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CREATING OPPORTUNITY THROUGH
A FAIRER TAX SYSTEM

TUESDAY, APRIL 27, 2021

U.S. Senate,
Subcommittee on Fiscal Responsibility
and Economic Growth,
Committee on Finance,
Washington, DC.

The hearing was convened, pursuant to notice, at 12:30 p.m., via Webex, in Room SD–215, Dirksen Senate Office Building, Hon. Elizabeth Warren (chair of the subcommittee) presiding.

Present: Senators Cassidy, Wyden, and Carper.

Also present: Democratic staff: Gabrielle Élul, Economic Policy Advisor for Senator Warren; Michael Evans, Deputy Staff Director and Chief Counsel; and Laura Gerrard, Scheduler for Senator Warren. Republican staff: Katie Hadji, Tax Counsel for Senator Cassidy; Owen Morgan, Policy Advisor for Senator Cassidy; and Jeffrey Wrase, Deputy Staff Director and Chief Economist.

OPENING STATEMENT OF HON. ELIZABETH WARREN, A U.S. SENATOR FROM MASSACHUSETTS, CHAIR, SUBCOMMITTEE ON FISCAL RESPONSIBILITY AND ECONOMIC GROWTH, COMMITTEE ON FINANCE

Senator WARREN. This hearing will come to order. Good afternoon. Welcome to this year’s first hearing of the Finance Committee’s Subcommittee on Fiscal Responsibility and Economic Growth.

I want to thank our ranking member, Senator Cassidy, for working with me and my team to make this hearing successful. We have a vote today at 2:30, so Senator Cassidy is voting at the top of the hour. He will come back, and he’ll take the gavel so I can vote.

This is a subcommittee that will focus on how we can create opportunities for every American, how we can build a more equitable economy, and how we can invest in future prosperity. President Biden has proposed a $2-trillion infrastructure package, outlining the benefits of investing in roads and bridges and broadband and housing, the things people need to get to work. He’s also about to unveil a plan for the care-giving economy, including child care, universal pre-K, and free community college. Current estimates put the price tag of that package at about $1.5 trillion.

All these investments would make the lives of millions of people better, but they carry a total price tag of about $3.5 trillion. So how do you pay for it? Today we will address that question by talking about revenues—where the money comes from to build a stronger future. There are a variety of proposals that would help us move
toward that stronger future, and I am going to highlight just three that I have put forward.

First, a wealth tax would impose an annual 2-cent tax on fortunes bigger than $50 million. It would not raise taxes on 99.9 percent of Americans by a single penny. That one tax would bring in $3 trillion.

Second, the Real Corporate Profits Tax would force companies like Amazon, FedEx, and Nike that make billions of dollars in profits and pay little or nothing in Federal income taxes, to pay more. The Real Corporate Profits Tax would apply only to corporations that report profits to their shareholders and the public of more than $100 million. These companies would pay 7 percent of those reported profits, which they use to justify the big salaries and bonuses that they pay their CEOs, and they would pay that no matter how many tax loopholes they find or how many scams they run. President Biden has a similar approach. My approach would raise about $1.3 trillion.

And then finally, I have proposed increasing tax enforcement for wealthy individuals and giant corporations. This plan provides mandatory funding for the IRS that is focused on making sure that the rich and powerful get caught when they break the law. Estimates from the Commissioner of the IRS indicated that we lose about a trillion dollars a year from tax cheating. If we stepped up enforcement to cut the cheating by only 20 percent, we could raise as much as $1.8 trillion over the next decade.

These three big ideas alone would raise more than $6 trillion, enough to pay every single penny of President Biden’s American Jobs Plan, and pay for every single penny of his American Families Plan, and still have more than $2 trillion left over.

As these numbers show, our Nation can do both—invest in American families, and pay for it without raising taxes on those same families. We can build a country that creates opportunity, not just for those at the top, but creates opportunities for everyone.

Now these big ideas have their critics. In fact, I invited one of the loudest critics, billionaire Leon Cooperman, here today to discuss these proposals with the members of the committee and the American public. After all, that is how democracy is supposed to work: citizens and stakeholders discuss ideas, and then our elected representative’s vote.

I am disappointed that Mr. Cooperman decided that he was more comfortable taking softball questions on cable news than subjecting his views to debate in the United States Senate. Now Mr. Cooperman may have been too frightened to come here today, but others were not.

Today we are joined by a panel of distinguished witnesses, including several academics and tax policy experts, by millionaire Abigail Disney, and by small business owner Cheryl Straughter, who have a variety of views on these proposals and are willing to discuss and debate them in public. A fairer tax system is about making our country better and stronger. It is about allowing us to make investments in our economy by asking the wealthiest Americans and biggest corporations to pay their fair share.

So I am looking forward to this discussion today, and I thank our witnesses and my colleagues for joining us. I would at this point
ordinarily turn to Ranking Member Senator Cassidy for his opening remarks, but I think he is still voting. As soon as he rejoins us, he can give us those remarks.

[The prepared statement of Senator Warren appears in the appendix.]

In the meantime, I am going to go ahead and introduce our witnesses. First, I am very pleased to introduce Dr. Abigail Disney, who is the CEO and the owner of Fork Films. Next is Ms. Cheryl Straughter, who is the chef and the owner of Soleil Restaurant in Boston, MA. Next, Mr. David Gamage, professor of law at Indiana University Bloomington’s Maurer School of Law. Then, Mr. Scott Hodge, president of the Tax Foundation. Dr. Jeff Hoopes, associate professor at the University of North Carolina Chapel Hill’s Kenan Flagler School of Business. And finally, Mr. Kyle Pomerleau, a resident fellow at the American Enterprise Institute.

I want to thank every one of our witnesses for joining us today. And, Dr. Disney, I would like to recognize you for 5 minutes, please.

STATEMENT OF ABIGAIL E. DISNEY, Ph.D.,
CEO AND CO-FOUNDER, FORK FILMS, NEW YORK, NY

Dr. Disney. Thank you, Chair Warren and Ranking Member Cassidy, for the opportunity to speak today.

When a person is born in this country, it pretty much goes the same way every time. When a baby comes out, it gets a little slap on the tushy till it cries, and gets handed over to the parent.

But in a family like mine, it goes a little bit differently. The baby comes out. It gets slapped on the tushy a little bit. And then the doctor looks deep in that baby’s eyes and says, “Never spend capital.” It is as close to a religion among people who inherit wealth as anything else.

So why is capital so sacred? Well, it is the goose that lays the golden eggs. The more capital you have, the more income and growth you can count on, the more stuff you can buy, and so forth.

The subtext of “never spend capital” is of course that jobs are for chumps. If you ever find yourself reduced to earning your living by labor, well then, you have surely lost the lottery that you were given when you were born. That is how rich people stay rich.

I was born very lucky, and continue to be very lucky today. But a lot of things have changed since I was born in 1960, and a lot of it has been very good for me financially. For one thing, Disney stock has soared, in part because of good management, and in part because the stock market has soared.

So I have owned my way to the top. But there is another thing that is more pertinent for our purposes today, and that is that a lot of what the government has done for the last 40 years has been to shape policies that fight against the natural forces that would normally pull an inheritor like me back down to earth. Things like low corporate taxes and a high tolerance of tax avoidance—those savings go to executives and to shareholders like me. Companies plowing their skyrocketing profits and tax savings into share buybacks help only, yes, shareholders like me and executives.

A tax avoidance industry has been growing up that has been advising individuals and families like me about how to minimize
their tax obligation in ways that are both quasi-legal and even potentially criminal, an assault on public spending that included the evisceration of the IRS, the SEC, and all the other regulators that might be more able, if better supported, to restrain some of the trickery.

And finally, corporate and individual spending on lobbying and on political campaigns has warped and changed the political processes, rendering some representatives opaque, corrupt, and downright uninterested in the well-being of regular people.

When I was born in 1960, the U.S. had a tax system that privileged income from labor over income from wealth. But somewhere along the line, that turned upside down. Now, the more likely a person is to come home with an aching back and sweat on their brow, the more likely I am to be paying a lower effective tax rate than they are.

If a tax system is a statement of a country’s values, then I really do question ours. The levels of inequality that now characterize American life are historic. And the pandemic has only exacerbated the problems. Wealth among U.S. billionaires has grown by over $1.3 trillion just over the past year.

That kind of money would cover a $3,900 stimulus check for every American citizen. The rich may have run amok. They have run amok for the last 50 years of American history, and our government’s complicity in their antics has permitted a handful of egregiously wealthy human beings to accumulate massive, budget-warping, mind-blowing amounts of money, all at the continuing expense of all the other Americans.

We need to address this inequality by restoring to the working class the benefits that used to come with just being a regular American citizen. But working people will never, by salary alone, be able to catch up with the folks who have succeeded in putting so much distance between themselves and everyone else. Only a wealth tax will get us there.

I will go to bat for the wealth tax against any and all businessmen who want to tell you that it impinges on the American Dream. If you have $50 million and you cannot invest it for more than 2-percent growth, well then, you have a bigger problem than the wealth tax.

And if you have a billion dollars, and you do not know how to live on $999 million, then you do not need a better tax system; you need a psychiatrist. A tax is not a penalty. A tax is not a theft. A tax is a responsibility. It represents what you owe to society. A tax is the least you can do. It is your patriotic duty.

Thank you, very much.

[The prepared statement of Dr. Disney appears in the appendix.]

Senator WARREN. Thank you, Dr. Disney. And now I call on Ranking Member Cassidy, who’s going to give his opening statement. I am also turning the gavel over to him while I go to vote.

OPENING STATEMENT OF HON. BILL CASSIDY, A U.S. SENATOR FROM LOUISIANA

Senator CASSIDY [presiding]. Thank you, Madam Chair. Thank you, Chairman Wyden, again Subcommittee Chair Warren, and
Ranking Member Crapo. And I thank my witnesses, whom we will be hearing from.

First, let’s acknowledge that conservatives and liberals both want what is best for our country. Sometimes we have this spirit of division that suggests that is not true, one for the other. We all wish to have prosperity for those who are doing less well, but as this hearing will show, we have different visions on how to achieve that goal.

Conservatives believe in allowing the American people to keep their resources as much as possible, to make decisions best for them. Allowing markets to dictate—with safeguards from Federal and State governments—as to where money should be best allocated, that is what has given us prosperity to date, and I feel, and conservatives feel, more likely to give us prosperity in the future.

Now it is not just we who have seen that, however. We have seen countries which are socialist or communist acknowledge this and evolve toward that path. Whether it is the Czech Republic, or China, or countries that have tried wealth taxes like that which we discuss today—Sweden, Austria, Denmark, Germany, the Netherlands, Finland, Iceland, Luxembourg—they all have abandoned it.

I think it is fair to say, and this hearing will show, that the left has a different view. The view is that it is better to take resources from the American people, filter them through the government bureaucracy, allow that bureaucracy to make decisions as to where to spend, and then the American people will more greatly benefit from these government decisions, as opposed to those made by private investors.

That is really not what has given us prosperity to date. And again, that is what many countries have abandoned. Now there are those on the left who will object, quote, “Hold on a second. We’re not talking about taxes on anybody but the most wealthy.” But this is disingenuous, a disregard that even the revenue from taxing every billionaire in the country at 100 percent would not come close to funding the programs that have been proposed so far.

It is also disingenuous because it presupposes that those whom the left wishes to tax are sitting on a pile of gold, like the dragon in “Lord of the Rings,” not using it in order to invest, in order to create wealth for others, but no, just sitting there.

As Dr. Disney said, if you have got a billion dollars, if you cannot live on $999 million, then maybe you need to see somebody. But they are not living on $999 million. They are reinvesting it. And I would argue that that wealth is typically not liquid; that it is invested and reinvested, creating jobs and wealth. And the people who do this successfully create more jobs than will the government bureaucrats who would just not, frankly, feel as invested. It is not his money or her money, as opposed to the entrepreneur—it is their money, and they are going to do what brings the best return and, along the way, bring return for others.

Our first Supreme Court Justice John Marshall said, “The power to tax involves the power to destroy.” We are not reinventing the wheel here. When you decrease taxes, you encourage investment, and jobs follow. When you increase taxes and you increase government control, you destroy investment, and job numbers suffer.
Now again, we have some case studies here. Before COVID, Republican-led tax cuts spurred the greatest economy of our lifetime; record low unemployment for every demographic—the disabled, the high school dropouts, for African Americans, for women, for veterans, you name it—record low unemployment, record high employment driven by investments in the private sector.

We have wage growth disproportionately in the lower-income strata. Now this may be an inconvenient truth for some on the other side of the aisle, but it is truth nonetheless. We know what works.

In fact, let’s have a thought experiment. Let’s contrast the logical outcome of the two visions of the two sides. Those who like to raise taxes on the wealthy—it is kind of a principle—would like us think that the disinterested bureaucrat is able to make a wiser decision as to where to deploy capital than the person whose livelihood depends upon it.

In the private sector, if an organization providing these services fails, it is on the dime of the company. Someone else steps up, takes the position to increase productivity, to increase jobs and wages. That is what happens in the private sector, and this is what this hearing is about.

