifting. It also means addressing the profit shifting of foreign-based MNCs operating in the United States by reforming inbound base protection laws.

In the domestic tax arena, it is likewise important to reduce preferences in our tax code that favor capital income over income from working. Beyond that, it is essential to address the tax gap, which is forecast to total about $7 trillion over the coming decade. This large tax gap creates both inefficiencies and inequities. Honest small businesses who pay their tax obligations in full compete with businesses whose owners shirk their tax responsibilities. Workers who earn solely wage or salary income overwhelmingly report that income accurately and face higher tax burdens than the taxpayers who have more opaque sources of income, where tax evasion is both easier and far more common. Those at the top of the income distribution are disproportionately responsible for the tax gap, and providing the Internal Revenue Service (IRS) with the resources and information that they need to promote compliance will result in a tax system that is more progressive.\(^{12}\)

Proposals to fully fund the IRS, and to increase financial reporting of taxpayers, will benefit American taxpayers across many dimensions. First, the IRS will have the resources necessary for answering taxpayer questions and ensuring that taxpayers receive the benefits they are entitled to. Second, compliant taxpayers will have a lower probability of costly audits since additional information, as well as increased technological capability, will enable the IRS to more accurately target audits toward tax evaders. Third, the revenue potential from these reforms is substantial, and the hundreds of billions of dollars raised by working to close the tax gap will result in one or more beneficial consequences for typical taxpayers: lower taxes, less debt, better government services, or any combination of these results. In short, a strong and stable tax administration system is an essential part of fiscal sustainability.

In summary, the present moment is a very consequential one for the future of tax policy. We have an opportunity to create a modern tax system for the 21st century that is both efficient and fair. These reforms will help level the playing field across multiple dimensions: reducing tax preferences for foreign business activity relative to domestic business activity, reducing tax preferences for large businesses relative to small ones, treating income from wealth more like income from work, and reducing the advantages for tax evaders compared to honest taxpayers. These changes will make our tax system fairer by asking for larger contributions from those who are best equipped to pay more while lessening tax burdens on typical American workers and families.

These tax changes will also help fund the urgent fiscal priorities that address today’s greatest needs: investments in infrastructure, research, worker education and training, and climate change mitigation. Such investments are essential to the creation of a prosperous U.S. business environment and inclusive economic growth benefiting all Americans.

Written Testimony for Hearing, “Building Back Better: Raising Revenue to Invest in Shared Prosperity”

Chye-Ching Huang
Executive Director of the Tax Law Center at NYU Law

The United States Joint Economic Committee
October 06, 2021

Chairman Beyer, Ranking Member Lee, and distinguished members of the Committee, thank you for the opportunity to testify. 1

Part I of my written testimony explains that sound tax policy can both lift living standards of low- and moderate-income Americans and support economic growth with shared benefits for workers, families, and businesses. Tax policy designed to achieve these goals should:

- Raise revenues to support needed investments in a dynamic, sustainable and inclusive economy—including the next generation of workers and entrepreneurs;
- Ensure that investment flows to where it is most productive rather than where tax savings are the most lucrative; and, in doing so
- Level the playing field for small and domestic businesses so they can fairly compete with businesses that currently use tax avoidance, profit-shifting to tax havens, or even outright tax evasion as a business strategy.

Part II discusses revenue-raising proposals before Congress that are well-tailored to these ends, including proposals to:

- Ensure that large corporations and wealthy filers pay taxes they already owe under the law. Increasing tax compliance will ensure honest businesses that do not cheat on their taxes are not unfairly penalized.
- Reverse some of the 2017 tax law’s corporate provisions that went beyond even what corporate lobbyists asked for, and reduce the tax code’s subsidy for shifting profits and investments offshore; and


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• Reduce tax subsidies for income from wealth compared to income from work.

Part III explains that such policies are far more likely to strengthen the economy and raise the living standards of low- and moderate-income Americans than maintaining tax cuts and subsidies that flow directly to the well-off.

It reviews the evidence that tax policies such as the 2017 corporate tax cuts have failed to live up to their proponents’ promises. And it systematically refutes arguments for maintaining tax cuts for wealthy filers and corporations that: (1) cite unsound paid studies; (2) inaccurately describe the actual revenue proposals; and (3) promote a view of “competitiveness” that misattributes America’s economic success to its willingness to subsidize multinationals’ tax avoidance, rather than the quality of American research, innovation, workers, markets, and institutions.

PART I: TAX REVENUES SUPPORT INVESTMENTS THAT DIRECTLY RAISE THE LIVING STANDARDS OF LOW- AND MODERATE-INCOME AMERICANS, AND PROMOTE GROWTH WITH SHARED AND SUSTAINABLE BENEFITS

Low- and moderate-income workers and families should be at the center of policymaking: they have faced decades of near-stagnant wages, and COVID-19 has disproportionately impacted low-wage workers and workers of color.² Income and wealth inequality are high in the U.S. relative to other countries and heavily skewed by race due to historic and current barriers to full economic opportunity for people of color.³ Children in low- and moderate-income families in the U.S. have lower rates of upward economic mobility than their counterparts in nearly all other rich countries.⁴

Tax policy can help address these challenges by raising revenue for sound investments that together: (1) directly raise living standards for low- and moderate-income American workers and families; and (2) promote economic growth that is sustainable, increases mobility, and helps U.S. workers, researchers, innovators, and entrepreneurs realize their full potential.

1. Raising revenues to support investments in a dynamic and sustainable economy.

Investments in physical infrastructure, work supports including job training, educational support, and research and development (R&D) have long been recognized as delivering proven long-term economic benefits.⁵ Other investments can forestall and mitigate large foreseeable costs, such as

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² See: Huang (May 2021), supra note 1 at fn 58.

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those from climate change. The proposals before Congress have sound investments in all of these areas, and overall are designed in ways that would address racial, gender, and geographic disparities that are the result of “historical and continuing barriers to economic opportunity.”

Further, a growing and robust body of research shows that financial support for low-income families increases the likelihood that children in those families grow up healthier, do better in school, attend college, and earn more as adults. Thus, proposals including strengthening the Child Tax Credit (CTC) should be seen as a true “investment” that will deliver continuing benefits for the life trajectories of children and the broader economy.

Based on this body of research, Harvard University economists Hendren and Sprung-Keyser estimate that the long-term economic benefits of policies that invest directly in low-income children – like a CTC that is fully available to low-income families -- can significantly reduce or offset their initial fiscal costs.

Such estimates do not account fully for positive effects that are harder to quantify but nonetheless potentially important. For example, new research suggests that expanding economic security for children in low- and moderate-income families can help ensure more children can


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develop and apply their talent for innovation and entrepreneurship, leading to follow-on benefits for the economy at large.\(^{11}\)

Critics worry that revenue-raising proposals will negatively affect the economy but they fail to consider the economic benefits of new investments. This is a mistake:

- **Harvard University Professor of Economics Raj Chetty** noted of the Biden Administration’s recovery proposals, “[t]he impacts of the infrastructure programs are likely to be an order of magnitude larger than any disincentive effects from the taxes.”\(^{12}\)
- **Moody’s Analytics** estimates that the *combined* effect of the investments and taxes in the infrastructure and economic investment legislation would be a net plus for economic growth, and “direct the benefits of stronger growth to lower-income Americans and address the long-run skewing of the income and wealth distribution.”\(^{13}\)
- **Seventeen recipients of the Nobel Memorial Prize in Economic Sciences** have noted that by financing investments that boost long-run economic capacity, revenue-raising tax policies can ease long-term inflationary concerns.\(^{14}\)

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11 Bell et al found that if girls, children of color, and children from non-rich families grew up to invest at the same rate as white boys from high-income families, there would be four times as many inventors in America as there are today. Studies indicate that the reason for these “missing inventors” is that children with equal talent and potential are growing up in households too poor and/or not connected enough to make use of those talents. Alex Bell et al., “Who Becomes an Inventor in America? The Importance of Exposure to Innovation,” Quarterly Journal of Economics, Vol. 134, Iss. 2, May 2019, https://opportunityinsights.org/paper/losestein/. Also see: Wesley Tharp, Michael Leachman, and Matt Sacek, “Tapping More People’s Capacity to Innovate Can Help States Thrive,” CBPP, December 9, 2020, https://www.cbpp.org/research/state-budget-and-tax/tapping-more-peoples-capacity-to-innovate-can-help-states-thrive.


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Such revenue-raising policies can also be designed to support growth in other important ways, discussed below.\^15

2. Sound tax policy can help ensure that investments flow to where they are most productive and businesses can compete based on delivering real-world value rather than tax avoidance and evasion.

The tax code includes various tax breaks and incentives for specific types of income, such as:

- Capital gains income from the growth in value of assets is taxed at a lower rate than income from work\^16—or even a zero percent rate for gains on assets held until death.
- The public subsidizes the foreign profits of multinationals by about $60 billion per year with a lower tax rate for those profits (between zero and 10.5 percent) than the 21 percent tax rate on domestic profits.\^17
- The 2017 tax law created a new tax expenditure (section 199A) that provides a special lower rate on most income earned through pass-through business entities. It allows very high-income business owners to game the tax code and reap windfalls by re-characterizing their income so that it qualifies for the tax break. Despite supposed guardrails, tax advisors have called section 199A a “gaping hole” in the code.\^18

These tax breaks invite aggressive avoidance strategies that stretch the boundaries of the law, with a weakened IRS unable to push back. The erosion of IRS enforcement has also invited blatant tax evasion, as discussed below. This can encourage businesses and individuals in search of tax savings to move resources away from more productive uses, undermining what economists term “allocative efficiency.”\^19

For example, the zero percent tax rate on capital gains on assets held until death encourages the wealthy to hold onto old investments, even across generations, instead of reallocating resources to investments that would deliver a higher return if the tax rate did not exist.

\^15 Tax policy can help address growth by ensuring that the costs of certain economic activities (such as pollution including carbon, the community and public costs of certain products, or even overleveraging of certain financial institutions that creates systemic economic risks) are borne by those who create those costs. Revenue raising proposals of this kind are not currently a major component of proposals before Congress but would be another sound source of revenue.

\^16 Long-term capital gains are taxed at a max of 20% (23.8% including the net investment income tax), while ordinary income is taxed at a max of 37% (43.4%). 26 U.S.C. §§ 1, 1411.


\^19 For a review of the empirical literature suggesting that allocative efficiency effects can be more substantial than supply-side impacts in the context of individual income tax reform, see William Gale and Andrew A. Samwick, “Effects of Income Tax Changes on Economic Growth,” The Brookings Institution, February 1, 2016, https://www.brookings.edu/research/effects-of-income-tax-changes-on-economic-growth/.

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Such tax breaks can also spawn various tax shelters and other tax planning techniques that both pull investment away from more productive activities, and also pull talent and creative energy into the production of tax schemes rather than innovations with more widespread benefits.

The result is an uneven playing field that can undermine the competitiveness of businesses that are unable or unwilling to use tax avoidance as a business strategy. A purely domestic, small, or start-up business that pays what it owes and does not engage in complex tax avoidance schemes can be at a disadvantage compared to an established multinational that uses a web of tax havens to reduce its tax costs.

Sound tax policies can support economic productivity by scaling back or eliminating tax breaks that create such a lopsided competitive environment.

PART II: KEY REVENUE PROPOSALS ARE WELL-DESIGNED TO SUPPORT GROWTH

Lawmakers are considering three main categories of proposals that would raise substantial revenues, finance critical investments, and reduce after-tax income inequality.20 These proposals are on the whole well-designed to support growth by reducing opportunities and incentives for unproductive tax gaming.21

1. Ensuring that profitable corporations and well-off filers pay the taxes that they already owe under the law.

The “tax gap” of taxes owed but not paid is an estimated $7 trillion over the next decade.22 More than a fifth of federal income taxes that go unpaid due to income underreporting (or, recent research suggests, more than a third) come from the highest-income one percent of filers.23 Even assuming the lower estimate (more than a fifth) is accurate, Treasury estimates the top 1 percent are responsible for $163 billion in unpaid taxes annually.

Shrinking the tax gap can raise revenue by ensuring high-income filers and large corporations pay what they already owe. Tackling this issue requires adequately funding the IRS. Between 2010 and 2019, the IRS enforcement budget was cut by more than a fifth, the IRS lost more than


21 I have discussed in other forums and am happy to explain ways in which some of the proposed tax policies might be refined on the margins, including testimony in hearings examining specific revenue-raising proposals. See: Huang supra note 1, Committee for a Responsible Federal Budget, “Tax Policy in the Build Back Better Act,” Panel Discussion, September 30, 2021, https://www.youtube.com/watch?v=1EGd4s82nZM. Directionally, the broad contours of these proposals being discussed by lawmakers are substantial improvements on current law.


a third of its expert revenue agents, and audit rates on America’s highest-income filers and largest corporations fell by more than half.24

The IRS also needs information that will allow it to identify non-compliance by wealthy filers and large corporations. Compliance for wage and salary income is already 99 percent due to information reporting and withholding, but the income of large businesses and wealthy filers is generally not subject to similar reporting requirements.25 The Administration’s financial account information reporting proposal to address this gap is designed to:26

- **Place no new burdens on taxpayers.** Banks would simply report information that they already hold—total inflows and outflows through accounts—like they do with interest income. Taxpayers would not have to do anything more.

- **Safeguard taxpayer privacy.** The IRS would not see any information about specific transactions in accounts (just total inflows and outflows); and

- **Protect low- and moderate-income filers** by requiring that “[a]udit rates will not rise relative to recent years for those with less than $400,000 in actual income.”27

Information reporting is a crucial component of the compliance proposal because it would reduce unnecessary audits on accurate filers.28 Instead, the IRS would be able to use existing audit flags along with evidence of large amounts of unreported cash flowing through filers’ accounts to identify non-compliance more accurately.

Increasing tax compliance will also support fair competition and productivity by leveling the playing field for honest businesses and filers that comply with their tax obligations.

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28 As CBO notes, this “might reduce the burden on compliant taxpayers by allowing the IRS to better target noncompliant ones and to reduce the number of audits that resulted in no change in tax assessment.” Phil Swagel, “The Effects of Increased Funding for the IRS,” CBO, September 2, 2021, https://www.cbo.gov/publications/57444.

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2. Corporate and international tax proposals to reverse some of the 2017 tax law’s tax cuts that went beyond even what corporate lobby groups asked for, and reducing the current tax code’s subsidy for shifting profits and investments offshore.

The 2017 tax law cut the top corporate rate from 35 percent to 21 percent, even below the 25 percent rate corporate lobbyists asked for. It moved the U.S. tax regime towards a “territorial” system by permanently excluding certain foreign income of U.S. multinationals from U.S. tax. Today, U.S. companies can enjoy a tax rate on certain foreign profits that is lower than the rate on U.S. profits—and can be as low as zero percent.

After the 2017 tax law came into effect:

- **Corporations used the bulk of their tax cuts for buybacks and dividends,** with firms announcing a record $1 trillion in stock buybacks in 2018.30
- **Economy-wide investment and wages failed to grow any faster than predicted by pre-enactment trends, and analyses accounting for the uneven impact of the tax cuts across industries and the impact of other economic conditions found no evidence of the large supply-side impacts predicted by the law’s proponents:**

> There was “no indication of a surge in wages in 2018 either compared to history or relative to GDP growth,” the Congressional Research Service (CRS) found.31

> “There is no evidence that the 2017 tax law has made a substantial contribution to investment or longer-term economic growth,” Harvard University Professor of Economics and Peterson Institute for International Economics Senior Fellow Jason Furman found.32 “The patterns in the data suggest instead that corporate tax cuts did not help workers very much,” a 2021 Brookings Institution analysis found.33

> “[T]here is little evidence that the [2017 tax law] meaningfully increased underlying investment. Instead much of the tax windfall went into share repurchases and bigger dividends. If the tax cuts

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31 CRS, supra note 30.


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did not lift economic growth, it is tough to argue that increasing them will appreciably hurt growth,” Moody’s Analytics Chief Economist Mark Zandi and Assistant Director Bernard Yaros Jr. wrote.35

- Multinationals report about the same share of their income in major tax havens as they did before the law.36

- The corporate tax cuts have drained revenues: corporate revenues sunk from 1.5 percent of GDP in 2017 to 1.1 percent of GDP in 2019.37 Each percentage point of the 2017 tax law’s corporate rate cut costs about $100 billion over ten years, the Joint Committee on Taxation (JCT) estimates.38

Reversing some of the 2017 tax law’s rate cuts along with international tax system reforms could ensure that highly profitable corporations contribute adequately to national investments from which they benefit. Aside from raising substantial revenues, sound international tax reform would help strengthen the economy by reducing current tax incentives for companies to locate profits and investments offshore or invest.39 Reducing large multinationals’ ability to use cross-border tax avoidance as a profit center would help create a fairer competitive environment for U.S. businesses that are unable or unwilling to use tax avoidance as a business strategy. Rather than sinking resources into a tax-avoidance arms race, companies will be free to focus on customers, products, and innovation.

3. Reducing tax subsidies for the wealthy.

Lawmakers are considering proposals that would rein in preferences that predominantly benefit the wealthy, including those that lead to income from wealth being taxed more lightly than income from work.

These proposals include raising the top tax rate on capital gains closer to the top rate on salaries.

Other proposals would reduce tax preferences for pass-through income, which flows overwhelmingly to the highest-income filers and is also a major source of tax non-compliance.40 For example, proposals include scaling back the section 199A pass-through deduction (61 percent of which goes to the top 1 percent), and eliminating a loophole that allows certain

35 Zandi and Yaros Jr., supra note 33.
37 OMB Historical Table 2.3, https://www.whitehouse.gov/omb/historical-tables/
39 Kimberly A. Clausing, supra note 36.
40 Chye-Ching Huang (May 2021), supra note 1.

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owners of pass-throughs to avoid Medicare surtaxes on both earnings and investment income. \footnote{41} Improving the complex and inconsistent rules for taxing partnerships (overwhelmingly large finance and holding companies) would ensure their tax treatment is closer to the economic reality, less gameable, and more administrable. \footnote{42} If implemented, such policies would help reduce unproductive tax planning and evasion.

Lawmakers should also address a gaping hole in the tax code: the ability to wipe out accumulated tax on capital gains on assets held until death. This means large incomes of the wealthiest filers never face income tax, during their lifetime or their heirs’ options include:

- A Biden Administration proposal to tax these gains when the asset is passed to heirs, while allowing the gain to continue accumulating untaxed over the original owner’s lifetime. \footnote{43}
- A proposal to tax the gains of the very wealthiest filers as those gains accumulate, in the same way that wages and salaries are taxed in the year they are earned.
- A “carryover basis” approach, which would require a person’s heirs (or their heirs’ heirs, etc.) to pay tax on accumulated gains when the asset is eventually sold, rather than erasing the tax on gains altogether.

These options have strengths and drawbacks relative to each other, \footnote{44} but each, if well-designed, could improve on current law.

**PART III: SUPPLY SIDE CHANNEL HAS NOT DELIVERED PROMISED RESULTS**

Those who favor cutting taxes on income from assets (for both individuals and businesses), argue that their approach will spur substantial investment, which will then cause higher productivity, which will then flow through to higher wages for workers.

But there are many reasons why this “supply-side” channel may fail to produce large promised benefits. \footnote{45} Private investment may not be as sensitive to after-tax rates of return as some


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predict, any impact on private investment may be offset by the impact of tax cuts on public
debt, and any growth gains may not in fact make it into the wages of low- and moderate-income
workers. Instead, careful research on the real-world effects of tax changes indicates that
supply-side impacts are at best modest, and can be negative for low- and moderate-income
workers when considering how the tax cuts are financed.

In the face of mounting empirical evidence and disappointing results of supply-side tax cuts,
some proponents of such tax cuts have turned to three other types of flawed evidence:

1. Deeply flawed studies funded by industry groups.

Various industry and other special interest groups have mobilized against proposals to scale back
their favored tax cuts or other tax advantages. As a lobbying tactic, such groups fund various
studies purporting to predict large GDP or job losses from specific tax proposals.

Huang, “Raising Today’s Low Capital Gains Tax Rates Could Promote Economic Efficiency and Fairness, While
fairness. Chye-Ching Huang, “Recent Studies Find Raising Taxes on High-Income Households Would Not Harm
Skew to Shareholders and CEOs, Not Workers as Administration Claims,” CBPP, August 16, 2017.
administration

One reason may be a large share of these returns is from “excess returns” including rents from advantages such as
market power. Laura Power & Austin Frenich, “Have Excess Returns To Corporations Been Increasing Over Time?”
of-the-statutory-u-s-corporate-tax-rate/

A low interest rate environment may mute the impact of deficits on investment—but equally mute theoretical
supply-side effects of cutting tax rates such as the corporate tax rate. Alan Auerbach and Bill Gale, “Tax Policy

Even if gains were distributed proportionate to wages, the bulk of gains would flow to high-wage workers such as
executives and CEOs, rather than low-wage workers. See: Chye-Ching Huang and Brandon DeBot, supra note 45.
Further, due to market power or other factors, workers’ wages may not reflect their productivity. WCEG, “Boosting
wages for U.S. workers in the new economy: Ten essays on worker power, worker well-being, and equitable

William G. Gale and Andrew A. Samwick, “Effects of Income Tax Changes on Economic Growth,” The

Tony Romm, “Corporate America launches massive lobbying blitz to kill key parts of Democrats’ $3.5 trillion
policy/2021/08/31/business-lobbying-democrats-reconciliation/

For example, Ernst & Young, Repealing Step-up of Basis on Inherited Assets: Macroeconomic Impacts and

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These studies are often treated as a black box, and the paid ads that cite the studies typically use only the headline findings. Analysts who look inside the box, however, often find severe methodological flaws.