But we have a contrasting vision. Think school teachers’ unions in Chicago. Children not allowed to be in a class because a teacher’s union, against recommendations of the CDC, against science, against their Mayor’s wishes, still would not reopen. What did they get for that failure of service? They demanded and received billions and billions for union priorities, paid for by U.S. tax dollars which, I guess from this tax, have come from the wealthy who would otherwise use the money to invest in the private sector to increase jobs.

I would argue that the vision of creating jobs for all, as opposed to rewarding the inactivity of some who are politically connected, is part of what underlies this conversation.

Now, by the way, rather than talking about whether new taxes are actually needed, we actually will hear how they are justified: successful individuals used as strawmen pitting Americans against each other to build support for a political agenda. Success will be vilified. Undefined goals like “fairness” will be used as blank checks to justify a tax and spend agenda.

But what do you tell a family who loses their job because new taxes on the rich corporations make their employer’s business model no longer viable? “It is okay to lose your job because we really stuck it to the rich.”

The rich will do fine. The rich are going to do fine. Again, as I said earlier, they will find some way to live on quite a comfortable lifestyle. My fear is for the everyday working person caught in the crossfire of taxing priority which destroys the private investment capital and incentive that made their job possible in the first place.

By the way, some will say, “Don’t worry, we are going to expand transfer payments and take care of this fallout. We will have expanded transfer payments.” I would argue that this obviously creates government dependency, but I would argue that Americans want independence not dependence.
So I will just say, I think we are going to hear a fundamental difference between our two parties. The Republicans believe that the best stimulus is a paycheck. And a job is better than a transfer payment to support your family. By the way, statistics bear that out as well.

I will come close to finishing by saying that a wealth tax is opposed by John Cochrane of the Hoover Institute, I guess on the right; the former Treasury Secretary Larry Summers on the left. It is also opposed by the AEI, the Tax Foundation, Brookings, and the Manhattan Institute, which have all reported on the negative aspects.

So I hope the Biden administration will work with Republicans to get small businesses back on their feet so they can get Americans back to work earning better wages to keep the economy moving in the right direction. We will not tax our way to prosperity. Small businesses and other employers wish to operate under a fair, predictable tax code. They will do the rest.

There are some good things we could be discussing here. Tax relief afforded to the middle class and small businesses through the Tax Cuts and Jobs Act expires in just 4 short years. My Republican colleagues and I propose providing predictability to taxpayers by locking in the current individual tax policies on a permanent basis, including the expanded Child Tax Credit and lower tax rates on the middle class. This will help everyday Americans.

I look forward to the testimony, and now I call upon Mr. Straughter. You are recognized for 5 minutes.

[The prepared statement of Senator Cassidy appears in the appendix.]

STATEMENT OF CHERYL STRAUGHTER, OWNER, SOLEIL RESTAURANT, BOSTON, MA

Ms. Straughter. Hi. Are you referencing Ms. Cheryl Straughter?

Senator Cassidy. Yes; if I mispronounced something, I apologize. I did not have my glasses on [laughing].

Ms. Straughter. Here we go. To our distinguished chair and Ranking Member Cassidy, I want to say “thank you” for this opportunity. To members of the committee, I want to thank you all for allowing me to testify.

I am not a billionaire, or an ultra-millionaire; I am not even close. During my life, there have been times when I worried about my status as a thousandaire. I am a chef and owner of Soleil Restaurant, a small business located in Boston, MA. I am also a social worker and a member of the Boston Black Hospitality Coalition.

I opened my restaurant in 2018 in an area of Boston called Nubian Square. This was a thriving commercial district when I was younger, and I fondly remember shopping with my mother, Shirley, and boarding the elevated train that once operated all the way downtown.

Over the years, disinvestment in the community led businesses and families to leave. But when an opportunity arose to take over a vacant space in the neighborhood, I knew that I wanted to be a part of the future of Nubian Square. I am proud to run this small business. Along the way to my current role, I have been an em-
ployee, I have been a student, and a care giver. I work hard for myself, my family, and my employees in my community, and I care deeply about all of their well-being.

That is why it is important that we have a fair tax system. I can’t say that I enjoy paying taxes, but I am proud to pay them. The revenue collected from our taxes is what we use to pay for government services. We care about schools, health care, Social Security. I value those services, and I know they make my community and our Nation better.

But the unfairness of the current tax system is what drives people crazy. At Soleil, I have eight employees who work for me. Their income is reported to the IRS, and they pay their taxes based on that income, including paying a percentage of their income for Social Security and Medicare. But I know the ultra-rich are different.

Their income does not usually come from a paycheck. It comes from investment and other holdings. That means they often pay less in taxes than my own employees. And I know the ultra-rich have a bunch of ways to hide their income or avoid paying taxes at all. That is unfair.

Asking ultra-millionaires and billionaires to pay a small percentage of their massive wealth is a no-brainer. If you have a huge fortune and you benefit from all that this country has provided, you ought to be paying your fair share. It is more than fair that they be asked to pay a small percentage of their wealth, and I just cannot understand why the wealthiest and luckiest people in the world would be complaining about it being such a hardship.

It is the same with big businesses that I compete with. They are able to use their resources to lower the amount of taxes that they pay, like hiring expensive lawyers and accountants, or shifting some of their profits overseas. Many Fortune 500 companies do not pay any taxes at all. It is hard enough to compete and run a business during a pandemic; it is nearly impossible to do that when the tax system is rigged against you.

Our country has many needs right now. A fairer tax system would give us the opportunity to provide affordable child care, create a better education system, and repair our roads. We could provide more support to small businesses—especially those owned by African Americans and other groups that do not have easy access to financing—and make housing more affordable.

These are important national priorities, and they are also things that I want for my family. I know these investments will make our communities better and stronger, and help our economy grow. That would be good for me and for my employees, be good for my customers, and good for my business and businesses all over the country.

I am happy to answer any of your questions. Thank you for inviting me to today’s hearing, and thank you for all of the work to make our tax system fairer and our Nation stronger.

[The prepared statement of Ms. Straughter appears in the appendix.]

Senator WARREN. Thank you so much, Ms. Straughter. I appreciate it.

Mr. Gamage, you are recognized for 5 minutes.
STATEMENT OF DAVID GAMAGE, PROFESSOR OF LAW, MAU- 
RER SCHOOL OF LAW, INDIANA UNIVERSITY, BLOOMING- 
TON, IN

Mr. GAMAGE. Thank you, Chair Warren. Thank you, Ranking 
Member Cassidy, members of the committee, for your invitation to 
speak with you today.

I have been asked to speak on three sets of proposals for reform- 
ing ways in which our tax system is currently written. Each of 
these proposals has the potential for reforming ways in which our 
tax system is broken by limiting abusive tax gaming by billionaires 
and mega-millionaires and by large corporations.

Each of these proposals would help create opportunities for ordi- 
nary Americans and small businesses by leveling the playing field. 
Each of these proposals could help promote shared economic 
growth by limiting abusive forms of tax gaming that are harmful 
to the economy and by funding needed public investment.

First, the IRS has been starved of funding and resources for over 
da decade now, which has caused incredible harm to our tax system. 
The ultra-wealthy and largest businesses now readily hire tax law- 
yers who often charge up to $1,000 an hour to set up complicated 
structures for avoiding tax.

The IRS is simply outgunned in trying to police these abuses. It 
is common today for the ultra-wealthy and the largest businesses 
to wastefully spend millions on tax planning because this saves 
them tens or hundreds of millions of dollars in taxes.

Prior Congresses have created this disgrace by hobbling the IRS. 
I urge this Congress to act quickly to restore adequate funding to 
the IRS and to the other tax police, to protect that funding from 
the winds of the annual appropriations process, and to enact ac- 
companying reforms for promoting tax compliance, like expanding 
information reporting and by extending the False Claims Act to 
very large tax claims.

Second, current law allows large corporations to keep two sets of 
accounting books: one for reporting to the SEC and investors, the 
other for reporting to the IRS for tax. It is well known that cor- 
porations generally inflate the earnings reported on this first set of 
books to appear more profitable to investors, and in particular to 
increase managers' stock options. It is also well known that cor- 
porations generally under-report earnings on the second set of 
books through tax gaming to appear less profitable to the IRS so 
they can pay less taxes.

Both of these sets of shenanigans are harmful to the economy 
and to creating a level playing field. To address these problems, the 
best academic analysis of this issue recommends 50-percent con- 
formity between tax and accounting books. We currently have zero 
percent. The Real Corporate Profits Tax proposal would be an im- 
portant step in improving this, effectively creating 25-percent tax 
conformity, deterring both tax and accounting shenanigans and 
raising funds needed for public investment.

This would be a meaningful step toward fixing our broken cor- 
porate tax system so as to help level the playing field, deter econo- 
mically harmful tax and accounting shenanigans, all while rais- 
ing funds to use for public investment.
Third, and most importantly, I cannot emphasize enough how our existing income tax is broken, as applied to mega-millionaires and billionaires, and urgently in need of reform. The ordinary rich, like the well-compensated doctor, typically pay quite a lot of income tax. But the progressivity of the income tax falls apart when it comes to billionaires and mega-millionaires. The economic literature finds that, on average, billionaires and mega-millionaires only ever report less than a quarter of their true income to the IRS, ever. And what is eventually reported then qualifies for tax preferences and preferred rates. Estimates of some billionaires often find that these billionaires only report around 2 percent of their true income to the IRS.

The income tax is generally progressive with respect to the ordinary rich, but not the ultra-wealthy. If anyone tells you otherwise, based on IRS data, remember that the ultra-wealthy never report most of their true income to the IRS. Most of the ultra-wealthy tax scheming is legal, but very harmful. This tax scheming damages the economy and prevents ordinary Americans and small businesses, especially members of historically disadvantaged groups, from being able to catch up.

Fixing the income tax system is hard, but urgently needed. One of the best ways to fix the income tax is by taxing extreme wealth holdings of billionaires and mega-millionaires directly as the proposed ultra-millionaire wealth tax would do.

When it comes to taxing heirs of giant fortunes, it is much easier to identify and measure the approximate size of those fortunes than just the income produced by those fortunes. Enacting a tax on extreme wealth holdings would take pressure off the income tax, while providing the IRS with the information on giant fortunes needed to make the income tax and the overall tax assessments work with respect to the ultra-wealthy.

A wealth tax has been a pillar of the Swiss tax system for over 100 years, and provides substantial revenues for Switzerland. The Swiss model shows how we can design an effective and administrable tax on extreme wealth. Plus, recent innovations in information technology and financial reporting make it much easier to design an administrable and effective wealth tax than it was in the past.

Giant fortunes benefit from the protection and services provided by the States, including the military and police and the legal system. Billionaires and mega-millionaires should not be permitted to pay a lower share of tax on their true incomes than do ordinary working-class Americans, as is currently generally the case.

All three sets of reforms I have spoken on today would help fix broken parts of our tax system; would help level the playing field for ordinary Americans, small businesses, and members of historically disadvantaged groups; and would promote shared economic growth by deterring economically harmful tax scheming and providing the funds to use for public investment.

I strongly support all three sets of proposals, and I look forward to your questions.

[The prepared statement of Mr. Gamage appears in the appendix.]

Senator WARREN. Thank you very much, Mr. Gamage.
Mr. Hodge, you are now recognized for 5 minutes.

STATEMENT OF SCOTT A. HODGE, PRESIDENT, TAX FOUNDATION, WASHINGTON, DC

Mr. HODGE. Thank you, Chair Warren, Ranking Member Cassidy, and members of the committee. I appreciate the opportunity to be with you today.

A famous economist once said, “There are no solutions, there are only trade-offs.” And that lesson is especially true in tax policies, and in the choices that lawmakers must make in funding public investments.

The scales of justice may have two trays, but tax policy has three trays: revenues, equity, and economic growth. But those factors cannot be balanced equally, so lawmakers must decide which is most important.

Empirical evidence tells us that there is a clear tradeoff between progressivity and economic growth. And this is especially true with so-called “success taxes” like taxes on capital and business income.

Understanding these dynamics matters in how you fund government investment. Research by the Congressional Budget Office tells us that government investments deliver only half of the economic returns of private-sector investments. Private-sector investments, according to CBO, return 10 percent on the dollar, whereas government investments return just 5 percent.

So, considering the opportunity costs that come with government spending, lawmakers must be careful in choosing offsets that do not do more harm to the economy than the modest benefits generated by those public investments.

Indeed, the U.S. tax system is already one of the most progressive tax and redistributive systems in any industrialized country. So making the tax code even more progressive through proposals such as the wealth tax, a minimum tax on book income, or an increase in the corporate tax rate, are among the most economically damaging options that can be used to fund government programs.

For example, the Tax Foundation in our General Equilibrium Model, found that Senator Warren’s wealth tax could raise over $2 trillion over a decade, but at a pretty high economic cost. The model found that the wealth tax’s hit to GDP was greater than the effects of raising the corporate tax rate to 28 percent, and 4 times greater than the economic effect of a $25 per ton carbon tax. More importantly, the model determined that the taxes would result in a shift in the ownership of U.S. assets, as wealthy taxpayers sold off their assets to pay the tax.

But because the U.S. is an open economy, the model shows that foreign investors would come in and buy up those assets at a discount. So what the wealth tax would do is lead to a transfer of wealth from rich Americans to rich foreigners, which would put those assets out of reach of the wealth tax.