For example, when former ICT economist Patrick Driessen evaluated an Ernst & Young study purchased by the National Association of Manufacturers claiming the Administration’s international tax proposals would lead to large GDP and job losses, he found it relied on data so inappropriate and flawed as to “pretty much destroy the study’s credibility.”

2. Incorrect descriptions of the proposals.

Other lobbyists have repeatedly mischaracterized tax proposals.

For instance, bank lobbyists have falsely said the Administration’s financial account reporting proposal would require reporting of “all transactions” of covered accounts or “monitoring” of accounts. This is untrue. The proposal would require reporting only of the total dollar amount of inflows and outflows without transaction-level details, using the same kinds of annual information returns that banks already file for accounts yielding $10 or more of interest.

Similarly, opponents of the Administration’s proposal to address the step-up in basis provision have repeatedly ignored its provision that inheritors of family farms and small businesses would not pay any tax on those assets until the assets are sold, in order to assert that the proposal would negatively affect these sympathetic figures.

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52 See the landing page and twitter ads for NAM’s 2021 anti-tax campaign: National Association of Manufacturers, “Don’t Tilt the Playing Field,” 2021, https://www.nam.org/don-t-tilt-the-playing-field/. The more sophisticated version of this argument is couched in what Ed Kleinbard termed a “battle of the neutralities,” which he and others have established does not provide a sound framework for policymaking. Claims that these frameworks support lower taxation of multinationals rest on assumptions that not well-supported by empirical evidence. See: Edward D. Kleinbard, “Throw Territorial Taxation From the Train,” Tax Analysts, February 5, 2007.


54 See, Murr and Jacoby, supra note 26; Hanlon, supra note 26.


3. A “competitiveness” assertion behind which sits a narrow view of America’s economic strengths.

Multinationals repeatedly claim proposed corporate tax reforms would hurt their competitiveness. In essence, these large, profitable corporations are insisting they cannot compete with foreign companies unless the American public continues to subsidize them by retaining their access to tax havens.

This does not withstand scrutiny. U.S. multinationals are very profitable, and make up a disproportionate share of the most profitable companies in the world. In fact, even before the windfalls they enjoyed as a result of the 2017 tax cuts, U.S. multinationals had been so profitable that they held “about $2.6 trillion in profits offshore in order to avoid U.S. tax,” and their lobbyists pushed for the 2017 tax law to allow them to access these profits at a greatly discounted rate.

The view of competitiveness advanced by U.S. multinationals relies on an extremely narrow vision of U.S. economic strength. Fundamentally, they argue that America’s economic success does not depend on the skills and creativity of U.S. workers and entrepreneurs, or the strength of U.S. physical infrastructure, institutions, markets, and basic research. Rather, it depends on tax cuts for large corporations.

Lawmakers should reject this constrained view of America’s economic potential. The building blocks of a dynamic economy can foster the next generation of researchers, inventors, innovators, and entrepreneurs who might be responsible for new breakthrough products and services with widely shared benefits. Existing profitable corporations with market power and lobbying operations are certainly louder today, but to secure U.S. economic growth it is important to take a long-term, expansive view of what drives a strong, inclusive U.S. economy rather than focusing narrowly on tax breaks that add to corporations’ short-term profits.

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Testimony of Dr. Wendy Edelberg  
Director, The Hamilton Project  
Before the United States Joint Economic Committee  
October 6, 2021

Chairman Beyer, Ranking Member Lee, and Members of the Committee:

My name is Wendy Edelberg and I am the director of The Hamilton Project and a senior fellow at the Brookings Institution. Before coming to Brookings, I was chief economist at the Congressional Budget Office. Thank you for this opportunity to discuss the effects of the tax provisions currently being considered in the reconciliation package.

Despite the headwinds created by the Delta COVID-19 variant, the economy is recovering. Economic growth during the pandemic has generally surpassed consensus expectations while households and businesses have maintained a surprising amount of activity and spending while social distancing. Much of that strength owes to the fiscal support enacted by Congress over the last 18 months. The current rapid economic recovery and expected slowing in the near term creates risks that policymakers should heed. Nonetheless, the policy proposals that Congress is currently considering would not notably add to those risks.

This is the moment to strengthen the social insurance system and to enact an ambitious federal investment package. Together, those policy changes would make the US economy more resilient and productive over the longer term. Additionally, they would broaden the degree to which prosperity in the United States is shared across workers and families.

**Strengthening the social insurance system**

The proposals that are currently included in the reconciliation package would strengthen the social insurance system, and empirical evidence shows that those changes would improve well-being and make our economy more resilient.

The social insurance system in the United States, implemented by federal, state, and local government agencies, provides protection against what President Franklin Delano Roosevelt called the vicissitudes of life: disability, the loss of earnings in old age, being laid off, and other
setbacks. The social insurance system also provides support to help people meet their basic needs and gain the skills and services they need to enter and succeed in the workforce. It encompasses a wide range of government programs, from the Social Security system, to Unemployment Insurance, to early childhood education. Nearly everyone in the United States directly benefits from the social insurance system at some point in their lives. Moreover, everyone indirectly benefits from it—either from knowing the system would be there for them during some unexpected hardship or simply because it helps to support the overall economy.

**How does the social insurance system reduce income inequality and poverty?**

Although the social insurance system reduces income inequality, it could do more. The United States is among the advanced OECD countries with the greatest inequality before taxes and transfers; it also has the widest inequality after these policies are taken into account. This is a result both of pre-tax-and-transfer income inequality being high in the United States relative to the other advanced OECD countries and of the reduction in inequality from taxes and transfers being smaller in the United States than in most other OECD countries (figure 1).

**Figure 1.**

Gini Coefficients Before and After Tax and Transfers in Advanced OECD Countries

![Gini Coefficients Chart]

Using a measure of poverty that includes benefits from federal programs (the Supplemental Poverty Measure, or SPM) data show that in recent years social insurance programs had cut the SPM poverty rate in half after post-tax-and-transfer income is taken into account. As a result of the enormous fiscal support provided to households in 2020, the percentage of the US population in poverty, as measured by the SPM, fell from 12 percent to 9 percent; if Congress had not enacted relief for families, SPM poverty would have risen to 13 percent rather than falling to 9 percent. The two policies that had the most significant effects relative to earlier years, because they were the most changed from prior policy, were the expansion of unemployment compensation and checks to households.

Figure 2.

Poverty Rates Using the Official and Supplemental Measures of Poverty

With respect to children, in 2019 the child poverty rate before benefits and taxes was 20 percent. After benefits and taxes are taken into account, the child poverty rate was 13 percent. In 2020, owing to the robust fiscal support in the face of a massive economic shock, the SPM poverty rate for children fell to 10 percent. Nonetheless, for some groups of children, poverty rates after taxes and transfers remained very high. Data from 2015 highlights the disparities: the National Academy of Sciences found that in that year, child poverty rates for Black and Hispanic
children were more than twice as high as non-Hispanic white children. The same report found that children of single parents endure double the poverty rate of a two-parent household (NAS, 2019).

In 2021, continued fiscal support—particularly the full refundability of and the increase in the child tax credit and increases to the Supplemental Nutrition Assistance Program (SNAP) maximum benefit—as well as the continued labor market recovery should help to lift households out of poverty. Another factor behind the decrease in poverty was the relatively strong wage growth for those at the bottom of the income distribution who remained employed. Notably, those wage gains came on the heels of strong wage growth in 2018 and 2019, when the tight labor market benefited lower-wage workers.

How would the proposed policies alleviate poverty, reduce inequality, improve well-being, and make the economy more resilient?

The successes in 2020 and 2021 of expanding and improving our social insurance system show some of the potential of making improvements in policy. Of course, the pandemic also exacerbated long-standing challenges and highlighted areas where better policies are needed. Making some policies permanent would make sustained progress in reducing post-tax-and-transfer poverty and provide more insurance protection to families.

In this section, I summarize evidence for the benefits of reforming and expanding the social insurance system in the following areas: the Child Tax Credit, child care, paid leave, the Earned Income Tax Credit, and health care. In an appendix, I offer additional detail on those areas of the social insurance system and evidence about the programs’ efficacy. Although the changes discussed here are not the only improvements to the social insurance system included in the reconciliation package, I limit my discussion for tractability and because the changes I describe here are useful illustrative examples.

**Child Tax Credit (CTC).** Extending the changes that the American Rescue Plan (ARP) made to the CTC for 2021—most importantly, making permanent the full refundability of the tax credit—would lock in place the enormous good this policy is doing for child poverty rates. Those changes the ARP made to the CTC, along with the other measures in the ARP, are projected to reduce poverty among children in 2021 from 14 percent to 8 percent (CPSP 2021). Indeed, more than 400 economists signed onto a letter supporting this change, based on evidence that CTC
reduces child poverty and improves academic and long-term outcomes for children without affecting parental labor supply (Hoyes and Schanzenbach 2021).

Child care. The current policy proposal would make permanent the recent expansion of the Child and Dependent Care Tax Credit (CCDTC) and grants and tax subsidies aimed at raising wages of child-care providers. Those changes would help families with earnings too low to owe federal income tax afford child care and would improve the quality of child care and early childhood education, the benefits of which are well-documented. Together, the changes would boost the labor supply of parents of young children.

Paid leave. Standing up a federal paid family and medical leave program would improve children’s health, reduce worker turnover, and increase labor force participation with perhaps the largest effects for disadvantaged children and mothers.

Earned Income Tax Credit (EITC). The current proposal would make permanent the recent expansion of the EITC for adults without children. Doing so would reduce poverty and income inequality and increase labor force participation.

Health insurance. If Congress made permanent the expansions to health-insurance premium tax credits and cost-sharing subsidies included in the ARP, the uninsured rate would fall by 13.6 percent (4.2 million) and lower-income households would be more financially secure (Banthin et al. 2021). Further expansions in access to Medicaid would do more to extend access to health care, where we have ample evidence that access increases annual health-care use among child and adults and improves the quality of life.