Similarly, our modeling of the minimum book tax found that it would reduce the size of the economy by 1.9 percent, lower the capital stock by over 3 percent, trim wages by 1½ percent, and cost the economy over 450,000 jobs. And while those at the top of the income scale would see the largest declines in after-tax income, taxpayers in every income group would see their income fall as a
result. The economic effects of the President’s book tax proposal are not quite as severe as Senator Warren’s, but the biggest effect of both is the complexity they add to the tax code, and the fact that they out-source key aspects of the tax system to the unelected decision-makers of the Financial Accounting Standards Board.

Turning now to the issue of raising the corporate income tax, economists at the OECD determined that the corporate income tax is the most harmful tax for economic growth, because capital is the most mobile factor in the economy and thus the most sensitive to this high tax rate.

But an even more important factor to consider is that academic research is finding that workers are bearing a greater share of the economic burden of the corporate tax through lower wages, because capital is mobile, and workers are not. A recent study found that workers bear 51 percent of the economic burden of the corporate tax through lower wages, with women, low-skilled workers, and younger workers impacted the most. These are the workers who have been most hurt by the COVID recession, and the ones whose incomes were rising most before COVID hit.

Well, in closing, you know, it may be kind of a cliché, but there is no such thing as a free lunch in government spending, or in tax policy. Inevitably, progressive tax policies will slow the economy and reduce the living standards of the very people that the new government investments are intended to help, leaving taxpayers and the economy worse off.

Thank you very much, Chair, and I am happy to answer any questions that you might have.

[The prepared statement of Mr. Hodge appears in the appendix.]

Senator WARREN. Thank you very much, Mr. Hodge.

Dr. Hoopes, you are now recognized for 5 minutes.

STATEMENT OF JEFFREY L. HOOPES, Ph.D., ASSOCIATE PROFESSOR, KENAN FLAGLER BUSINESS SCHOOL, UNIVERSITY OF NORTH CAROLINA, CHAPEL HILL, NC

Dr. Hoopes. Thank you, Chair Warren. Chair Warren, Ranking Member Cassidy, distinguished members, I appreciate the opportunity to participate in this hearing today.

My testimony today will focus on perceptions of fairness in the tax code and proposals to fix them, specifically, a tax on book income and the wealth tax. My main message is that corporations and individuals often remit the taxes they do, including in situations some perceive as unfair, generally because of explicit allowances in the tax code. We wish to revise the tax code in ways that make it simpler, rather than layer on other provisions that will make it more complicated, costlier to administer, and have negative consequences. Taxing the book income and a wealth tax are two examples of such inadvisable taxes.

Perceptions of unfairness in corporate tax payments sometimes occur when corporations are seen as reporting different incomes to their shareholders than with the IRS. These perceptions ignore the purpose of the different accounting systems corporations are subject to. In general, when tax and book numbers are not aligned, it is because Congress has made the law such that the two numbers
are different. We provide three examples based on public IRS data from 2017.

In 2017, the difference between book income and taxable income as a result of depreciation, the allowance for net operating losses, and the general business tax credit which includes the R&D tax credit, accounted for $138 billion in lost tax revenue. Considering the total corporate tax receipts of $388 billion, the $138 billion is economically very large.

This lost revenue is the result of explicit allowances in the Internal Revenue Code made by Congress, and not aggressive tax planning by firms. All three of these items are generally accepted by tax experts as acceptable, are tax provisions shared by many other countries, and research suggests they are useful in accomplishing the goals for which Congress enacted them. Let’s compare those three items to estimates of the cost of corporate income shifting, one of the more common forms of tax planning.

One estimate of income shifting suggests that between 4 and 8 percent of tax revenues are lost through profit shifting, which in 2017 would amount to between $16 billion and $31 billion. The most extreme estimate is that $100 billion was lost in 2017.

Similarly, the most recent estimates of the losses due to illegal income tax evasion by all corporations from the IRS suggests losses of about $32 billion. There is reason to believe that in a post-tax-reform world, these estimates are over-stated. Even so, they are still only a fraction of the cost of just the three tax provisions I mentioned above.

Owing to the perception that corporations do not pay a fair amount of tax, there are proposals to tax financial accounting or book income. We should not tax book income. First, including book income in the tax base would distort book income and make stock markets less efficient as companies would manage their earnings to pay less in tax.

Evidence from a 1986 tax change suggests this previously happened. And we have reason to believe it would happen again if we again tax book income.

Second, taxing book income would politicize the Financial Accounting Standards Board, the creators of U.S. GAAP, making earnings less reliable. Taxing book income is a Band-Aid solution that would create more problems than it solves.

There is also a common perception that wealthy people do not pay a sufficient amount in tax. One proposed solution for this problem is a wealth tax. Wealth taxes rely on the wealthy disclosing and valuing their assets annually. Recent research by Guyton et al., 2021, finds that some of the wealthy are very adept at hiding their assets from even the most thorough IRS audit, suggesting uncovering these assets would be costly.

I would expect much more of this type of asset concealment if a wealth tax were implemented. Further, once uncovered, valuing these assets would also be very costly. Private companies can be very difficult to value. The cost of administration and enforcement of a wealth tax would not justify the revenue a wealth tax could raise.

These costs are one reason a dozen EU countries have tried the wealth tax, and few of these taxes persist. My main message is
that many of the ways in which large corporations and wealthy taxpayers remit taxes at a level the general public may perceive as unfair are frequently legal methods, intentionally legislated by Congress. Certainly some illegal tax evasion occurs. Congress should take action to stem these evasions, including by increasing funding to the IRS.

But the best estimates of this evasion suggest that the dollars at stake are much less than the explicitly legal means taxpayers take to reduce their tax liabilities. Members of Congress perceive the tax system as unfair and seek to raise additional revenues in order to expand the size and scope of government. They should fix whatever provisions they deem unfair and not implement additional taxes that are difficult and costly to administer and would have adverse consequences.

I look forward to answering your questions. Thank you.

[The prepared statement of Dr. Hoopes appears in the appendix.]

Senator WARREN. Thank you, Doctor Hoopes.

And finally, Mr. Pomerleau, you are recognized for 5 minutes.

STATEMENT OF KYLE POMERLEAU, RESIDENT FELLOW, AMERICAN ENTERPRISE INSTITUTE, WASHINGTON, DC

Mr. POMERLEAU. Thank you, Chair Warren, Ranking Member Cassidy; thank you for the opportunity to speak today.

In my testimony, I will briefly discuss two policies under consideration: the first, taxing the book income of corporations; and the second, an annual tax on wealth. I will then conclude by discussing alternative sources of revenue that I think lawmakers should at least consider.

There are currently two proposals to tax book income of corporations, and I think that they are distinct. First is President Biden's proposal for a 15-percent minimum tax on book income. And the second is Senator Warren's proposal for a 7-percent add-on book income tax that would be paid each year.

Both of these proposals are driven by a perception that profitable corporations that report low or no tax liability are engaged in aggressive tax avoidance. There is no doubt corporations try to minimize their tax liability, but as has been argued already, taxing book income would not necessarily address tax avoidance.

Low effective tax rates relative to book income are often driven by differences in how book and taxable income are calculated. And what are called these “book tax gaps” arise from differences in how book and taxable income deals with things like capital expenses, executive compensation, the treatment of losses, and the treatment of foreign income earned by U.S. multinational corporations.

And rather than addressing tax avoidance, taxing book income may result in corporations adjusting book income to avoid taxation, which could reduce the informational quality of book income. And at the same time, taxing book income may undermine Congress's own policy goals in other places.

Congress frequently uses the Federal income tax to encourage or discourage certain behaviors. For example, Congress has limited the deductibility of executive compensation since the 1990s. However, for book tax purposes, executive compensation would be fully
deductible, which would reverse some of that policy change that Congress deemed appropriate.

And lastly, for the book tax, it would also likely influence investment incentives. Now these incentives will depend greatly on the structure of the tax, whether it is a minimum tax or a parallel tax, but one of the biggest changes it would make is with the treatment of accelerated depreciation and expensing, which are important parts of the corporate tax base that limit the distortion of corporate tax on the domestic economy.

In addition to the book tax, some lawmakers are also proposing an annual tax on the wealth of very high net worth households. While some argue an annual wealth tax is a modest tax, it actually would place a significant burden on savings. For an example here, an annual wealth tax, even what seems to be a low rate, say 2 percent, would reduce an asset that earns a return of 3 percent by 67 percent. In other words, it would be equivalent to a 67-percent income tax.

As Mr. Hodge mentioned, this would have an impact on the broader economy, reducing the after-tax return on savings; would reduce the stock of national savings; could lead to a smaller capital stock, lower wages for workers, and lower economic output; and due to the openness of the U.S. economy, would result in an inflow of foreign capital from abroad, an increase in the trade deficit in the short term, and a reduction in national income.

In addition, the revenue potential of the wealth tax is somewhat uncertain and often over-stated. For example, there is little agreement over how much wealth is even held by the very top. Research has estimated that the share of wealth held by the top one-tenth of 1 percent could be anywhere between 10 percent of all wealth, or 20 percent of all wealth.

And one thing that concerns me about the wealth tax is that it risks not raising any revenue whatsoever. And this is because a wealth tax, if enacted, would likely face a constitutional challenge. And while some have argued that the wealth tax is constitutional, it is worth emphasizing that other taxes would not even face this question at all.

Now, given the challenges with taxing wealth and book income, I think lawmakers should consider other sources of revenue that would be simpler to administer and more economically efficient. Raising the gas tax, or enacting the vehicle miles traveled tax, would be a reasonable way to pay for infrastructure. A carbon tax would help address climate change while raising revenue. And a value-added tax would be a broad-based tax that could raise a lot of revenue with limited negative impact upon the economy.

In addition to funding more spending, these taxes could also be used to offset more distortionary taxes.

Thank you, and I am happy to answer any questions.

[The prepared statement of Mr. Pomerleau appears in the appendix.]

Senator WARREN. Thank you, Mr. Pomerleau.

I now recognize myself for 5 minutes of questioning.

Our tax system is broken. Everywhere you look, there is one set of rules for most Americans, and a different set of rules for the richest people. One of the most glaring examples of this is how the
tax code treats wealth. The typical white family has about $188,000 in wealth. For black and brown Americans, that number is far lower, just $36,000 for Latino families, and $24,000 for black families.

So let’s just focus for a minute on what wealth looks like at the top. Let me start here. Dr. Disney, if you don’t mind my asking, how much wealth do you have, and how much did it grow last year?

Dr. Disney. I have about $120 million, maybe more depending on how the stock market is on any given day. It grows at about 4 to 8 percent annually.

Senator Warren. Okay; thank you. And so let’s just say—you said 4 to 8 percent—let’s just say an average growth of about 6 percent. That would mean that your wealth grew by about $7 million last year. That is almost 60 times the total wealth of the typical American family.

So let’s just for a minute talk about that increase. Do you know how much in taxes you will pay on your $7 million increase in wealth this year, Dr. Disney?

Dr. Disney. Not that much. It comes not from wages, but from things like dividends and capital gains and interest and so forth. So all of that qualifies for a lower tax rate than income.

Senator Warren. All right. And what about your total $120 million fortune? How much do you think you will pay in taxes on that this year?

Dr. Disney. Nothing. There is no wealth tax, so there won’t be any taxes.

Senator Warren. So, thank you. As I am sure you know, your situation is not unique. In fact, 99 percent of Americans pay about 7.2 percent of their wealth in total taxes every year. But the top one-tenth of 1 percent, they only pay about 3.2 percent. The unfairness runs deep.

Home ownership is the number one way that most middle-class Americans build wealth. And those Americans pay property taxes every single year on that wealth. But if you are an ultra-millionaire, or a billionaire, you have a million different kinds of assets—stock, paintings, diamonds, gold, cash—and you get to hang onto all of those assets as they appreciate, without paying taxes. And if you decide to sell, you’ll have an army of lawyers, and an endless supply of carefully crafted tax loopholes, to help you avoid paying taxes.

Now I’ve proposed a tax on the wealth of the very richest Americans. This is a 2-cent tax on every dollar of wealth above $50 million, and a few cents on every dollar above a billion. It would raise $3 trillion in revenue that we could use to build economic opportunities for every person in America, from universal child care to investments in education to fixing our roads and bridges.

The tax would be paid by the wealthiest 100,000 families, including yours, Dr. Disney. Poll after poll shows that Republicans, Democrats, and independents support this idea. Now, not everybody likes it. Leon Cooperman, a hedge fund billionaire who was hauled up before the SEC for boosting his fortune by using illegal insider trading, is one critic. He has described my 2-cent wealth tax as “dumping on the American Dream.”
I invited him here to make his case to Congress today, but I guess he prefers to stay in the safe space of financial news networks, where he can say whatever he wants and nobody pushes back.

Dr. Disney, you agreed to appear today, so let me ask you. If my wealth tax was the law, you’d owe nearly $1 1/2 million on your fortune. Of course, you would still be fabulously wealthy, and your wealth, which you said grew by about $7 million last year, would still have grown, but only by about $5 1/2 million.

So let me ask. Do you agree with Mr. Cooperman that this increase in your taxes would be—and I am paraphrasing the word he used—dumping on the American Dream?