The effect on the economy of the reconciliation package and the bipartisan infrastructure package

The ambitious policies included in the reconciliation package and the bipartisan infrastructure package would not create worrying inflation risk and their effect on the long-term fiscal trajectory would be modest. The revenue raising policies would have only muted negative effects on incentives to work and invest, while some other policies would increase those incentives.
Muted near-term economic effects on output and inflation

The policies Congress is currently considering would have only a modest effect on economic activity in the short term. We should not think of those policies as fiscal stimulus. Take for example expansion of tax credits and other tax policy changes being proposed by the House Ways and Means committee. The staff of the Joint Committee on Taxation estimates that those provisions, on net, would be nearly deficit neutral over the next two years. Other parts of the reconciliation package, such as the clean energy initiatives, would likely take over a year to fully implement.

Instead, the effective expansion of the social insurance system, some right-sizing in tax revenues, and investments in social and physical infrastructure would make the economy more productive and resilient over the longer term and lead to greater well-being and more equitably shared growth.

Moreover, the reconciliation package in combination with the bipartisan infrastructure package would not create notable inflation risk in the near term. The recent increase in inflation is largely attributable to the recent burst in consumer demand, which has outpaced supply, and also to various disruptions in global supply chains. Policymakers across many countries are rightfully paying attention.

There are two primary reasons why the rise in inflation is unlikely to persist. First, the significant shifts in demand and bottlenecks are a function of the recent, temporary pace of economic activity. For example, demand for automobiles recovered quickly during the pandemic to high levels even as production was curtailed, in part due to disruptions in the supply chain for critical semiconductors. The result has been a sharp increase in prices for new and used vehicles. Second, as production is increased (with normalization of global supply chains) and growth in demand abates, inflation should slow overall. Nonetheless, certain factors will continue to create inflationary pressure, even with the slowdown, economic activity over the next year or so will continue to exceed the sustainable level. We might also see price spikes in certain services as demand shifts. For example, from March 2021 through July sales at restaurants were up 14 percent while sales at building materials and garden stores were down 11 percent. Such changes could lead to price surges at restaurants that more than offset softer prices at stores selling building materials and garden supplies. In addition, the rapid rise we have seen in home prices will likely translate into significantly higher rental costs across the country.
Fiscal trajectory little changed

Policymakers have stated their goal is to include increases in tax revenues and decreases in spending that would fully offset the decreases in revenue and increases in spending. If something close to a full offset is achieved, the reconciliation package would do little to the projected debt trajectory.

To be sure, as has been true for a long time now, policymakers have long-term challenges with regards to the federal budget. However, that fiscal trajectory is not an urgent challenge that policymakers need to take on in this legislative effort. Over the next decade, under current law, debt as a share of GDP rises only modestly in CBO’s baseline. And, notably, that baseline includes roughly a doubling of the 10-year rate over the next decade. So, an increase in interest rates is not, on the face of it, a risk to that debt trajectory; an increase in rates is already reflected in that trajectory.

Beyond the next decade, debt as a share of GDP is indeed projected to rise – with rising interest costs and rising spending on major health care programs coupled with relatively flat revenues as a share of GDP. However, this reconciliation package – even if the estimates end up showing it would modestly increase the cumulative deficit over the next decade – would not meaningfully worsen those challenges.

The long-term economic effects

An essential aspect of a federal budget is raising revenue, and it is virtually impossible to raise revenue without creating some negative incentives to work or to invest. But, good tax policy minimizes those negative effects. The tax provisions that raise revenue that are currently being considered in the reconciliation package would raise substantial revenue and have only modest negative effects on incentives.

Because the policies would undo some of the changes enacted as part of the 2017 tax act, it is instructive to consider how those prior changes were estimated to affect the economy. CBO, as well as a broad consensus of other groups, estimated that the 2017 tax act boosted the level of economic output in the longer term by less than 1 percent, with essentially no effect on the long-term growth rate. CBO estimated that positive incentive effects on spending on nonresidential
fixed investment raised the level of GDP after several years by less than one-half percent (CBO 2018).

Economists are currently debating whether effects on investment following the enactment of the 2017 tax act were smaller than projected (Gale and Haldeman 2021; Gravelle and Marples 2019; Kopp et al. 2019). One reason for that debate – and why it won’t ever be definitively settled – is that the projected effects were themselves small relative to the size of the US economy. As a result, it is difficult to disentangle what happened to investment from the tax act or from the many other effects and economic developments. In sum, the effect of the tax act on investment was small enough that it is getting lost in the noise.

Similarly, consider how the 2017 tax act cut effective marginal tax rates on labor income – averaged among all workers in the US – by a little over 2 percentage points at its peak. That was estimated to increase average hours supplied by the workforce by about a quarter of a percent. The reconciliation package currently includes a similarly sized increase in the effective marginal tax rates on labor income – but only for a small portion of the labor force comprised of the highest income people. If that increase in tax rates were enacted, the aggregate effect on labor supply would be small enough that we likely could not separately identify it.

Nonetheless, the increase in effective marginal tax rates for the highest income earners is not the only aspect of the reconciliation package that would dampen incentives to work. To some degree, people work as many hours as they do because they are financially desperate, or because they fear financial hardship owing to such events as losing a job or suffering from a health event. Although the vast majority of people who benefit from the social insurance system work for pay (for example, well over 90 percent of families receiving the Child Tax Credit [Goldin and Michelmore 2020]), a lessening of those factors could reduce hours worked per week. To put such effects in context, policymakers should focus on what a policy’s primary goal is: providing insurance, improving well-being, increasing labor force participation and hours worked per week, or raising revenue.

While the revenue raisers in the reconciliation package would have muted negative effects on incentives to work and invest, other policies would increase the incentives to work and invest. For example, improving access to high-quality and affordable child care and ensuring that workers have access to paid family leave would lower the cost of working among parents of young children and thus increase their supply of labor. It would also, over the longer term,
improve the earning potential of those children who benefit. As another example, expanding the EITC would increase labor force participation. In addition, with a larger and more productive workforce, firms would have greater incentives to invest in the US and expand the capital stock.

**Conclusion**

Although these remarks have focused on the fiscal effects and the aggregate economic effects of the policies under consideration, those should not be the only – and perhaps not even the primary – points of consideration. The tax provisions being proposed, and indeed many of the policies being proposed, would improve well-being and ensure that our prosperity is more widely shared. GDP estimates and net deficit effects attract attention because they are numbers with seemingly a lot of precision. And numbers have power. However, I urge policymakers to step back from those estimates and consider whether the policies they are debating would move us closer to the kind of society we want to live in.
Appendix. Further Discussion of Changes to the Social Insurance System

In this section, I offer additional detail on these areas of the social insurance system and evidence about the relevant programs’ efficacy: the Child Tax Credit, child care, paid leave, the Earned Income Tax Credit, and health care.

Child Tax Credit (CTC)

The CTC is a per child tax credit, which prior to the ARP provided a credit of up to $2,000 per child to eligible tax filers with children under age 17. Most low-income children, however, and many modest-income children as well—about 27 million children in all—received either no credit or only a partial credit because families with earnings below $2,500 did not qualify, and the credit phased in very slowly as a family’s earnings rose above that level.

For 2021, the ARP makes low- and modest-income children eligible for the full credit amount per child, removing the earnings requirement and slow phase-in. The ARP also raises the credit for 2021 to $3,600 per year per child under age 6 and $3,000 per child for those aged 6–17, thereby adding 17-year-olds to the eligible pool. It also changed the distribution of the tax credit to periodic rather than annual (unless a filer opts to receive the credit annually). Those changes, set to expire after 2021, along with the other measures in the ARP, are projected to reduce poverty among children in 2021 from 14 percent to 8 percent (CPSP 2021).

The CTC extends far up the income scale: with changes made by the 2017 tax act, married filers with incomes up to $400,000 can receive the full credit and married filers with two children and incomes between $400,000 and $480,000 can receive a partial credit. In fact, prior to changes made by the ARP (and after those changes, which are currently scheduled to be in effect for only one year, expire), the CTC was more valuable to higher-income families than to lower-income families. That was a consequence of families with no or very low earnings not qualifying, the size of the credit phasing in slowly for working-poor families as their earnings rise, and the imposition of a limit on the size of the credit for filers who did not earn enough to have federal income-tax liability.

Child care

The Child and Dependent Care Tax Credit (CCDTC) subsidizes a portion of child-care costs. Prior to 2021, that credit primarily helped middle-income families. The ARP enlarged the
credit and made it fully refundable for 2021, so that families with earnings too low to owe federal income tax can receive the full benefit of the credit.

Improving access to the CCDTC helps to provide access to high-quality, affordable child care and early childhood education. Early childhood education, or ECE, is a term used to describe center-based care and other nonparental forms of supervised child care. ECE can refer to preschool or pre-kindergarten programs that support children’s early social and academic development as well as day care. Programs that directly support access to child care for eligible families include Early Head Start, Head Start, the Child Care Development Fund (CCDF), and the Preschool Development Grant (PDG). As of 2019 there were 5.4 million children in a federal or state ECE program. Nonetheless, there is not sufficient capacity for all eligible families to be served by the public programs. As a result, many lower-income families do not have the resources to enroll their children in a preschool program (Workman and Jessen-Howard 2018; Malik 2019). Extending access to the CCDTC helps to shore up those resources.

However, improving the CCDTC is not enough. Our underinvestment in ECE is evident in the challenges faced by providers. As described in a Hamilton Project proposal by Elizabeth Davis and Aaron Sojourner:

For childcare providers public underinvestment means low wages, high turnover, and an inability to expand or improve services (Whitebook et al. 2014; Workman 2018). Those working in the child-care field earn among the lowest average wages of any occupation, and pay and benefits lag well below the earnings of workers with similar educational credentials (Vogtmann 2017). Quality in ECE depends on the stability of nurturing relationships between adults and children, but high turnover of staff due to low pay disrupts those relationships (Caven et al. 2021). One study found that the average annual turnover rate of child-care staff was 30 percent, which imposes significant costs on child-care businesses and also impacts the quality of care by disrupting child-teacher relationships (Porter 2012).

As a result of under-resourcing of ECE, the sector has been unable to pay workers anything close to their marginal social value. The system should provide resources so that ECE workers’ earnings are at a level that recognizes the value
they create and permits ECE employers to attract, motivate, and retain talented caregivers.

Furthermore, our society underestimates the value of care work, connected to the fact that women, and especially Black and Latina women, disproportionately do this work. More than 93 percent of ECE workers are women. Non-Hispanic white Americans make up a 13 percent lower share of the child-care workforce than their share of the population, while Black Americans make up a 24 percent higher share. Furthermore, Black educators were more likely to work in low-wage child-care centers (Caven et al. 2021; Data USA 2020). Recognizing the full value this work creates in our community by directing more resources to the workforce would constitute concrete progress against racism and sexism in the labor market.