Dr. Disney. Well, my American Dream would be alive and well, because the only effect a wealth tax would have on me would be to slow the growth of my wealth. It won’t be taking anything from me that I need.

And my American Dream also includes a lot of the people who are not currently having the benefit of things like roads, and schools, and parks, and good health care, and so forth. So to me, it is part of the American Dream to step up and pay my fair share.

Senator Warren. Thank you.

And, Ms. Straughter, if I can, let me ask you: a wealth tax would allow us to invest in the health and well-being of your workers. It would help us repair roads so it is easier to get to work. It would help level the playing field for small businesses like yours.

How would that affect your ability to pursue the American Dream?

Ms. Straughter. Yes. Using the voice of small business, it would allow me to increase my staff. It would allow me to grow from a small-sized business to a medium-sized business. It would allow me to pivot. So right now, I am in the headquarters of the Boston School Department, and right now many of the employees are working from home. So I am trying to increase my capacity as a caterer.

So what would help is the ability to have my business positioned to go after more contract work.

Senator Warren. Thank you. That is very helpful.

President Biden has called for raising taxes on the wealthy and on giant corporations to fund his Build Back Better agenda, and I agree. A wealth tax raises more revenue from those most able to afford it than just about any other plan on the table. It would allow us to build back better, and to make the American Dream a reality for millions of families.

I now recognize Senator Cassidy for his questions. And once again, I am going to hand him the gavel while I go vote, and I’ll be back.

Senator Cassidy [presiding]. Thank you, Madam Chair.

Mr. Hodge, again I do not have my glasses on, so now I cannot read my own writing. Was it you who said——

Mr. Hodge. You could use mine.

Senator Cassidy. What’s that? Thank you, yes. 1.75? Anyway, was it you who said that private investment will give you about a 10-percent return, and government investment about 5 percent,
and that is the opportunity cost of having it filtered through the
government?

Mr. Hodge. Exactly. Actually, that is the Congressional Budget
Office. In a very in-depth report and analysis of the returns to in-
frasctructure spending they found in that data that government in-
vestments return about half the returns of private-sector invest-
ments, for a variety of reasons——

Senator Cassidy. Okay, just hold that. Just hold that. So, Ms.
Straughter mentioned how she feels as if the investment that may
come through what is being called the infrastructure package, or
something such as that, may help her business grow. But what I am
hearing is that if that is an economically viable project, and if
you were to do the same thing through the private sector, you
would have more bang for your buck, less friction cost, and that
you may either have more investment, or investment not just there
but someplace else. Is that the logical conclusion from the CBO
study?

Mr. Hodge. That is exactly right. And what they did not take
into account is the harm to the economy of taxing those dollars in
the first place in order to pay for the investment. So there are real-
ly two hits to the economy. One is the opportunity cost of a lower
investment for government. The other is through the economic
harm through the taxes that are raised in order to pay for it.

Senator Cassidy. Yes, I do find that government tends to take
care of itself. I note Ms. Straughter is in a building where all the
teachers have been teaching remotely. I suspect if you went to a
private or a parochial school—well, maybe not; maybe Boston has
locked down everybody. But if we go to Chicago, we know that
some schools have been open, some have not, and the government
employees are the ones who have lost. I say that as a government
employee. There is a certain investment that you make.

So, Mr. Gamage, let me find my question here. I have been told
that since 1990, at least nine European countries with a wealth tax
have abandoned it, leaving only three that retain a wealth tax.
What are your thoughts about that? And why should that inspire
confidence in the ability to administer such?

Mr. Gamage. Thank you, Mr. Cassidy. With respect, it's
"Gammaj" not "Gamahj."

Senator Cassidy. "Gammaj?"

Mr. Gamage. Yes, "Gammaj," thank you.

Senator Cassidy. I am from Louisiana, so I am going to put a
little bit of a French inflection upon it. I am sorry.

Mr. Gamage. Totally understood. So the countries that so-called
"abandoned" wealth taxes, mostly that was during the Reagan-
Thatcher era where countries across the world were abandoning all
sorts of progressive taxes based on flawed economic analysis that
has not held up.

Countries have not abandoned the wealth tax, for the most part,
recently. It is very effective, and has been for over 100 years——

Senator Cassidy. But I know that in France, they abandoned it.
That was after—I mean, I do not think of France as being under
the sway of Reagan and Thatcher, but it was after the Reagan-
Thatcher movement that they first attempted to place and then
they abandoned it.
Mr. Gamage. Yes. There are two issues with that. One, the French wealth tax was poorly designed. Some other wealth taxes were poorly designed and should have been abandoned because of poor designs.

Two, it used to be quite easy for very wealthy individuals and families to hide wealth and income abroad. Since 2010, with the implementation of FATCA, it increased information technology and other financial reporting innovations. This is now very difficult. And both income taxes, with respect to wealth supposedly moved abroad, but also wealth taxes, have worked much, much better than they did——

Senator Cassidy. So let me ask you about that, because we have been recently told from various people, from the IRS Director, that there is a tax gap, that there are dollars out there that need to be taxed, but they are being hidden.

I think in your testimony I heard that you recommend—or maybe it is this bill—$70 billion that would go towards improving IRS enforcement, data collection, et cetera. So that suggests to me that maybe the ability to gather the data is not as robust as your last statement seems to suggest. Am I just not connecting the dots correctly?

Mr. Gamage. With respect, I’d say you are not. It is true that there is a tax gap which measures tax evasion. The tax gap is much larger for the ultra-wealthy than it is for ordinary Americans. But the tax gap is tiny compared to legal tax avoidance.

Senator Cassidy. Well, that is my point. My point is that, if these figures are so readily ascertained—oh, we can figure them out, don’t worry about it—and these collection systems are so efficient that the wealth tax would now work where formerly it could not, then how are people able to evade? And why do we need to give the IRS so much more money?

Mr. Gamage. People have limited, although significant, ability to evade. They have substantial ability to avoid legally the income tax because the income tax by law only collects tax if salaries are paid, stock or financial assets are sold——

Senator Cassidy. But it seems like you are talking about two different things. One is the legal avoidance, and the other is the evasion. And when you told me that the wealth tax in France did not work because people could too easily hide income, and now they can’t, but nonetheless I am hearing other testimony that suggests that there is still substantial evasion, and therefore we have to invest this money in the IRS, there actually seems to be a disconnect between these two statements.

Maybe I should just move on, because I am not sure that we are not just talking past each other, but I do think my question is a valid one.

Mr. Hodge, what is your perspective? Going to the other side, why did European nations abandon the wealth tax?

Mr. Hodge. Well, there are three primary reasons. One is the complexity that has already been discussed, and the very difficult administrable aspects of it. The other one is, it raised very little revenue. In fact, Switzerland is often held up as the paragon of the successful wealth tax that has been there for more than a century,
but it raises less than 4 percent of all tax revenues in Switzerland. So it has, basically, a trivial impact on their fisc.

And then lastly is the avoidance issue and the fact that people can move. And this is what drove France to eliminate their wealth tax, because the wealthy in France were fleeing. They decided that they could live quite nicely elsewhere and not pay the tax.

Senator Cassidy. Mr. Gamage, then with that statement do you favor a world-wide wealth tax? Because that does not seem practical to me, but that seems to be, if people can move, and they do, and if capital can move and it does, it seems as if the one example, for instance, I understand that China has an incredible capital flight. And if there is any country that has done its best to surveil everything about every one of its citizens, it’s China, and yet they have significant capital flight.

So, would you recommend a global wealth tax?

Mr. Gamage. The United States’ tax system, the current income tax, is citizenship-based and taxes all world-wide income for citizens, and always has. This is the key difference between the U.S. tax system and the French tax system. You cannot escape the U.S. tax system without revoking your citizenship and paying a substantial exit tax. That is current law, and it works quite well.

Senator Cassidy. And so the idea that somebody would give up their citizenship—I think one of the partners who made a lot of money from selling, or some big Silicon Valley company going public, renounced his citizenship and moved to Singapore, if I remember correctly.

I am gathering from you, you feel as if that problem would be minimal.

Mr. Gamage. It historically has been minimal. And you—— Senator Cassidy. Unfortunately, we haven’t had a wealth tax, and so I am not sure we can use past history to predict future actions, to kind of paraphrase the financial commercial.

Mr. Gamage. Again, you pay a substantial exit tax under current law by revoking citizenship. Not many people do it. Some do. If they do not value the protections and services provided to citizens of the United States, then fine. But the protections and services provided to extreme wealth are huge, and most ultra-wealthy benefit tremendously from being United States citizens and having those protections and services. And it is fair to have them pay a reasonable amount of tax on that, which they currently are not.

Senator Cassidy. Mr. Pomerleau, just to kind of spread out the questions, there seems to be a lot of, if you will, verbal slight-of-hand in that people are conflating wealth and income.

Now we know people get that confused. Warren Buffett used to say that he paid more in taxes than his secretary, but I think at that time he was the richest, or second richest person in the world—excuse me. I have to take a quick recess. They just passed me a note I have to go vote very quickly, but Senator Warren will be right back, and then we will resume. A quick recess, probably just minutes.

[Brief recess.]

Senator Warren. We are back in session. I apologize for the delay, but that’s what happens when you have to vote.
So our rigged tax code allows big corporations to report enormous profits to their shareholders, and at the same moment report little or no profits to the IRS. Of course, when giant corporations don't pay taxes on their profits, somebody has to pay. And the tax burden falls mostly on working families.

That is why I proposed a Real Corporate Profits Tax to force the biggest and the most profitable corporations to pay their taxes. For every dollar in profits over $100 million that a corporation reports to their investors, they have to pay 7 cents to the IRS. No tricks. No deductions. No loopholes. Nothing fancy.

President Biden has proposed something similar. One of our witnesses today is Abigail Disney, a shareholder in the Disney Company. So let's talk about how companies like Disney use the current tax system.

Dr. Disney, one scheme that Disney uses to pay less in taxes is to write off stock options that it awards its executives at a higher value than they report on their financial statements. So how much has Disney benefited from deducting stock options?

Dr. DISNEY. Disney has been able to save about a billion dollars from 2008 to 2015, just by this one bit of trickery alone.

Senator WARREN. Wow! A billion-dollar loophole that does not require the company to do anything differently, just file some paperwork. So, thank you.

Dr. DISNEY. Right.

Senator WARREN. Ms. Straughter, you own a business. What about you? How much in stock options have you deducted on your tax returns in recent years?

Ms. STRAUGHTER. Pardon the smile. Zero. Now, we have talked about a few things here today, and I have not been able to do that.

Senator WARREN. Okay. So let's do another example. Multinational corporations are able to use accounting maneuvers that shift money they have earned in the United States to lower-tax countries, which artificially lowers their U.S. profits.

Dr. Disney, how much has Disney benefited from these profit-shifting schemes?

Dr. DISNEY. Well, I do know that, in the year 2013, they were able to save about $315 million, 3-1-5 million dollars, on their tax bill.

Senator WARREN. Okay; and Ms. Straughter, how much of your business's income did you shift to a subsidiary in a lower-tax country?

Mr. STRAUGHTER. I did not do that at all.

Senator WARREN. Yes.

Now many companies also lobby Congress for specific tax breaks. In other words, these companies write the tax rules that apply to them.

Dr. Disney, has Disney been lobbying members of Congress for any special tax credits?

Dr. DISNEY. Disney spends a lot of time lobbying Congress, as well as local governments, and anyone else who has a say in what they pay in taxes.

Senator WARREN. Okay. And, Ms. Straughter, how many high-paid lobbyists are walking the halls of Congress to find tax breaks that will benefit you personally?
Ms. STRAUGHTER. I have not met one yet.

Senator WARREN. You know, this is the problem. Our tax code is rigged in favor of giant corporations like Disney, and everyone else, people like Ms. Straughter, are paying for it. Disney isn’t alone. In recent years, dozens of profitable companies have gotten away without paying 1 cent in Federal income taxes for the entire tax year—companies like Amazon, Nike, FedEx, Chevron, Netflix, Eli Lilly, Starbucks, IBM, HP, Halliburton.

So, Professor Gamage, we have gone through a couple of ways—just a couple—that big corporations use their massive resources to rig the tax system. Would a tax on book income, like my Real Corporate Profits Tax, ensure that these giant companies can’t get away with paying nothing in taxes?

Mr. GAMAGE. Yes; absolutely, Chair Warren. Because, since corporations can keep two books, they can currently report high earnings to investors and to increase stock options for management, while reporting low earnings or no earnings to the IRS through tax shenanigans.

The Real Corporate Profits Tax would limit both of these sets of accounting games. To briefly give just one more example, as I believe all three of the Republican-invited witnesses noted, the tax books allow accelerated appreciation and full expensing, which could in theory be part of a good corporate tax system. The problem is, it only works if you combine it with very strict limits on interest expense deductions, which we currently don’t have.

When you have generous interest expense deduction limits and these other provisions, as we currently do, it is not all that difficult for high-priced tax lawyers, like my friends and former students, to design wasteful, complicated transactions, earning enormous fees to reduce tax payments on the corporate side without affecting reported earnings.

The Real Corporate Profits Tax would deter all of these financial tax accounting shenanigans to the benefit of the real economy and creating a level playing field.

Senator WARREN. Well, thank you, Professor Gamage. You know, this is why the President’s Made in America plan is so important. It includes no-brainer policies like raising the corporate tax rate and cracking down on overseas profit shifting. But it also contains a backstop similar to my Real Corporate Profits Tax.

As President Biden has said, we have firemen and teachers paying 22 percent, while these giant companies pay nothing. That is wrong. Yes, that is wrong, and Congress can change it.

With that, I recognize Senator Carper for 5 minutes.

Senator CARPER. Thank you for inviting me to join you all today. And to our witnesses, there are a number of hearings that are going on and important votes on the floor, so do not take the fact that we are not all here at once the wrong way.

We are delighted that you have joined us today, virtually and in reality, and we are grateful to the chair for bringing us together.

Madam Chair, long before I was a Senator or Governor, I was a House member, and I used to hold town hall meetings, lots of them, hundreds of them. I loved town hall meetings. And one of the things I would do every year was do sort of like a budget workshop
in a town hall meeting, and we would invite people to spend a couple of hours, just ordinary citizens, helping us balance the budget.

And at the time the balance or the deficit was closer to $100 billion than $2 trillion, but I remember this one—and usually we were actually able to make progress and find common ground and balance the budget in a 2-hour episode. And I used to say, “We ought to elect you guys and bring you down to Washington.” But I remember this one particular meeting we were having with all these citizens at this workshop. I remember saying to the group that was there that part of balancing budgets is making sure we have an ample revenue side, and I quoted Oliver Wendell Holmes, who said that taxes are what we pay for a civilized society.

But anyway, I remember this one lady in the room, she said, “You know, I don’t mind paying taxes. I just want to make sure that other people are paying their fair share of taxes.” I have never forgotten that. And, Madam Chair, you know that about a week or so ago we had the Commissioner of the IRS here, Chuck Rettig, and in past years previous Commissioners like John Koskinen, who is a terrific public servant. And among the things we have talked about are what could we do as an oversight committee of the IRS, what could we do to better ensure that the IRS has the resources. One is providing guidance and advice to taxpayers to know how to complete their taxes. And two—going back to the lady’s comments years ago in a budget workshop—is to make sure that everybody is paying taxes.

And for the almost I think 10 years that John Koskinen was the Commissioner of the IRS, he would come before this committee in this room and ask for additional revenues for the IRS so that he could hire some additional people, and to hire the kind of people with the skills that they needed, and to buy the technology that would enable them to better ensure that everybody is paying their fair share. And his testimony, very sadly, fell on deaf ears year after year after year. And over in the House of Representatives, the Republicans in the House sought to impeach him—impeach him. Not just rake him over the coals, but to literally throw the book at him.

And that did not succeed. He finished up his tour, and he is now, I think, still gainfully, maybe not employed, but he is still working and contributing. But I remember he used to tell us that for every dollar we would provide for the IRS, they could collect anywhere between $5 to $10. That is a pretty good return on investment. And he would say the same thing about hiring people and providing the technology that was needed. Subsequently, he retired, and our new Commissioner, Mr. Rettig, has testified just in the last month in this same room. And he said very much the same thing that Commissioner Koskinen said: we need resources, we need people, we need technology to help us better advise people, to help people to complete their returns and file their taxes, pay their taxes. But we also need, for some of the folks whose businesses have very, very complex finances, we just need to have the wherewithal to drill down on those and make sure that they are paying their fair share as well.

So we have reformed the estate tax and step-up in basis. I like to treat other people the way I would want to be treated, and I am
sure that all of us feel that way. But when I was a House member years ago, I believe that there was an exclusion for the estate tax. I want to say it was about a million dollars for a couple. And today, if I am not mistaken, it is about 20 times that. And I thought, maybe arguably, a million dollars was too low. I think, just as arguably, given the size of the deficit we face, $20 million is too high.

A reporter asked me today how I felt about reforming the estate tax, and I said I think there is probably a number between 1 and 20 that actually would probably help us on the budget side, but also I just try to be fair to folks who are filing their taxes.

So, it is something that I am interested in, and I am delighted that you are holding this hearing. I have maybe—this is to the Professor, and I am going to butcher this name, but it's spelled G-A-M-A-G-E. How does he pronounce it?

Mr. GAMAGE. Gamage, please.

Senator CARPER. Gamage, like damage? It rhymes with damage?

Mr. GAMAGE. Absolutely.

Senator CARPER. All right, Professor Gamage, not Damage, where are you joining us from today, sir?

Mr. GAMAGE. Indiana University, our School of Law, currently at my home in Bloomington.

Senator CARPER. Okay. We have just confirmed an Indianan to be Deputy Administrator for the EPA. Her name is Janet McCabe, and she was confirmed on a bipartisan vote, and we are delighted with that. A good woman.

Mr. Gamage, thanks to—again, our thanks to Senator Warren for pulling this together. I mentioned the earlier testimony of John Koskinen and Chuck Rettig, the current Commissioner, and I have—I am not going to repeat that again, but I would ask this question. Can you share your thoughts on how we can best equip the IRS to close the tax gap? And this is a question I have asked repeatedly of the previous Commissioner and the current Commissioner. But your thoughts on how we can best equip the IRS to close the tax gap, and what will greater enforcement mean for broader fairness in the tax code. Mr. Gamage, please.

Mr. GAMAGE. Thank you, Senator. The tax gap from illegal tax evasion is a real problem and should be policed better, as I will explain. Looking back to Senator Cassidy's question to me earlier, it is important to understand that illegal tax evasion is small compared to legal tax avoidance enabled by loopholes in the current system. But illegal tax evasion is, if anything, especially harmful, both because of the small but significant direct revenue loss, but also to tax firms, to tax morale, compliance norms, and faith in the overall economic and political system.

The academic literature is clear that, first, the most important thing to do is fund the IRS adequately, and protect that funding from the winds of the appropriations process. The committee is considering some important measures to do that.

On top of that, improving information reporting would be the next most critical step. On top of that, I would strongly recommend extending the Federal False Claims Act to large tax claims of ultrawealthy families and individuals in the largest businesses, like New York State does, as an important backstop to the IRS's tax enforcement.
Again, tax evasion is not the biggest portion of the problem. It is small in revenues compared to fully legal tax avoidance. But it is important, both on its own for the revenues, and perhaps even more importantly for the impact on faith in the tax system and overall tax morale.

We need to fund the tax police and give them better tools to do their job. Thank you.

Senator CARPER. Thanks very much. I have a couple of other questions for the record, including ones for Dr. Disney regarding taxation and generational inheritance and helping to create a fairer, more fiscally responsible tax system with respect to the estate tax. Thank you so much.

Senator WARREN. Thank you, Senator Carper.

The chair now recognizes Senator Wyden.

Senator WYDEN. Thank you very much, Chair Warren. And I think it is extraordinarily important that you are addressing income inequality through the tax code. And I want to pick up on some of the issues that have been discussed today, apropos of this question of the IRS and tax enforcement.

We were told of course in the committee that the tax gap was much bigger than anyone had anticipated. And today we got additional information that drives this particular assessment.

I asked the Justice Department to get us information about whether Credit Suisse continued to help wealthy Americans defraud the Internal Revenue Service even after it signed a settlement agreement to stop the practice.

So every time you turn around, we do see issues relating to whether or not affluent Americans, the fortunate few, can take advantage of an under-manned, out-gunned Internal Revenue Service—their words, not mine.

And, Professor Gamage, your points here are well-taken, and we expect the Justice Department to give us that information promptly, because there are some issues with respect to Credit Suisse that are very timely.

So, I think what I would like to do is turn to two other issues that drive income inequality in the tax code and, Professor Gamage, get your assessment on this.

The first is the effect that the loopholes in the tax code have. I mean, it seems to me that wealthy taxpayers have found ways to largely avoid the estate and gift taxes through complex shelters and trusts and the like. And large corporations have found ways to shrink their tax liabilities also through complicated schemes.

Tell us, if you would, how that contributes to this issue of driving income inequality in the tax code.

Mr. GAMAGE. Yes; thank you, Senator. And I would be remiss if I did not note that the work you and your staff are doing on mark-to-market reforms is, I think, one of the most exciting developments in tax reform since I have been a tax professor, and maybe in our Nation’s history.

Senator WYDEN. Thank you.

Mr. GAMAGE. To answer the question, most Americans have wage and salary income which is taxed at relatively high rates. That means, if you are not born into inherited wealth and you have to work or earn the money to invest, you get much less after tax. By
contrast, if you are born into inherited wealth, or you have the social capital, or you are part of a big enough business operation to borrow at very cheap rates—borrowing is currently not included in the tax base, and there are a variety of deductions to make borrowed investment financing tax-favorable, often making wasteful investments profitable to the taxpayers, ones that are harmful to the economy, profitable after tax in the form of tax shelters. All this makes it quite easy to pay comparatively little tax if you already have the wealth or capital, or the social capital to borrow from parents, friends, or others.

This makes it hard to catch up for anyone who was not born into those privileges, for small businesses that want to expand to compete with larger businesses. It is an uneven playing field partially created by our tax system, and it should be addressed. Thank you.

Senator Wyden. It seems to me what you are telling Chair Warren and the committee is—and I asked about loopholes, but I think you have gone even further now to describe what I really call the fundamental flaws that underpin the two tax codes in America.

If you are a nurse in Medford, OR this afternoon and you treat COVID patients, you pay taxes with every single paycheck. If you are a billionaire in an affluent suburb somewhere, to a great extent, if you have good accountants and good lawyers, you can pay what you want when you want to, and often hardly anything at all.

So it seems to me what you have helped us do, Professor, and we appreciate it, is describe not just the loopholes, but the inherent inequity baked into this notion that there are two tax codes in America.

And I would be interested in your assessment of that as well. So if you add it up, you have given the chair testimony about how part of the problem is that the IRS is out-gunned and out-resourced, and that is why I asked about this problem with respect to Credit Suisse and what happened with respect to whether they told the truth to the Justice Department. That is part of it. Then loopholes are part of it.

Then there is the question of whether basically the underpinnings of the system are fundamentally unfair. And I would be interested in your last assessment, because your other two were very good on enforcement and loopholes. What is your assessment of the fact that this inequity is just baked into this two-tiered system?

Mr. Gamage. That's absolutely correct, Senator. What do high-priced tax lawyers do? What do my friends in practice do, and what do I train my students to do? Find one way of saying this—or one of the things they do is to find what might seem like a small loophole and figure out how to drive a giant truck through it. Those are complicated, wasteful, excessive structures designed for tax planning.

There is not a clear division between what you might call a loophole and a fundamental flaw of the tax system that generates these massive inequities. And for all the reasons you said, Senator, both our business-level corporate tax system and our personal tax system, with respect to the ultra-wealthy, are fundamentally broken and in dire need of reform. It matters in so many different ways, so many different harms to the social fabric of our country, and to the functioning of our economy.
Senator Wyden. I want to apologize to the committee’s other guests. This has been, I think, a very good panel, and I looked at the testimony. You have arrived at a particularly hectic time in the Senate, and I want to apologize to our guests and thank Chair Warren again for putting together a very important hearing. And I look forward to following up on what you tell us. Thank you all.

Senator Warren. Thank you, Senator Wyden.

Senator Cassidy?

Senator Cassidy. Professor Hoopes? Am I getting that correct, Professor?

Dr. Hoopes. Correct. Hoopes.

Senator Cassidy. Hoopes; gotcha. Thank you. What a name for a guy from North Carolina. I just would expect it; I just would expect it. I liked your testimony. You point out that a lot of the problems that, say, Senator Wyden is referring to, or Professor Gamage is referring to, are holes punched in the bucket by Congress.

I think I remember—and if I am wrong, I apologize in advance—that Senator Wyden is a really big advocate for tax credits for EVs. So I am a billionaire and a millionaire and a multi-billionaire, and I go buy a Tesla, at least when they had credits, and I got a big tax credit to buy the EV. I always found it ironic that the working people in my State are subsidizing the billionaire buying the Tesla. But that is their issue, not mine.

But to your point, if a corporation or an individual buys tax credits related to the production of renewable energy, we are being told that because their tax burden decreases, that somehow it is a little immoral and we should be going after it. On the other hand, this is the sort of social behavior we are trying to incent: people investing in such things. It seems like we are talking out of both sides.

Any thoughts on that, sir?

Dr. Hoopes. Well, I think this applies much more to these tax credits, and the loophole, for example, that Senator Warren was talking about using—

Senator Cassidy. The so-called loophole, right?

Dr. Hoopes. The so-called loophole. I mean, the stock options, you are literally just compensating your employees. That is perfectly legal to deduct on your tax return. So you use the term “loophole” in ways that, if you actually talked about the issues, nobody would have any issue with that at all, giving your employees compensation, and you should rightfully be able to deduct that.

Likewise, if Congress wants to incent more EV vehicles, if they want to incent clean energy, they are going to give a tax credit. So when you use this language, you do not actually talk about the specific tax issue, because there is broad agreement on most of these tax issues. Instead, we call everything a loophole and completely do not discuss the real issue, and as a result, we do not really make any progress.

I completely agree, we need to actually talk about, issue by issue, what these things actually are, whether they are justified, and eliminate them or not. And instead, we say everything is a loophole; it is all bad. We are just going to layer on this other layer of complicated taxes that are going to have their sets of issues.