Sojourner and Davis also document the significant imbalance in public investment across ages. As those authors write and the figure shows, “In 2019 public spending amounted to less than $500 per child in care and education during the first three years of life, and about $2,800 per child for children ages three to four, compared to $12,800 per child for elementary-age children.”

Federal, State, and Local Government Spending on Child Care and Education in 2019, by Age Group

<table>
<thead>
<tr>
<th>Age Group</th>
<th>Per Person Spending (2019 dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Two and Under (ECE Infants and Toddlers)</td>
<td>0</td>
</tr>
<tr>
<td>Three to Four (ECE Preschool)</td>
<td>4,400</td>
</tr>
<tr>
<td>Five to Eighteen (K-12)</td>
<td>11,800</td>
</tr>
</tbody>
</table>

Source: Cascio and Scharzenbach (2019); Census (2020); Crandall Hollick and Boyle (2019); Friedmann-Krause et al. (2003); Aguinner (2019); NCES (2002); NASSCE (2019); OCC (2011a; 2011c; 2011f); Office of Head Start (2019); author’s calculations.

Note: Expenditures include spending on the school-based prekindergarten programs, Child Care and Development Fund, Early Head Start, Child and Dependent Care Credit, and K-12 education. For additional details, see endnote four.
The benefits of high-quality ECE programs are well-documented. Evidence on the short- and long-term effects of ECE typically relates to the outcomes of specific programs, whether the evidence comes from the landmark evaluations of Perry Preschool, Abecedarian, and Head Start, or from the rollout of state preschool programs (see Cascio 2021 for a review). A meta-analysis of research on ECE concludes that children who participate in ECE programs in their first five years have lower rates of repeating a grade and higher high school graduation rates (McCoy et al. 2017).

**Paid leave**

The United States does not have a national paid leave program. At the national level, we only have the Family and Medical Leave Act of 1993 (FMLA), which allows eligible employees to take up to 12 work weeks of unpaid leave during any 12-month period for caregiving or illness recovery purposes. Employers and employees must meet several criteria for employees to use the FMLA for leave. The firm must be relatively large (at least 50 employees within a 50-mile radius, though in eight jurisdictions the threshold is lower); the employee must have worked for the employer for at least 12 months; and the employee must have worked at least 1,250 hours in the past 12 months. Additionally, the FMLA applies only to immediate family members in all but 11 jurisdictions. Some states and localities have passed laws requiring employers to give eligible employees paid leave. As of early 2021, however, paid family leave—leave that can be used for post-birth/adoption care and caregiving for sick family members—is available in only six states. Two others have passed legislation and are in the process of implementing it.

We have evidence of the efficacy of paid leave from those states and from the effects of FMLA. FMLA reduces worker turnover (Appelbaum and Milkman 2011) and enhances children’s health (Rossin 2011; Ruhm 2000). Economic benefits of FMLA for workers and employers include increased labor-force participation, increased lifetime earnings and retirement benefits, and increased use of leave (Boushey, O’Leary, and Mitukiewicz 2013). Research from states with paid leave programs find higher rates of maternal leave take-up and increased job return post-leave (Baum and Ruhm 2013; Byker 2016; Rossin-Slater, Ruhm, and Waldfogel 2011). The positive effects of leave are strongest among disadvantaged mothers (Byker 2016; Rossin-Slater 2013). However, some evidence shows negative wage effects from paid parental leave for women so the potential for paid leave policies to close the gender pay gap remain unclear (Bailey et al. 2019).
**Earned Income Tax Credit (EITC)**

The EITC is a refundable tax credit available to income-eligible households that work, which means that the IRS sends eligible claimants a refund check each year after they file their tax returns. The EITC phases in as a family’s earnings rise up to a certain income level and then gradually phases down above a somewhat higher income level.

The ARP expanded the EITC in 2021 for workers not raising children at home; in 2020, its maximum benefit was $538; workers who are not married (most beneficiaries of the childless EITC are single) became ineligible at incomes of only $15,820. For tax year 2021, the ARP nearly triples the maximum benefit for the childless workers’ EITC to about $1,500, raises to $21,427 the income at which the credit phases out entirely for single workers, and makes workers 65 and over and workers who are 19 to 24 years old eligible for the childless workers’ EITC for the first time, excluding students under 24 who are in college at least half time.

While the point estimates vary, studies find that EITC raises labor force participation and annual income among lower income families (Eissa and Lieberman 1997; Meyer and Rosenbaum 2001; Hoynes and Patel 2018; Bastian 2020; Schanzenbach and Strain 2020; see Hoynes and Rothstein 2016 for a review of the literature). Indeed, the EITC has a stronger effect in increasing labor force participation than it does in increasing the number of hours worked among those already employed (Saiz 2010). Scholars have found that EITC improves many aspects of well-being, including economic (Baughman and Dickert-CONLINE 2009; Neumark, Asquith, and Bass 2019), health (Hoynes, Miller, and Simon 2015; Braga, Zblavín, and Gangopadhyaya 2020), and human capital (Chetty, Friedman, and Rockoff 2011; Bastian and Michelmore 2018).

**Health insurance premium tax credits and cost-sharing subsidies**

Despite the different programs aimed at increasing the availability of health coverage in the United States, millions of Americans are still uninsured. A report from the CBO suggests the high cost of health insurance premiums and deductibles and the complexities for enrolling for coverage create obstacles for some of the eligible to receive coverage. (CBO 2020b).

For those who are not eligible for public health insurance and who do not have access to affordable employer-based coverage, the Affordable Care Act established premium tax credits that people with incomes between 100 percent and 400 percent of the poverty line can use to subsidize the purchase of health insurance in the Affordable Care Act’s marketplaces, along with a series or rules to ensure the marketplaces function effectively. A second set of subsidies, to
reduce cost-sharing charges, is available to people enrolled in marketplace plans who have incomes between 100 and 250 percent of the poverty line. The tax credits generally are not paid directly to beneficiaries; rather, the US Department of the Treasury sends them directly to the insurance company in whose plan a beneficiary is enrolled.

The American Rescue Plan both increases the size of the subsidies and eliminates the 400 percent of poverty eligibility cut-off for 2021 and 2022. If this change were made permanent, the Urban Institute estimates that the uninsured rate would fall by 13.6 percent (4.2 million) and save enrolled households more than a thousand dollars (Banthin et al. 2021)

References


Whitebook, Marcy, Deborah Phillips, and Carollee Howes. 2014. “Worthy Work, STILL Unlivable Wages: The Early Childhood Workforce 25 Years after the National Child Care Staffing Study.” Center for the Study of Child Care Employment, University of California, Berkeley, CA.

Testimony of Dr. William H. A. McBride, Vice President of Federal Tax and Economic Policy, Tax Foundation

Before the Joint Economic Committee


October 6, 2021

Chairman Beyer, Ranking Member Lee, and members of the Joint Economic Committee, thank you for inviting me to testify today.

I am Dr. William McBride, Vice President of Federal Tax and Economic Policy at the Tax Foundation, and today I will share the key findings of our analysis of the most recent iteration of the President’s Build Back Better Agenda.

There are three primary takeaways from our analysis. The first is that the corporate tax is not just paid by corporate shareholders: raising the corporate tax rate will reduce investment and productivity growth, ultimately leading to lower wages across the board.

The second is that further increasing the progressivity of the tax code by raising individual income taxes for high-income earners comes with a cost: it will reduce incentives to work, save, and invest, broadly reducing employment opportunities throughout the economy.

And lastly, the tax code is not an effective tool for social policy: optimal tax policy raises the amount of revenue needed while creating minimal economic costs, and other goals are better addressed through proper spending programs.
Point 1: Raising Corporate Income Taxes Will Reduce Investment in America

Raising corporate income taxes has a large negative impact on the U.S. economy, because it reduces the after-tax return on corporate investment, reducing incentives to invest. As investment shrinks, worker productivity declines along with wages and hiring.

Our modeling of the Ways and Means Committee’s latest Build Back Better proposal found that the plan would reduce the size of the economy by about 1 percent in the long run, shrink the capital stock by 1.8 percent, cut wages by 0.7 percent, and cost more than 300,000 jobs. While the proposal would increase tax revenue by about $1.06 trillion over 10 years, conventionally estimated, in the long run it would reduce GDP by more than $2 for every $1 raised.

The revenue and economic impacts are largely driven by the plan’s increase of the corporate tax rate to 26.5 percent, which would reduce long-run GDP by 0.6 percent, the capital stock by 1.1 percent, wages by 0.5 percent, and cost over 100,000 jobs.

### Overall Impact of the Ways and Means Package

<table>
<thead>
<tr>
<th>Economic Indicator</th>
<th>Percentage Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long-Run Gross Domestic Product</td>
<td>-0.98%</td>
</tr>
<tr>
<td>Long-Run Gross National Product</td>
<td>-1.01%</td>
</tr>
<tr>
<td>Capital Stock</td>
<td>-1.84%</td>
</tr>
<tr>
<td>Wage Rate</td>
<td>-0.68%</td>
</tr>
<tr>
<td>Full-Time Equivalent Jobs</td>
<td>-303,000</td>
</tr>
<tr>
<td>Conventional Revenue (10-Year)</td>
<td>$1.06 trillion</td>
</tr>
<tr>
<td>Dynamic Revenue (10-Year)</td>
<td>$804 billion</td>
</tr>
</tbody>
</table>


### Impact of Selected Corporate Provisions from the Ways and Means Package

<table>
<thead>
<tr>
<th>Economic Indicator</th>
<th>Raise the Corporate Tax Rate to 26.5 Percent</th>
<th>International Provisions (combined)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long-Run Gross Domestic Product</td>
<td>-0.6%</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Long-Run Gross National Product</td>
<td>-0.5%</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Capital Stock</td>
<td>-1.1%</td>
<td>-0.2%</td>
</tr>
<tr>
<td>Wage Rate</td>
<td>-0.5%</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Full-Time Equivalent Jobs</td>
<td>-107,000</td>
<td>-12,000</td>
</tr>
<tr>
<td>Conventional Revenue (10-Year)</td>
<td>$704 billion</td>
<td>$136 billion</td>
</tr>
</tbody>
</table>


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The international tax increases on U.S. multinationals (MNEs), including higher taxes on Global Intangible Low-taxed Income (GILTI) and a new limit on interest expense, further reduce the size of the economy by about 0.1 percent, the capital stock by 0.2 percent, wages by 0.1 percent, and jobs by 12,000. Higher GILTI taxes reduce the incentive of U.S. MNEs to invest in research and development (R&D) in the U.S. due to reduced after-tax income from intellectual property (IP) that has been located abroad. There is an additional effect of higher international taxes that we have not modeled (due to a lack of data): the reduction in American incomes arising from the incentive of U.S. MNEs to avoid the international tax increases by selling foreign assets to foreign competitors.