Senator Cassidy. So in your testimony, it is not just your opinion—because you have an opinion, you are a learned person—but
if I remember correctly, your testimony in one of the footnotes quotes academic literature that political rhetoric actually—and now I cannot find the doggone footnote—but that political rhetoric actually drives tax policy, and if somebody wishes to kind of stick it to another person, they just use the rhetoric. They heat it up. They use pejorative terms. And that which just might be the internal buildup not being taxed in that nurse in Medford, Oregon's 401(k), suddenly becomes a loophole.

Do I remember it was you who had that reference?

Dr. Hoopes. Yes. I think often the way we talk about taxes, we have to generate a demand for either tax increases or tax cuts. Certainly, both sides of the aisle are not innocent of this.

Senator Cassidy. And what did—you also refer to Amazon. Somehow there was political pressure to change the way that Amazon reported. I tell you, I am sensitive to that. We have incredible power in Congress to pressure people, to really put the screws on them. If you don't comply, by golly, you are not going to get whatever you are seeking. And that is just a little bit too authoritarian for me. Because, frankly, I have seen how government can make incredibly bad decisions, keeping people in dependency when they themselves would prefer to live independently.

So I am very sensitive to that. And again I apologize—I should have said it better. But I gather that their accounting rules changed as a result of political pressure, and it put such political pressure on the FASB as would likely intensify if we were to tax book income.

Would you like to comment further on that, besides that which I just said?

Dr. Hoopes. That's correct. I mean, it's not that the accounting rules changed because of pressure, it is that they have not been allowed to change. So this difference that Chair Warren mentioned between Amazon expensing stock options for tax purposes but not for financial accounting purposes, that actually should not be the case. The treatment should be similar in both cases, and the tax code actually gets it right.

The reason why financial accounting, in the opinion of most experts, is actually incorrect on this issue is because, every time the FASB has said we need to correct this, to recognize the compensation as an actual expense, the Congress has not allowed it, and has basically threatened to put the FASB out of business. That to me is just exactly what would happen if we had a tax on book income. When the stakes get high and we are actually taxing that number, taxing book income as part of the tax base, if the FASB wanted to make consequential decisions to try to actually reflect the economic value on the firm, as is their role, Congress would step in just as they have in the past and not allow that to happen.

The very poster child for the Real Corporate Profits Tax is a result of Congress having essentially messed up the work of the FASB, and that would continue to happen, or even worse, if we were to have a Real Corporate Profits Tax.

Senator Cassidy. Got it. Political control of the economy.

Senator Warren?

Senator Warren. Thank you very much, Senator Cassidy.
So I think a big part of making the tax system fair is about how the IRS enforces the tax laws that are already on the books. When a teacher gets ready to do her taxes, the school sends her a W–2 form, and they send the same thing to the IRS. She knows how much income to report, and the IRS knows how much income she is supposed to report. It is called third-party reporting. It keeps people honest, because the IRS can spot it if somebody fudges the numbers on their return.

But not so for the top 1 percent. Most of their income comes from business interests and capital gains that they receive when selling assets. There is no third-party reporting for these types of income, so the IRS counts on the richest taxpayers to follow the honor system.

Professor Gamage, it sounds like we have two sets of rules here: wages for teachers and bank tellers and construction workers are all automatically reported to the IRS. But for the wealthiest Americans, it is the honor system.

So tell me, is the honor system working?

Mr. GAMAGE. No, it is not working, Senator, and it should be fixed. The academic literature is clear that compliance is very high for income subject to information reporting, and especially when there is both information reporting and withholding, as there is for the vast majority of the income earners, like ordinary Americans.

By contrast, tax compliance is quite a bit lower, much lower, when there is not information reporting or withholding, as is the case for much of the income earned by the ultra-wealthy. It is past time to fix this.

Senator WARREN. So this kind of under-reporting by high-income taxpayers creates what we call a tax gap: taxes owed but not paid. As some folks referred to earlier, IRS Commissioner Rettig was here last week, and he estimated that the tax gap may now be as high as a trillion dollars a year. That is about the same as the amount of all of the Social Security checks that were sent out last year.

Now the IRS tries to catch tax cheats by auditing tax returns. But the wealthy enjoy a different set of rules here too. After a decade of politically motivated Republican budget cuts, the IRS enforcement budget is now nearly 25 percent smaller than it was in 2010. And the agency employs 30 percent fewer enforcement personnel.

Professor Gamage, the Republican budget cuts hollowed out the IRS. So what has that meant for the IRS’s ability to conduct audits and catch tax cheats?

Mr. GAMAGE. Thank you, Senator. The IRS is simply out-gunned when it comes to trying to catch and police the tax shenanigans of the ultra-wealthy and the largest businesses, whether these be clearly illegal—what the tax gap is mostly measuring—or whether these be legal but very aggressive with layers on top, but the more important category may be the borderline category.

It is well known, for instance, among the highest-priced tax lawyers, that if you set up a complicated enough flow-through/pass-through structure through which income is earned, the IRS won’t have the resources to be able to audit and challenge and look through what happens in that flow-through structure. The idea is
to try to make—you know, many of the higher-priced tax lawyers
do this by staying just on the side of what is legal, but maybe
crossing over it. Although a fair amount of what goes on crosses
that line into clearly illegal tax evasion, regardless, the IRS just
does not have the resources and competence to look through these
excessively complicated structures.

And I will repeat again, this is economically wasteful. Lots of
money and resources are being tied up in these excessively com-
plicated structures for tax abuse reasons, tax planning reasons,
whether legal or illegal. We can and should prevent this, both
through tax reform and, importantly, through giving the IRS the
resources it needs to operate as tax police.

Senator WARREN. And looking at the numbers on this, audit
rates for people reporting more than a million dollars in income
have fallen by 70 percent. And for people reporting more than $10
million, it has fallen by nearly 80 percent. Audits of big corpora-
tions, those with more than a billion dollars in assets, have fallen
by more than half.

It is just as you say, Professor Gamage: these are complicated
audits to do. And when the budget gets cut, that is where the IRS
has been cutting.

You know, while the IRS has turned its eyes away from the
wealthy and from giant corporations, it has come down hardest on
the people who are cheapest to audit: very low-income taxpayers
who qualify for the Earned Income Tax Credit, or the EITC.

In fact, if you are earning $25,000 in a rural community in the
South, you are more likely to be audited than if you were a million-
aire living in New York City. The most-audited counties in the
country are poor, rural, and predominantly African American.

Ms. Straughter, does it seem fair to you that the IRS has all the
information it would need to double-check your employees’ income
right there at the IRS’s fingertips, but that the wealthy get to hide
income and would not likely face any consequences from that?

Ms. STRAUGHTER. Senator Warren, it is absolutely unfair on so
many levels to not have documentation to make sure that the
wealthiest Americans are paying their fair taxes. It is a disgrace.

The IRS knows what I should pay. You know, it was referenced
that they receive the W–2. They know how much income I have.
They know what I should pay. And to sit in this hearing today and
understand that the same rules do not apply to the wealthiest of
Americans—one thing that Mr. Cassidy said that is correct is that
the rich will do fine.

Senator WARREN. Yes. Thank you very much.

You know, I am working with my colleagues, including Chair
Wyden, on a bill that strengthens IRS enforcement. One of the fea-
tures of this bill is the requirement to strengthen reporting so that
the IRS can verify information on wealthy individuals’ income. An-
other is to give the IRS more funding to audit millionaires, billion-
aire, and giant corporations. Stepped-up enforcement against
these big tax cheaters would give us as much as $1.8 trillion in
new revenue over the next decade.

The only people who stand to benefit from a weaker IRS are
wealthy tax cheats. Fixing the IRS is about making sure that the
government is fair, and that we have the revenue we need to invest in a stronger future for all Americans.

Senator Cassidy?

Senator CASSIDY. Senator Warren, in all due respect, using terms like “tax cheaters” seems to prove what Professor Hoopes said, that we use rhetoric in order to shade the argument.

I would also like to do a little bit of fact-checking. The cuts to the IRS began under President Obama in 2012. I suppose Republicans would be blamed for a lot of things, wanting the American people to be independent and that sort of thing, but the cuts to the IRS began under President Obama, just to say that.

Mr. Pomerleau—did I get that name right, Mr. Pomerleau?

Mr. POMERLEAU. Pomer-low, yes.

Senator CASSIDY. Pomerleau, I'm sorry. I am having a tough time today.

There does seem to be a little bit of a verbal sleight of hand taking place here. We speak about—we are conflating wealth and income. And so as a percent of their wealth, people are paying so little. Now, reasonably speaking, if we go to a nurse not in Medford, OR, but say in Shreveport, LA, and she has a 401(k) with internal buildup, year by year she is not paying taxes on that internal buildup. Indeed, the taxes are deferred.

And so—now granted, those with great wealth have more of an advantage from this in absolute dollars because they have greater wealth, but I do not think we would conflate the fact that she is saving for her retirement with her income when it comes to taxes. Are there any issues with how I am analyzing that?

Mr. POMERLEAU. I think it somewhat comes down to different definitions of income, and philosophically what the tax base should be at the end of the day. I think many proponents of the wealth tax feel that the income tax, which they define as the tax that should apply to people’s consumption plus their change in net worth, does not do a sufficient enough job in raising revenue. So the wealth tax is there to fill that gap.

But yes, you mention another important point here, that the current tax code actually—on purpose in many ways—has been shifted more from an income tax to a consumption tax. So there are provisions such as 401(k)s that have been put in place to reduce the tax burden on the return to wealth for middle-income earners that are saving for retirement. And the idea there is that, if you reduce that tax burden, people will be able to save for retirement and have enough to care for themselves in the future.

But I think you are right that a lot of this, at the end of the day is, well, we really want to tax income, and we are upset that people are earning income that may not get taxed for a number of reasons, and that the wealth tax is really a backstop to that, rather than really just being upset that wealth itself is not being taxed.

Senator CASSIDY. Mr. Hodge, there seems to be a lot of unfavorable contrasting of us with countries like Switzerland, et cetera. It is my understanding, though, that our tax code is far more progressive than theirs. The value-added tax is inherently regressive. If you have a 21-percent VAT, every step of the value being added, you are getting another 21 percent. And if I am spending most of my disposable income upon consumables, like furniture, et cetera,
that ends up being quite regressive. And indeed the U.S. has a far more progressive tax code than such countries like, well, pick your European country. Any thoughts on that?

Mr. HODGE. The OECD has looked at this and found that the United States has one of the most progressive and redistributive income taxes of any industrialized country. In fact, they found that only Israel taxes their wealthy more and redistributes more through the tax system.

We actually do more than any other country to try to help low-income people through the tax code through things like the EITC and the refundable tax credits. And so the poor in America, according to the OECD, have the lowest income tax burden compared to the poor in any other country because of that.

Senator CASSIDY. Okay. I will—I have 30 seconds left. I know you have another set, and I will save my last round for my next 5-minute block.

Senator WARREN. Thank you.

And I love being fact-checked. So let’s do a little fact-checking on this. You say that the IRS budget cuts started in 2012, and President Obama was in the White House, and you are right. But I think you might want to go back and look at who actually led the charge to cut the IRS’s budget. And I think it was the Republicans, but I will do this for you. Either way, can we agree that those cuts to the IRS budget were a terrible idea, and that the IRS needs enough money to close this tax gap so that they are actually able to enforce the tax laws that are currently on the books? I am not even talking about putting more laws on the books, just enforce the dang stuff that is out there.

Senator CASSIDY. I am totally for the IRS being able to enforce the laws given to it. Of course, in any budget, tradeoffs have to be made, and so if folks decide to spend money here, as opposed to the IRS, then that is something which is a priority that Congress made.

I am not sure I would blame Congress, though, for a budget which the President signed.

Senator WARREN. Well, fair enough, but let’s just stick with what we want to do now. Because the one thing that is very different about spending money with the IRS is that it actually brings in more revenue. And so the question is, how much more revenue?

And I understand that you object to my calling people who do not pay the taxes that are legally owed “tax cheats,” but I do not know what else to call them.

Senator CASSIDY. Can I reply to that, because——

Senator WARREN. You sure can.

Senator CASSIDY [continuing]. Because Mr. Gamage tells us that indeed most folks are not paying taxes because of laws that Congress passed.

Senator WARREN. But that is not what the IRS Commissioner was talking about——

Senator CASSIDY. Well, that is different from what Mr. Gamage is saying.

Senator WARREN. What Mr. Gamage was saying is that $1 trillion in taxes that were owed were not paid. People who owe taxes and do not pay them, to me that is the definition of——
Senator CASSIDY. Maybe we need Mr. Gamage to clear up my misimpression, or your misimpression, because I had the sense that, as Professor Hoopes said, Congress has punched a hole in the bottom of the bucket. And whether it is EV tax credits, et cetera, the people with wealth are not paying taxes because of provisions that we have passed.

And I think I heard from Mr. Gamage that the amount that is legally avoided is far greater than the amount that is illegally avoided, but if I am wrong, please correct me, Mr. Gamage.

Senator WARREN. So I think that is what Professor Gamage said. The point is, let's just stop at least the part that is already legally owed and make sure that people are actually audited, especially wealthy people, and that they are audited more often than poor people—and that we collect the taxes that are owed. That is all I am doing here.