The international tax increases are intended to reduce profit shifting, i.e., the ability of U.S. MNEs to shift profits abroad where taxes are lower. However, we find that profit shifting would be made worse by the bill, as it would increase taxes on domestic income more than it would on foreign income. Specifically, the bill raises the statutory corporate tax rate 5.5 percentage points and raises the tax rate on Foreign Derived Intangible Income (FDII), while raising the effective tax rate on foreign income by between 2.4 and 5.1 percentage points over the budget window. On net, we estimate increased profit shifting by U.S. MNEs reduces revenue by $57.9 billion over a decade.3

These estimates do not include the benefits of infrastructure, since that is not included in the House reconciliation bill. However, in our modeling of the American Jobs Plan, which included about $1.7 trillion in infrastructure spending as well as a higher corporate tax rate of 28 percent among other tax increases, we found that plan would on net reduce GDP by 0.5 percent and cost more than 100,000 jobs.4

The negative impact of corporate taxes on economic growth is well-documented.5 An OECD study examining data from 63 countries concluded that corporate income taxes are the most economically damaging way to raise revenue, followed by individual income taxes, consumption taxes, and property taxes.6 A study on taxes in the United Kingdom found that taxes on consumption are less economically damaging than taxes on corporate and individual income.7 A study of U.S. tax changes since World War II found that a 1 percentage point cut in the average corporate tax rate raises real GDP per capita by 0.6 percent after

one year, a somewhat larger impact than a similarly sized cut in individual income taxes. Based on U.S. state taxes, a study found that a 1 percentage point cut in the corporate tax rate leads to a 0.2 percent increase in employment and a 0.3 percent increase in wages.

Furthermore, several studies demonstrate that the corporate tax is borne in part by workers. For instance, a study of corporate taxes in Germany found that workers bear about half of the tax burden in the form of lower wages, with low-skilled, young, and female employees disproportionately harmed.

The corporate tax is also borne by owners of shares, including retirees earning considerably less than $400,000. In the short run, the Joint Committee on Taxation (JCT) assumes owners of capital bear all of the corporate tax, yet that includes more than 90 million tax filers earning less than $200,000. In the long run, JCT assumes workers bear a portion of the corporate tax, such that the burden falls on more than 150 million tax filers earning less than $200,000.

In its distributional analysis of the House bill, including the corporate taxes, the JCT finds that 34.8 percent of filers earning between $100,000 and $200,000 will see a tax hike of more than $100 in 2023, and by 2027 that figure grows to 85.8 percent.

Another downside to raising corporate taxes is it would reduce the competitiveness of U.S. companies. In a global economy in which firms based in countries all over the world compete to reach customers globally, corporate taxes are an important factor. As it stands, the U.S. corporate tax rate is competitive, but the GILTI tax is not, as it is a unique tax burden that only applies to U.S. firms over and above corporate tax paid to foreign governments on earnings abroad.

Regarding the corporate tax rate, at 25.8 percent inclusive of the average state corporate tax rate, the U.S. ranks slightly above the OECD average of 22.7 percent. The House bill would raise the federal corporate rate from 21 percent to 26.5 percent, which results in a combined federal-state corporate tax rate of 30.9 percent—the third highest corporate tax rate in the OECD, behind only Colombia and Portugal. A similar result holds when...
accounting for various deductions and other tax preferences, i.e., U.S. effective corporate tax rates would rise to among the highest in the OECD under the House plan.\textsuperscript{15}

Regarding the U.S. international tax system, we estimate that GILT\textsuperscript{1} and other features of the current international tax system, including expense allocation, add about 5 or 6 percentage points of U.S. residual tax to the foreign earnings of U.S. MNEs, i.e., on top of foreign taxes. The international tax changes proposed in the House bill would increase the U.S. residual tax to about 10 percentage points or more, an increase of more than 70 percent in 2022.\textsuperscript{16} That sort of tax increase on an already high U.S. residual tax could invite


U.S. MNEs to engage in a variety of maneuvers to avoid it, including tax inversions and other mergers and acquisitions, along the lines of what we observed prior to the Tax Cuts and Jobs Act (TCJA), in which several major U.S. companies moved their headquarters abroad to low-tax countries.17

**Point 2: Increasing the Progressivity of the Tax Code Comes with a Cost**

On its own, the appeal of living in a society where incomes are more evenly distributed is understandable, and potentially desirable to many Americans. However, doing so by raising taxes on high earners, as the House bill proposes, comes with serious economic costs. Namely, it reduces incentives to work, save, and invest, negatively impacting the broader economy, particularly entrepreneurs who are starting and growing the next generation of businesses, including pass-through businesses such as partnerships and S corporations.

The pass-through sector is large, representing more than half of U.S. private sector employment.18 These firms “pass through” earnings to owners who report them on individual income tax returns. The House bill levies several tax increases on pass-through business income, including:

- Raising the top marginal tax rate on ordinary income to 39.6 percent,
- Adding a 3 percent surcharge on modified adjusted gross income over $5 million,
- Capping the Section 199A pass-through business deduction at $500,000 for joint filers,
- Applying the 3.8 percent net investment income tax (NIIT) to active pass-through business income in excess of $500,000 for joint filers, and
- Limiting losses for pass-through businesses.

As a result of these tax increases, the top federal tax rate on pass-through business income, as well as ordinary income, would reach 46.4 percent—the highest since 1986. Including state-level income taxes, the combined top marginal tax rate would exceed 50 percent in 41 states.19

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It may be claimed that the proposed tax increases only impact a small percent of firms, but economically it is more important to consider the share of business income that is affected. Our estimates indicate that more than half of pass-through business income would face a tax increase under these proposals.20

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Our modeling of the House bill indicates the individual income tax increases would reduce the size of the economy by about 0.3 percent in the long run, shrink the capital stock by 0.6 percent, cut wages by 0.1 percent, and cost more than 140,000 jobs. Most of the economic impact results from the five major tax increases on pass-through businesses listed above.

### Impact of Selected Individual Income Tax Provisions from the Ways and Means Package

<table>
<thead>
<tr>
<th></th>
<th>Increase Income Tax Rate to 39.6 Percent and Apply to More Income</th>
<th>Apply a 3 Percent Surcharge to Modified Adjusted Gross Income</th>
<th>Other Pass-through Business Provisions (Combined)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long-Run Gross Domestic Product</td>
<td>-0.1%</td>
<td>Less than -0.05%</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Long-Run Gross National Product</td>
<td>-0.1%</td>
<td>Less than -0.05%</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Capital Stock</td>
<td>-0.1%</td>
<td>Less than -0.05%</td>
<td>-0.4%</td>
</tr>
<tr>
<td>Wage Rate</td>
<td>Less than -0.05%</td>
<td>Less than -0.05%</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Full-Time Equivalent Jobs</td>
<td>$64,000</td>
<td>$52,000</td>
<td>$24,000</td>
</tr>
<tr>
<td>Conventional Revenue (10-Year)</td>
<td>$157 billion</td>
<td>$131 billion</td>
<td>$39 billion</td>
</tr>
</tbody>
</table>


The bill also raises the top long-term federal capital gains and qualified dividends tax rate 8 percentage points to 31.8 percent inclusive of the 3.8 percent NIIT and 3 percent surcharge. This would be the highest federal tax rate on capital gains since the 1970s. When considering state-level policies, the average top marginal combined tax rate on capital gains and qualified dividends would be about 37 percent.

Because the capital gains and qualified dividends tax increases reduce the after-tax return to saving for U.S. residents, U.S. saving would fall, and to some extent be replaced by foreign saving. As a result, we find that the share of U.S. investment financed by foreign savers would increase, with the returns to that investment accruing to foreigners rather than Americans, causing U.S. incomes, as measured by GNP, to decline about 0.1 percent in the long run.

There are several studies pointing to the economic costs of raising individual income taxes, particularly on high earners. A study based on postwar tax reforms in the United States found that reducing marginal tax rates for the top 1 percent of earners leads to increases in real GDP and declines in unemployment, with a 1 percentage point cut in the tax rate increasing real GDP by 0.78 percent by the third year after the tax change.25

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In looking at the experience of developed countries over the period 1971 to 2004, OECD researchers concluded that “a reduction in the top marginal [individual] tax rate is found to raise productivity in industries with potentially high rates of enterprise creation. Thus, reducing top marginal tax rates may help to enhance economy-wide productivity in OECD countries with a large share of such industries.”26

The Congressional Budget Office (CBO) recently modeled three types of tax increases to fund a permanent increase in government spending of 10 percent of GDP annually: a flat labor tax, a flat income tax, and a progressive income tax. The CBO found that a progressive income tax is the most economically damaging, reducing GDP by 10 percent after 10 years, and reducing lifetime consumption and hours worked especially for younger households.27

Finally, it should be noted that after all the tax code changes over the last 40 years, the tax code remains highly progressive. As a result, according to the latest IRS data for 2018, the top 1 percent of income earners paid 40.1 percent of federal individual income taxes—the highest share since 1980—while earning 20.9 percent of income.28 Accounting for all federal taxes, data from the CBO and Treasury Department confirm that the tax code is progressive overall. For instance, Treasury finds that the highest earners pay the highest average effective tax rates when considering all federal taxes—the top 0.01 percent will pay an average federal ETR of 32.9 percent under current law in 2022.29

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26 Åsa Johansson, Christopher Heads, Jens Arndt, Bert Bojs, Cyrille Schwellnus, & Laura Varka, “Taxation and Economic Growth.”
Point 3: Adding More Complexity to the Tax Code Is Problematic

Another economic downside of the plan is additional complexity and uncertainty. It adds 22 new tax credits and expands several existing ones, at a budgetary cost of more than $1 trillion over the next 10 years. This approach has several problems, in addition to the budgetary cost. First, while recognizing that tax cuts are effective incentives, this approach picks winners and losers through the political process rather than letting the market process determine the most valuable use of resources. Do we really think lawmakers have taken the time to do any sort of cost-benefit analysis on these proposals, and will they find time to effectively monitor and respond to the changing costs and benefits over time?

Second, the approach adds complexity and compliance costs for taxpayers and administrative burdens for the IRS. Third, many of the policies are temporary, which creates uncertainty for taxpayers. Fourth, the bewildering array of tax credits and other tax preferences contributes to a dysfunctional federal budgeting process that generates chronic deficits.
By far the largest tax credit in the plan is the extension and modification of the Child Tax Credit (CTC), which as part of the American Rescue Plan Act (ARPA) was expanded temporarily for 2021 to include full refundability, an advanced monthly payment, and a maximum annual benefit of $3,600 per child. The plan would extend the ARPA CTC through 2025 and permanently extend full refundability (allowing the maximum benefit regardless of income), which would have a budgetary cost of more than $100 billion per year through 2025, more than double the cost of the current law CTC. That is, more than $200 billion per year will be spent on the CTC, which is about 10 percent of all individual income tax revenue or more than half of all corporate tax revenue forecast under current law.

Because of this huge budgetary cost, both the expanded CTC and the current law CTC are temporary, and yet likely to be extended beyond their planned expiration in 2025, thus obscuring the full budgetary cost over the 10-year budget window. We estimate that extending the ARPA CTC permanently would cost about $1.6 trillion over the budget window, far exceeding all of the individual income tax pay-fors specified in the House bill.

The refundable aspect of the CTC makes the budgeting and oversight process all the more arcane and difficult to track for voters, taxpayers, lawmakers, and the IRS. The expanded CTC is being sold as a tax cut, but it is in fact largely an outlay effect, i.e., spending, due to refundability. The history of refundability with the CTC goes back to its introduction in 2001 when the maximum benefit was $1,000 per child, and it has expanded under every administration since. During that time, the refundable CTC has been plagued with improper payments, e.g., the Treasury Department found that nearly one-third of refundable CTC payments in tax years 2009 through 2011 were made in error. Over its entire history the refundable CTC has contributed to a worsening budgetary outcome of chronic and escalating deficits.

In addition to its budgetary impacts, the complicated design and implementation of the CTC, as well as its temporary nature, creates confusion for taxpayers, especially low-income earners. For example, a recent survey found that while most parents (88 percent) are aware of the expanded CTC, households with incomes below $25,000 are least likely to have heard about the credit.

31 For example, the Joint Committee on Taxation estimates that about $14 billion of the approximately $155 billion ARPA CTC expansion is an outlay effect. See Joint Committee on Taxation, "Estimated Revenue Effects of H.R. 1359,” JCS-4-21, May 5, 2021, https://www.gpo.gov/fdsys/pkg/JCS-4-21/pdf/JCS-4-21.pdf.
33 The last year the federal government ran a budget surplus was 2011.
One thing they probably have not heard about is that the new monthly CTC contains a new definition of a child. Whereas the current CTC determines eligibility based on where the child lives for more than six months of the year, eligibility for the new monthly CTC is based on a five-factor “care” test specific to each month, including “involvement by the taxpayer in, and financial and other support by the taxpayer for, education or similar activities of the individual.” For families with multiple caregivers, e.g., split custody arrangements where the child spends part of the month with one or another parent, a grandparent, aunt, etc., this is a recipe for confusion, conflict, and administrative uncertainty.36

There is another question about how the expanded CTC impacts work incentives. Economists have long understood the concept of an “income effect” in which the incentive to work is diminished because of having more income, including government benefits. A recent literature review indicates that a 10 percent increase in income from government benefits reduces hours worked by 1.5 to 1.6 percent.37 Partly out of these concerns, as well as concerns about budgetary costs, the CTC has historically been designed to phase in with income, effectively reducing marginal tax rates and increasing incentives to work for low-income households. The expanded CTC in the House bill eliminates the phase-in by making the CTC fully refundable, thus leaving only the work disincentive of the income effect for low-income households. In addition, the CTC phases out for higher income households, effectively raising marginal tax rates and reducing incentives to work for those households.38

Extending the CTC would provide relief for families, but it could be delivered in a less complex way that ideally would minimize work disincentives. Tax policy should be focused on how to raise revenue in the least economically harmful manner, and other goals should be handled as public spending subject to the appropriations process.39 Transforming the CTC into a spending program, delivered through, for instance, the Social Security Administration, would make the tax code more focused on its primary purpose, and make the budget process more transparent. This idea has supporters from both sides of the aisle.

The bill would also spend more than $20 billion per year on expansions of the Child and Dependent Care Tax Credit (CDCTC), Earned Income Tax Credit (EITC), and Premium Tax Credit, which come with their own compliance and administrative challenges. For example, the Treasury Department has routinely found that a large share of refundable EITC payments is made in error—25 percent in tax year 2018 according to a recent report.40

38 Eric York, Garrett Watson, Hucum LL “Temporary Policies Complicate the Child Tax Credit’s Future.”
40 Treasury Inspector General for Tax Administration, “Authorities Provided by the Internal Revenue Code Are Not Effectively Used to Address Erroneous Refundable Credit and Withholding Credit Claims.”
In addition, the bill provides or expands numerous smaller tax credits for specific economic activities, whether for certain types of clean energy investment, housing construction, or broadband development, among others. These credits have a mixed track record at addressing their core concerns. For instance, the Low-Income Housing Tax Credit has become increasingly ineffective as a means to stimulate affordable housing.\(^\text{43}\) Clean energy tax credits have been found to primarily benefit the wealthy.\(^\text{42}\)

Instead of these targeted incentives, lawmakers could address underlying biases against investment more generally, stimulating new projects in these specific areas in the process. As an example, by not allowing companies to fully deduct investments in structures, the tax code discourages new, more energy-efficient construction.\(^\text{43}\) Expensing for all capital investment would be a powerful pro-growth policy, while simplifying the tax code and helping solve many of these specific issues.\(^\text{44}\)

Indeed, the best provision in the bill is postponing the amortization of R&D expenses.\(^\text{45}\) Continuing to allow companies to fully deduct the cost of R&D is important for a wide range of crucial industries and issues, from pharmaceutical development to heavy manufacturing to green energy. However, the bill would not make full deductibility of R&D permanent, instead allowing it to expire after 2025 as opposed to after this year. Ideally, expensing of R&D would be permanent, providing companies with stable, long-term incentives to invest.\(^\text{46}\)


Conclusion

There are a couple of broad takeaways from this. When you tax something, you get less of it. This is why governments tax tobacco (and the House bill increases those taxes), because it reduces tobacco use. That, and it generates tax revenue. The costs of the higher taxes should be weighed against the benefits, e.g., more tax revenue, improved public health, etc. Likewise, taxing income will reduce the generation of income. That means a smaller economy, less prosperity, and less opportunity. The economic costs can exceed the benefits in terms of tax revenue, and that is what we find with the House bill.

The other takeaway is that the IRS can only do so much, and taxpayers are getting confused. The tax code is already excessively complex and the IRS is overwhelmed in its ability to administer and enforce the tax laws. There is a limit beyond which adding more complex provisions to the tax code no longer benefits taxpayers, the government, or the country as a whole. Rather than pushing the limit, we should seriously consider simplification.
ARTICLES FOR THE RECORD SUBMITTED BY REPRESENTATIVE SCHWEIKERT

1. Should the U.S. Copy Denmark’s Social Welfare Policies?

2. The Anti-Poverty, Targeting, and Labor Supply Effects of the Proposed Child Tax Credit Expansion

RESPONSE FROM DR. CLAUSING TO QUESTION FOR THE RECORD SUBMITTED BY SENATOR LEE

Dr. Clausing:
In your testimony, and in past work, you have each emphasized the importance of addressing income and wealth inequality. Yet, there is a contingent of lawmakers who are openly advocating for either lifting or repealing the $10,000 cap on the SALT deduction. Ironically, the success of the Build Back Better Act may hinge on whether changes to the cap are included.

According to the Brookings institution, “the SALT tax deduction is a handout to the rich.” Eliminating or raising the cap on this deduction is a policy change that would not meaningfully benefit middle-class households—or even upper-middle class households. Repealing the SALT cap would cost hundreds of billions of dollars in tax revenues and the top 5 percent of households would receive over 80 percent of the benefit.

What is your perspective on lifting or repealing the SALT deduction cap? Would including this change improve inequality or make it worse?

The Administration did not propose changes to the SALT deduction cap. However, any tax law changes should be evaluated on a holistic basis that considers the aggregate effects of all of the component parts. Although repealing the SALT deduction cap in insolation would reduce the progressiveness of the tax code between now and 2025 (the cap expires after 2025), any such repeal could be coupled with other reforms that make the tax system as a whole more progressive. As one example, the SALT cap was implemented in the context of a tax law change (the Tax Cuts and Jobs Act of 2017) that made our overall tax system less progressive. Likewise, a repeal of the cap could easily occur in the context of a tax law change that makes our overall tax system more progressive.

RESPONSE FROM MS. HUANG TO QUESTION FOR THE RECORD SUBMITTED BY SENATOR LEE

Ms. Huang:
In your testimony, and in past work, you have each emphasized the importance of addressing income and wealth inequality. Yet, there is a contingent of lawmakers who are openly advocating for either lifting or repealing the $10,000 cap on the SALT deduction. Ironically, the success of the Build Back Better Act may hinge on whether changes to the cap are included.

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What is your perspective on lifting or repealing the SALT deduction cap? Would including this change improve inequality or make it worse?

Thank you for your question, Senator Lee.

The Brookings estimate and Center on Budget analysis of the direct distribution and revenue impact of repealing the SALT cap are sound.

In the 2017 tax law, however, capping the SALT deduction was used to help offset the cost of tax cuts that were, overall, more tilted to the wealthiest filers than the benefits of the SALT deduction, so this was not a sound trade.

However, repealing the SALT cap now in the context of a package with a limited size is likely to mean less robust investments in other policies like the Child Tax Credit that directly benefit low- and moderate-income families, so that, too would be an unsound trade.3

Some proponents of repealing the SALT cap are concerned that the cap constrains the ability of states to raise progressive revenues and fund State investments with widely shared benefits. That is a reasonable concern, especially because in 2017, some supporters of capping the SALT deduction explicitly hoped that it would limit State revenue collection and investments.

However, the evidence on the SALT deduction’s impact on State budgets is inconclusive.4 For example, since the 2017 tax law went into effect, New Jersey has raised income taxes for households with incomes over $1 million, New York has extended and increased an existing millionaires’ tax, and three states (Connecticut, New York, and Washington state) have increased real estate transfer taxes on high-value homes.5 While it impossible to know precisely what states would have done without the cap in place, this does at least show that states can continue to raise progressive revenues and invest with the cap in effect.

Further, even if repealing or weakening the SALT cap were to make it somewhat easier to raise revenues for investments at the State level, that is likely to be a far less effective and cost-efficient way of delivering economic and budgetary benefits to states than alternatives proposed in President Biden’s Build Back Better agenda. For example, the proposed package makes critical investments in infrastructure, green jobs, community colleges and other areas of deep need.6 These investments would likely be far more effective, per dollar spent, at boosting strong and inclusive economic growth in states. Along with investments in areas like the CTC and child and elder care, these would be a far better use of the revenues raised by progressive tax changes.