Senator CASSIDY. What I don't know is if the poor people or any people are audited because they just have a computer program that kind of runs through and says, here's a guy with a W-2 and not much else, so therefore—I do have some stocks, et cetera—but, you know, somehow it is relatively easy, versus that which requires going out and looking at people's books.

If you are saying turn off the computers so that we are not going to look at that which we can easily look at, that does not seem very wise. On the other hand, we certainly should treat all Americans fairly no matter what the socioeconomic class.

Senator WARREN. Good. And I think that is the point. We want to make sure they have enough money to be able to go after the complicated tax schemes that the wealthy are able to use, and the big corporations.

So I just have a couple of questions I want to clean up. As we do this, we have heard a lot today about my wealth tax, including about how it would help close revenue gaps and grow the middle class. We also heard some criticisms, so I want to take the opportunity to get a few more things on the record.

Let's get some clarity about how a wealth tax could be implemented. Professor Gamage, a few of your fellow panelists have argued that it would be too hard to implement a wealth tax because we are unable to value the assets of wealthy individuals. Do you agree with that?

Mr. GAMAGE. Absolutely not. Now any tax system is going to be imperfect. A wealth tax would not be perfect. But it would not be hard at all to design a wealth tax that would be dramatically better than the existing income tax, much better as targeted to the ultra-wealthy mega-millionaires and billionaires, as the proposed wealth tax would be.

The vast—not the vast majority—the majority of wealth is held in the form of stock and publicly traded assets that are easy to value. And along with tax professors Darien Shanske and Brian Galle and economist Emmanuel Saez, and assistance from the Roosevelt Institute, I have been working on a model set of valuation and enforcement rules for wealth tax reforms based in part on the successful Swiss wealth tax experience.

The proposed ultra-millionaire wealth tax would give Treasury the authority to adopt our proposed rules, or perhaps to come up
with something better. I am extremely confident that the proposed ultra-millionaire tax, as implemented by Treasury, would do much, much better than our existing income tax at measuring and valuing and enforcing wealth, or the true economic resources of mega-millionaires and billionaires.

Senator WARREN. So thank you, Professor Gamage. Let me just look at an example of that.

Dr. Disney, how much of your wealth is in stock and other property like that?

Dr. DISNEY. Most of it.

Senator WARREN. Okay, and how much is in one-of-a-kind, hard-to-value Disney collectables, or other things that are hard to value?

Dr. DISNEY. Very little. It has been my experience it's very rare for a wealthy person not to know exactly where all their money is and how much everything is worth.

Senator WARREN. You know, there are plenty of tools available to value the assets of the wealthy. They are constantly being valued in the private markets, and for insurance purposes. The IRS values these assets when the wealthy die. And if it is really true that there are some billionaires whose wealth is so immense that we do not even know how to start counting it, then that is the best argument I have heard all day for a wealth tax.

I have another question I want to ask about. A few of the witnesses suggested that taxing book income like my Real Corporate Profits Tax, or President Biden's tax plan, would cause corporations to manipulate their financial statements to try to find the same kind of loopholes they now use in the tax code.

So, Professor Gamage, do you think that giant corporations would be willing to report lower book income so they could avoid paying a 7-percent Real Corporate Profits Tax?

Mr. GAMAGE. You have to start by remembering that profits reported for financial accounting purposes, as I think every tax analyst agrees, are currently inflated. They are inflated because inflating them gives managers higher compensation in stock options, among other reasons, and drives up share prices. So the Real Corporate Profits Tax Act would deter these financial shenanigans, and that would be good. And a reminder: the best research in the academic literature suggests 50-percent book tax conformity. We currently have zero percent. The Real Corporate Profits Tax would move us to 25 percent, a significant step in the right direction.

Senator WARREN. Okay. So would it be a fair characterization to say that by applying a tax to a number that corporate executives want to have as high as possible, that a book income tax would serve as a backstop to the existing loopholes in the tax code?

Mr. GAMAGE. Absolutely, yes.

Senator WARREN. Okay. Now, one last area I just want to hit, and then I will give this back to Senator Cassidy. Some of our witnesses have suggested today that a wealth tax and a Real Corporate Profits Tax would reduce economic growth.

Professor Gamage, we are back to you again. What kind of impact would these taxes have on our economy, in your judgment?

Mr. GAMAGE. I think they would help the economy, and especially help shared economic growth and prosperity and level the playing field. The big problem in our economy today, as our eco-
nomic research finds, is not on the supply side, lack of resources seeking investment; interest rates are historically low. There are massive funds seeking investment. It is on the actual investment happening in a variety of ways.

These tax reforms would help with this, on the public side, through greater public investment, but also by deterring some of the tax planning shenanigans which make it so that, instead of productive investment, what we see happening is excessively convoluted structures designed to minimize tax, some legal, most legal, but some illegal, but regardless, wasteful and economically harmful. And the overall tax reduction that the ultra-wealthy get away with, and large businesses, through these structures, stands in the way of real economic growth and prosperity.

Senator WARREN. Well, these taxes would raise as much as $6 trillion that we can pour right back into communities and families all around this country. We can make serious investments in good jobs, in strong infrastructure, and quality child care for every family.

Those are investments that help families get ahead. And when families have the support they need and the jobs that pay fair wages, they can spend a little more at their local businesses, and maybe start a small business themselves.

Senator Cassidy, why don’t you ask whatever last questions you want to ask and make a closing statement. Then I will ask my last question and do a closing statement, and we will wrap this up.

Senator CASSIDY. Mr. Gamage—Professor Gamage, Mr. Hodge made the statement that when the private sector invests, you get about a 10-percent return. And when the public sector invests, you get about a 5-percent return. But it seems as if you are favoring so-called public investments.

I am sure you would argue that, no, I want both, but I was just told 2 days ago that when the New York school system builds a building, it costs 50 percent more than when a private company would build the same building. And I have here an article, “Why New York will never build another subway.” And they just talk about the incredible expense and delay of building their last few miles of subway in New York. Let’s see, at 1.5 miles—a 1.5-mile subway cost $4.6 billion.

I am not sure I am as confident as you that that private-sector investment will be as fruitful. Now are you speaking not of construction projects, but of, you know, paying for child care workers? And if that is the case, I did not think that economists were quite as positive about such consumables, as one economist called it, leading to long-term economic growth as infrastructure.

There is a lot there, and I apologize, and I have to ask you to go quickly, because I have a couple more questions and just a little bit of time.

Mr. GAMAGE. Okay, I will try to be quick. I would say two things. One is, the public and private sectors are better at different things. Each are important for a society with shared prosperity.

Second, these tax measures being considered do not create this choice between public or private investments. That may have been the case in the 1950s and 1960s that a big problem with our economy was lack of capital stock. That has not been true for decades,
and it does not appear that it will be true for some decades to come.

What the problem in the economy right now is, is lack of overall investment. And these tax measures, I do not believe would significantly or at all reduce private-sector investment. In fact, I think they might switch currently wasteful tax stratagems and excessively convoluted structures into real investment as another way of helping the overall real economy.

Senator Cassidy. So, Professor Hoopes, you had mentioned in your testimony that you think it is far more difficult to estimate overall wealth than Professor Gamage seems to think. And I also—so please give your perspective on how easily that that can be done. And secondly, do you also agree that these tax stratagems are diverting so much investment that could otherwise go well that our society would be far better off?

Dr. Hoopes. Valuation is difficult. So it is difficult to value things, and that is actually the underlying root of another big tax planning problem we have in the United States.

Several times people have mentioned profit shifting. The heart of the issue of profit shifting is not being able to value intangible assets and the return on those intangible assets back into the United States. If it was so easy to value these assets, then we would essentially not have this profit shifting issue.

Because we have the profit shifting case where the system does not depend on realization, we would have the exact same issue with the wealth tax. And so that valuation really is an issue you cannot just simply wave off, because there are already pieces of our tax code that seem broken because of valuation.

Now to get to the private investment piece, I do not think that corporations are spending such massive amounts on tax lawyers and accountants. As a producer of tax accountants, maybe I wish that were the case, but I do not think that they are actually hiring so many of them that they are unable to invest in profitable investments because——

Senator Cassidy. It seems like that would be a very marginal cost relative to the overall operations on, pick a corporation, Boeing or Google.

Dr. Hoopes. I do not have the numbers, but this is a knowable fact, and we have statistics on how much corporations actually spend on tax planning, and it is simply not that much money. To assert that it is, is simply not the case

Senator Cassidy. I kind of agreed with you when you said wave off the complexity of it. I will finish, before my closing statement, with an anecdote, because sometimes the anecdote proves the rule.

A gentleman back home grew up poor in north Louisiana, started a construction firm, and now it is, I'm sure—I do not know how much the guy is worth, but he is worth a lot. Along the way, he has made a lot of people very wealthy with profit sharing for his employees so that if he did well, they did well. And not just his chief lieutenants, but the people all the way down the line.

Now as I thought about—as this was going on, I thought about valuing his business year by year. One year, they may get a billion-dollar contract to do a massive public works contract, and then the next year they may not. They are just doing this, and the value of
it is depreciating. And then the next year, they may or may not. But then they may do really well, and then they may do really poorly.

And a family-owned business would have to then really spend money on valuation, with the potential for audit, because the value of the company presumably is fluctuating every year, depending upon their book of business.

And I can see doing it one time. You know, I am selling off the business. I am turning it over to my kids, whatever you want to do. But on a year-by-year basis, that would be a degree of complexity that would require a higher marginal cost for tax planning.

Dr. Hoopes, I think your analysis, just in the real world, sounds better than Professor Gamage’s—more accurate.

One more thing I will say is, obviously Dr. Disney’s income is passive, and in the case of this gentleman, his is active. And along the way, I have found multiple people in whom he has invested—in their business. He never told me; they told me. And then they end up doing very well.

So when you actually have to work your wealth, you create wealth for others. That is different, I suppose, from passive wealth.

Let me finish with my closing remarks. I thank all the witnesses for a very informative meeting. We had a great deal of promise about the benefits of new taxes, but I think our discussion highlights that there is no such thing, no such thing as a tax that does not hit workers, consumers, and investment. Mr. Hodge, in his comments, said there is a balance there between equity, between revenue for the government, and between investment.

As we recover from the pandemic, businesses seek certainty and predictability so they can get back to normal. Congress should work to get the economy back to normal, back to the economy we enjoyed prior to COVID, which was done by lowering taxes, not by threatening to have higher taxes.

Thanks again to Chair Warren, and to all the witnesses today. I yield my time.

Senator WARREN. Thank you, Senator Cassidy.

You know, we’ve talked a lot about tax reform today. Tax reform is just about choices. We can let our roads and bridges crumble, not upgrade broadband, make no investments in child care or getting lead out of drinking water, and let rich people keep paying taxes at about half the rate as everyone else.

Or, we could ask those at the very top to pay a wealth tax. We can require giant corporations to pay a tax on book profits. We can get serious about tax enforcement for the rich and powerful.

Those three changes in the tax code would give us trillions more than we need in order to pay for President Biden’s infrastructure plan, and his care economy plan. It is all about choices.

So let me ask you, Ms. Straughter, what kind of difference would it make to close these multimillion-dollar tax loopholes, and instead invest that money in communities like yours?

Ms. STRAUGHTER. I think if more members of Congress walked the streets as I do, as ordinary—and not to say that Congress is not ordinary—but as the lay people who are out here working day by day, paying taxes, this would make a tremendous difference in our communities. Whether they are communities of color, commu-
nities that are rural that might not be of color, when we think about the division between the haves and the have-nots, it is huge. To not pay taxes is something that should not occur. To hide your tax money should not occur. To have multiple levels of ways of paying and not paying taxes should not occur.

So we need this in our communities. We need the taxes to be equitable and equal among everyone.

Senator Warren. So let me ask you, Ms. Straughter, what does it mean to you to pay taxes?

Ms. Straughter. It means I am doing my fair share. I went to school. My grandchildren go to school. So taxes are necessary. They are necessary for services. I do not want to say I enjoy paying taxes, but I understand why I pay taxes. It is a requirement of civilized society to take care of themselves and take care of others.

So I pay my taxes, you know? If not on time, I get an extension, but I pay my taxes.

Senator Warren. Good for you. You know, the tax system has been tilted towards the wealthy and powerful for far too long. And America's families have paid the price. So let's unlock a brighter future for our Nation by finally making this tax system work for working families.

I want to say a very special "thank you" to Ranking Member Cassidy for his help on this committee hearing today. Thank you to our witnesses, every one of you, for being here today and for providing testimony. For Senators who wish to submit questions for the record, those questions are due 1 week from today, on Tuesday, May 4th.

For our witnesses, you have 45 days to respond to any questions, and thank you again for volunteering your time, for being here.

And with that, this hearing is adjourned.

[Whereupon, at 4:38 p.m., the hearing was concluded.]
Thank you, Chairman Wyden, Subcommittee Chair Warren, and Ranking Member Crapo.

First, let’s acknowledge that conservatives and liberals both want what’s best for our country. We wish to have prosperity for those who are doing less well. But we have different visions of how to achieve that goal.