RESPONSE FROM DR. EDELBERG TO QUESTION FOR THE RECORD SUBMITTED BY SENATOR LEE

Dr. Edelberg:

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- What is your perspective on lifting or repealing the SALT deduction cap? Would including this change improve inequality or make it worse?

My colleagues at the Brookings Institution, Christopher Pullam and Richard Reeves, have examined the state and local tax (SALT) deduction cap and find that under the current SALT cap, over ¾ of the tax benefit goes to the top quintile of households by income. Those authors point out that the main argument for the SALT deduction “is that it encourages states to spend more by making it easier for them to tax more.” Many of the State and local policies that are implicitly subsidized through the SALT deduction are progressively structured and aim to support disadvantaged households, despite the benefits of SALT tax relief disproportionately accruing to those with the highest incomes. However, repealing the SALT deduction cap is not the optimal policy approach if the goal is to provide fiscal support to fiscally active State and local governments. If the cap were raised or fully eliminated, the tax benefit would flow overwhelmingly to households at the top of the income distribution while providing little benefit to the after-tax incomes of middle-class households. Moreover, proposals to repeal the SALT cap that also include revenue raising offsets, such as increasing the top marginal income tax rate, risk exhausting a finite source of potential revenue while failing to address any of our Nation’s critical priorities. A better approach would provide additional Federal aid directly to states and localities in the form of grants to better target funding toward key priorities like K–12 education, infrastructure, and health care.

RESPONSE FROM DR. MCBRIDE TO QUESTION FOR THE RECORD SUBMITTED BY SENATOR LEE

Dr. McBride:

We know that pro-growth policies, like tax cuts and deregulation benefit low-income and otherwise disadvantaged Americans by creating strong labor markets and a healthy economy. Americans experienced these benefits following the 2017 tax cuts. Unemployment was historically low, including for women, Black Americans, and Hispanics. In my home state of Utah, per capita income grew 17 percent in the 3-years before the pandemic and some of the largest wage gains benefited the lowest income Americans. This strong pre-COVID economy is a testament to the power of getting the government out of the way and unleashing American ingenuity.

• Key pieces of the Democrats’ plan are targeted at reversing the very policy changes that helped support our strong economy. Can you speak briefly to the successes of the 2017 Tax Cuts and Jobs Act and then describe how these new tax increases might undermine some of the gains that Americans experienced?

A central goal of the Tax Cuts and Jobs Act (TCJA) was to reduce the tax burden on business investment, which it did primarily by reducing the corporate tax rate as well as tax rates on pass-through business income among other measures. Basic economic theory and much empirical evidence predicts investment increases when the after-tax return on investment increases, leading to a larger capital stock, more productivity, higher wages, more jobs, and faster economic growth.

Indeed, the Congressional Budget Office (CBO) projected that the effects of the TCJA would “include higher levels of investment, employment, and gross domestic product (GDP).” By most measures, the actual performance of the economy post-TCJA exceeded CBO’s forecasts, until the pandemic hit two years later. CBO forecasted in June 2017, prior to enactment of the TCJA in December 2017, that business investment (i.e., real nonresidential fixed investment) would grow by 4.8 percent from the fourth quarter of 2017 to the fourth quarter of 2019, but it actually grew 9.4 percent—even exceeding the CBO’s post-TCJA forecast from April 2018 of a 9.2 percent increase. Employment grew about 3 percent over the two years fol-


lowing TCJA, roughly tripling CBO's pre-TCJA forecast and matching CBO's post-TCJA forecast. Growth in wages and GDP also exceeded CBO's pre-TCJA forecast, although not to the extent forecast post-TCJA.

While there were certainly other non-tax factors in play—e.g., deregulation may have added to investment and the trade war may have subtracted from investment—tax reform should not be dismissed as a major factor driving the higher performance of the economy after TCJA. Proposals to unwind major pro-growth elements of TCJA, by raising tax rates on corporate and individual income, would push the economy in the other direction, reducing incentives to work, save, and invest, and leading to fewer jobs, lower wages, and a smaller economy than would otherwise exist.

RESPONSE FROM DR. CLAUSING TO QUESTIONS FOR THE RECORD SUBMITTED BY SENATOR WARNOCK

Small Businesses (Dr. Kimberly Clausing)

According to polling done by the Small Business Majority, nearly three-quarters of small businesses say the current tax system favors big businesses over small businesses and that their business is harmed when big corporations use loopholes to avoid taxes. If you're a small business, such as those structured as a pass-through business, I am sure it can sometimes feel like you are swimming upstream.

1. What will it mean for the economy to enact policy that effectively raises the necessary revenue without raising taxes on small businesses?

   For pass-through businesses, no tax increases will occur if the owners are below the $400,000 threshold. Indeed, According to Treasury Department analysis, the President’s Agenda will protect 97 percent of small business owners from income tax rate increases, while delivering tax cuts to more than 3.9 million entrepreneurs.

2. What benefits will small businesses have through the enacted of programs such as providing affordable childcare to working families, funding for workforce training programs, and lower higher education costs?

   The revenue raised from these tax proposals will help pay for investments that will grow our economy and create jobs, including investments in small business. These include investments in clean energy, research, technology, childcare, education, and workforce training. The Build Back Better Agenda will also increase access to contracting opportunities and provide financing and technical assistance programs for small businesses, including small manufacturers.

RESPONSE FROM MS. HUANG TO QUESTIONS FOR THE RECORD SUBMITTED BY SENATOR WARNOCK

Child Tax Credit (Ms. Chye-Ching Huang)

In the past, there has been discussions about the economic impact of corporations, but I think more about hard working Georgians, like the mother I met in Columbus, Georgia. She was laid off recently, but was able to use the money from the Child Tax Credit to pay for books for her little girl. I also think of the constituent who just last week sent me a note about how they've been able to use the credit to pay down debt incurred during the pandemic, afford teaching materials for their children participating in online learning, and told me that this money kept her family in their home and off the streets.

1. What kind of long term benefits to the economy will we see from reducing child poverty by implementing tax cuts, like the Child Tax Credit, that supports working families?

2. What benefits have we seen by having the Child Tax Credit paid monthly in advance to eligible taxpayers, instead of requiring Americans to file their taxes to receive the benefit?

Thank you for your question, Senator Reverend Warnock.

The experiences of these Georgian families are not unusual, which is why the CTC is so important for families and communities across the country.
Monthly distribution of the Child Tax Credit has made it easier for families to pay for recurring expenses throughout the year. Research shows that parents with low incomes have, like your constituents, spent their monthly CTC on basic needs like food, rent, utilities, clothing, or school supplies—and shortly after the first monthly check was distributed, food insecurity and financial hardship fell dramatically among households with children.

The monthly CTC has not only helped families make ends meet in the short-term, but a large body of research suggests that it is a true investment: it will also have positive effects on the life trajectories of children in the long run, and for the economy as a whole.

Investments in families with low incomes have been shown to improve infant and child health, improve children's academic performance in schools, increase the likelihood that children attend college, and boost earnings once children ultimately reach adulthood.

These long-term benefits for children and families can also mean broadly shared benefits for communities and the larger economy. They mean that children are more likely to be healthier as adults, attend college and have higher adult earnings. Boosting the health and earnings of the next generation also in turn reduces spending on health care costs and other macroeconomic costs associated with high child poverty rates over time.

Further, novel research suggests that investments in children from low- and moderate-income families can help more children develop and apply their talents for innovation. If equally talented girls, children of color, and children from low- and middle-income families grew up to be inventors at the same rate as white boys from rich families, there would be four times as many inventors in America as there are today. The research suggests that a key reason why this potential is being lost is simply because many families lack basic financial resources. Sound investments in these families can ensure more children are able to be a part of the next generation of innovators who may generate new breakthroughs and businesses with widely shared benefits.

RESPONSE FROM DR. EDELBERG TO QUESTIONS FOR THE RECORD SUBMITTED BY SENATOR WARNOCK

RACIAL WEALTH GAP

In 2019, the median net worth for all American families was about $121,000 while the median net worth of Black families was about $24,000.

1. What can a strong social insurance system, like those in the Build Back Better plan, do to address historical inequities in our economy?

2. What do you believe their long-term effect will have on our economy?

Improvements in the social insurance system can help to address historical inequalities in household resources, including wealth, which act to cushion families against financial setbacks, enable individuals to take risks, and provide people with...
access to better neighborhoods. The racial wealth gap is the product of exclusionary and discriminatory practices dating back to the foundation of this country. As a result, the median Black household was left far more vulnerable to the devastating economic effects of the COVID–19 pandemic.

Piling onto an already precarious situation for Black Americans, Black workers and Black owned businesses were disproportionately likely to be in the industries hardest hit by the pandemic [1]. As the economy recovers, a hot labor market will begin to close the racial and ethnic unemployment gap, but will not be enough to eliminate it [2]. Moreover, closing the unemployment gap does not close the racial wealth gap [1]. In fact, the racial wealth gap is observable even among households with similar incomes and at all levels of income, except for the bottom quintile in which median net worth is universally zero [3].

A stronger social insurance system can alleviate the harsh impact of recessions by bolstering household savings, reducing poverty and food insecurity, and guaranteeing access to preschool programs. Black households have less in emergency savings than white households, with $1,500 in liquid assets in 2019 as compared to $8,100 among white households [4]. Such disparities in financial resources would be mitigated by making the full refundability of the Child Tax Credit (CTC) permanent [5]. Notably, the expansions to the CTC in 2021 will help cut child poverty by more than 45 percent among all households, and more than 52 percent among Black households [6]. In addition, an improvement in access to childcare would lower the cost of working for parents of young children and, particularly, increase labor force participation among women [7]. An improved social insurance system would do more to curb the severity of economic crises and hasten recoveries, though it does not fundamentally address the racial wealth gap.

As articulated in The Hamilton Project blog on this subject, as published in December 2020:

“Indeed, closing the Black-white wealth gap will require that the deep and systemic economic disparities brought about by centuries of discriminatory policies are addressed through significant structural changes across a range of policy areas. As discussed in a previous Hamilton Project analysis, these policies range from redlining and the denial of financial services to minority communities, to the Jim Crow Era’s “Black Codes” strictly limiting opportunities in many southern states—all of which contributed to the disproportionate accumulation of wealth held by white households while exacerbating the economic fragility of many Black households. Overcoming the effects of these policies will necessitate substantive and systemic changes in education, small business, healthcare, broadband access, tax reform, and broader place-based policies.

The COVID–19 pandemic underscores the importance of the Black-White wealth gap and its impact on the ability of households to weather the economic shocks caused by recessions. By expanding policymakers’ focus not only on strengthening the safety net and income supports, but also on the inclusion of systemic and structural public policy changes across a range of areas to close the Black-White wealth gap, disparities in the ability of Black and White households to weather the next economic storm will be greatly reduced” [2].

References