Conservatives believe in allowing the American people to keep their own resources and to make the decisions that are best for them; that allowing markets to dictate—with safeguards from Federal and State government—where money should best be allocated is what gave us prosperity to date and which is most likely to give us prosperity in the future.

It’s not just we who have seen that, however. We can even see countries which are frankly more socialist or communist evolve towards this path, whether it is the Czech Republic or China, or countries that have tried wealth taxes like what we will discuss today—Sweden, Austria, Denmark, Germany, Netherlands, Finland, Iceland, and Luxembourg—but have abandoned them.

The left has a different view: that it is better to take the resources of the American people and filter them through government bureaucracy that will make decisions as to where to spend, and the American people will thereby benefit from the government’s decisions more than if they were allowed to spend as they see fit.

Now those on the left will object. “Hold on a second. We are not talking about taxes on those who are less well-off; we are just talking about the very wealthy.” But this is disingenuous. Disregard that even the revenue from taxing every billionnaire in the country at 100 percent would not come close to what’s needed to fund their trillions of dollars in proposed new spending.

It is also disingenuous because it presupposes that those whom the left wants to tax are sitting on a pile of gold, like the dragon in “Lord of the Rings,” not using it for purposes that create jobs and otherwise bring prosperity, but rather just sitting on a pile of gold. Nothing could be further from the truth. That wealth is typically not liquid; it is invested and reinvested, creating jobs and wealth for others along the way.

Our first Supreme Court Justice John Marshall said, “The power to tax involves the power to destroy.”

We are not reinventing the wheel here. When you decrease taxes, you encourage investment, and jobs follow. When you increase taxes—sure you increase government control—but you discourage investment, and job numbers suffer.

Before COVID, Republican-led tax cuts spurred the greatest economy of our lifetime. We had record low unemployment for every demographic: black, Hispanic, non-Hispanic, high school drop outs, disabled, you name it. We had wage growth disproportionately in the lower incomes.

These may be inconvenient truths for some on the other side of the aisle, but truths none the less. We know what works.

Now let’s have a thought experiment. Let’s contrast the logical outcome of the two visions of the two parties. The left would like us to think that the disinterested bu-
reaucrat is able to make a wiser decision as to where to deploy capital than the person whose livelihood is dependent upon it.

In the private sector, if an organization providing a service fails, it’s on the dime of the company, and someone else steps up, takes the position to once more increase productivity, increase the number of jobs, and increase wages. That is what this hearing is about.

Now, think school teachers in Chicago. Those children were not allowed to be in class because the teachers’ union, against science, against the CDC, still would not reopen. And what did they get for that failure of service? They still demanded and received billions and billions for union priorities paid for by U.S. tax dollars. The bureaucracy condones and even promotes it.

Rather than talking about whether these new taxes are actually needed, we will hear about how they are justified. Successful individuals will be used as strawmen, pitting Americans against each other to build support for a political agenda. Success will be vilified. Undefined goals like “fairness” will be used as blank checks to justify their tax and spend agenda.

But what do you tell a family who loses their jobs because new taxes on the “rich and corporations” make their employer’s business model no longer viable? “It’s okay that you lost your job, because we really stuck it to the rich.”

The rich will do fine. They always do fine. But it is the everyday working folk who get caught in the crossfire of tax and spend policies.

And by the way, the left’s promise to expand transfer payments just creates more government dependency. Americans want independence, not dependence.

And this is the fundamental difference between our two parties. Republicans believe the best stimulus is a paycheck. A job is better support for your family than a government program.

The wealth tax is opposed by John Cochrane of the Hoover Institution to former Treasury Secretary Larry Summers—conservative to liberal. AEI, Tax Foundation, Brookings, and the Manhattan Institute have all reported on the negative aspects.

I hope the Biden administration will work with Republicans to get small businesses back on their feet so they can get Americans back to work and keep the economy moving in the right direction.

We will not tax our way to prosperity. Small businesses and other employers want to operate under a fair, predictable tax code, and they will do the rest.

There are some substantive things we should be discussing here. Some tax relief afforded to the middle class and small businesses through the Tax Cuts and Jobs Act expires in just 4 short years. My Republican colleagues and I have proposed providing predictability to taxpayers by locking in the current individual tax policies on a permanent basis, including the expanded Child Tax Credit and lower tax rates on the middle class. This will help everyday Americans.

I look forward to hearing the testimony.

PREPARED STATEMENT OF ABIGAIL E. DISNEY, PH.D., CEO AND CO-FOUNDER, FORK FILMS

Thank you, Chair Warren, Ranking Member Cassidy, and members of the committee.

When a person is born in this country it pretty much goes the same way every time. You come out, you get a little slap on your tushy until you cry, and then you get handed over to your parent. But when a baby is born into a family like mine, there is a little twist. You come out, you get a little slap on your tushy until you cry, and then before they hand you over to your parent, the doctor looks deep into your eyes and says, “never spend capital.”

Okay, so maybe I am exaggerating a bit, but not spending capital is as close to a religion among people who inherit wealth as you can get.

Why is capital so sacred? Because it is the goose that lays the golden egg. The more capital you have, the more income and growth you can count on, the more stuff you can buy, and so on. As long as you can invest for a return that outpaces
inflation, your capital will grow and your buying power will grow with it, and you can leave this life with money to spare.

The subtext of the “never spend capital” mantra is, of course, that jobs are for chumps. If you ever find yourself reduced to earning your living by your labor, you’ve surely lost the big lottery you were born to win.

But back in 1960, when I was born, there was another point of faith among the industry of people who advise inheritors like me, and that was summed up in the phrase “shirt sleeves to shirt sleeves in three generations.” Put another way, this means that if you procreate at a normal rate, you’ll be unlikely to keep this whole scam going for very many generations. Because if you have four children, as my parents did, you are going to have to at least quadruple the amount you were left to leave them where you were when you started. That’s why dynasties are unnatural and hard to cultivate.

But I’m third generation. Why am I still flying so high?

Things have changed since I was born 61 years ago. For one thing, my father had the good sense to see that the goose laying his golden eggs was dying in the early 80s and was able to bring about changes in management that unleashed an enormous amount of pent-up value at the Walt Disney company, and that caused the stock to rise dramatically. Disney’s share price was also bolstered by a stock market that was known occasionally to suffer from, in Alan Greenspan’s words, an irrational exuberance.

So in other words, I’m flying high because of dumb luck. I did nothing to earn my massive windfall except have the good sense not to sell my particular golden ticket. I’ve owned my way to the top.

But there is a second reason, more pertinent for our purposes today. I’m in great shape today because a lot of what the government did in the last 40 years was designed to ensure that a person like me can stay flying high, in spite of all the natural forces of gravity that used to pull inheritors down to earth.

Those government actions include:

One. Corporate taxes are at an all-time low, and shameless corporate tax avoidance at an all-time high. Trillions of dollars are currently being stashed overseas in tax havens by Fortune 500 companies in ways both quasi-legal and potentially criminal. All of this value accrues once again to managers and to shareholders like me. And let’s be clear: there is nothing democratic about owning stock. Eighty-four percent of shares, in fact, are owned by the wealthiest 10 percent of the population.

Two. Profitability has skyrocketed at America’s corporations. For one thing, while worker productivity is up 250 percent since the end of WWII, mean wages have increased by only 60 percent of that amount. Much of the rest of that value is accruing to managers and to shareholders like me.

Three. Corporations buying back their own shares, a practice that was illegal until the early 1980s, has turned into business as usual among American companies. Rather than reinvest in the growth of their business or rethink salaries of their employees, companies are plowing profits and tax savings into buybacks that enrich only—you guessed it—managers and stockholders like me.

Four. An entire tax avoidance industry has grown up in the meantime advising individuals and families about how to minimize their tax obligations, in ways that skirt right around the edges of the law.

Five. A no-holds-barred assault on public spending has included the evisceration of the IRS, the SEC, and other regulators that might be more able to restrain some of this trickery if they had adequate funding and support.

Six. The finance industry, once populated by bow-tie-wearing poindexters bent on ensuring that grandpa’s pension was well taken care of has transformed into Godzilla himself, devouring and warping every industry and motivation it lays its claws on. Relying on ever more arcane investment rules and vehicles, the industry counts on the widespread inability of the general population to understand what they are up to in order to carry on lining their pockets with relative impunity.

And by the way, if you’re pretty smart and still have trouble understanding most of it—don’t blame yourself, that’s by design.

Seven. Corporate and individual spending on lobbying and on political campaigns have warped and changed our political processes, making some representatives
opaque, corrupt, and downright uninterested in the well-being of the regular folks paying the price of their machinations.

When I was born in 1960, the U.S. had a tax system that privileged income from labor over income from wealth. But somewhere along the line, things turned upside down.

Now a person like me pays less in taxes on the money I make simply from owning stuff than almost anyone who is making their money by working. The more likely a person is to come home from work with an aching back, the more likely I am to be paying less in taxes. You don’t have to be a Marxist to see that something is really wrong with these priorities.

If a tax system is a statement of a country’s values, then I wonder about ours.

In 1960, a middle-class worker could count on an income that enabled them to buy a home, a pension that would take care of them in retirement, and adequate health care.

In 1960, before massive disinvestment in public welfare, that person could send a child to a decent public school, spend weekends at safe and pleasant public parks, and drive to work on roads that were neither crumbling nor overcrowded.

For the last 50 years the wealthy in this country have continued to press their advantages. Their aggressive lobbying on their own behalf has resulted in a raft of changes both formal and informal that have resulted in an accumulation of wealth in the hands of an ever-narrowing segment of the population. And wealth has a self-reinforcing quality, especially given the unholy relationship our political culture has with money.

Some inequality is, of course, inevitable. But the levels of inequality that now characterize American life are historic. In 1960 the top 0.1 percent of owners controlled about 10 percent of the wealth in this country. Today the top 0.1 percent control over 23 percent.

And the pandemic has only exacerbated this problem. Wealth among U.S. billionaires has grown by over $1.3 trillion just over the past year, an amount that would cover a $3,900 stimulus check for every American citizen.

There are those who argue that the massive inequality we now face is fine, no problem, nothing to see here. But history tells us that such massive inequality is invariably correlated to corruption, unrest, and failed governance. And every indication is that the U.S. will be no exception should we allow these trends to continue.

And I can tell you from personal experience that too much money is a morally corrosive thing—it gnaws away at your character, it narrows your focus down onto your own well-being, it warps your idea of how much you matter, and rather than make you free, it turns you fearful of losing what you have.

The truth is, the rich have run amok over the last 50 years of American history, and our government’s willing complicity in their antics has permitted a handful of egregiously wealthy human beings to accumulate massive, budget-warping, mind-blowing amounts of money—all at the continuing expense of the vast majority of the American people.

We need to address inequality first by restoring to the working class the benefits that used to come with being any old American citizen: decent, high-functioning governments, good health care, a public school system that prepares all kids well for their futures, an infrastructure not in a perpetual state of decay, and a suite of public services that privileges the interests of those not already privileged in every other way.

Given how far we have let this inequality grow, I do not see how we can address this problem other than with a wealth tax. Working people will never, by wages or salary alone, be able to catch up with the folks who have succeeded in putting so much distance between themselves and everyone else. The public needs revenues to restore the commons to its former health, and the wealthy have too much money, plain and simple. That adds up to a pretty obvious solution.

I will go to bat for the wealth tax with any and all businessmen who want to tell you that it impinges on the American dream. If you have $50 million and do not know how to invest it for more than 2-percent growth, you have bigger problems than a wealth tax.
If you have a billion dollars and don’t know how to live on $999 million, you don’t need a better tax system, you need a psychiatrist.

QUESTIONS SUBMITTED FOR THE RECORD TO ABIGAIL E. DISNEY, PH.D.

QUESTIONS SUBMITTED BY HON. BILL CASSIDY

ESTATE TAXES

Question. Senate Majority Leader Schumer has stated, with regard to the estate tax... any organic business—a farm, a small business, and frankly a large business—that would have to be broken up because of the extent of the tax should not be. A business is an ongoing organism. It employs sometimes 10 people and sometimes 10,000 people. To have to break that business up to pay any tax, to me, is counterproductive.

Do you agree that the tax code should not inhibit owners of any size business from being able to pass along that business, in full, to future generations?

Answer. In fact, you are asking two unrelated questions. On the one hand, you are asking whether businesses should be broken up to pay estate taxes when inheritors have no access to other cash or assets with which to do so. If that is the question, then my answer is “no.” That would be a terrible thing, as a business is an ongoing, important organism that creates jobs and opportunities for more than just inheritors.

That phenomenon, widely repeated in stories about the estate tax, is, in fact, rare. Since the estate tax only applies to estates with assets worth more than $11.7 million, and since only fewer than two out of every 1,000 estates in 2019 qualified to pay the tax at all, this is not a widespread or common problem by any definition. In the rare case when such a large estate includes a growing concern and yet has no access to any liquidity, I would suggest that the inheritor has bigger problems than just a looming tax bill.

Liquidity is, I am sure you know, often a question of timing. Estates get up to 9 months to pay their taxes, estates that include farms and small businesses that make up more than 35 percent of the corpus get up to 35 years to pay the tax. In fact, when this provision was added to the tax code in 2017, Susan Collins told The Wall Street Journal1 that “We’ve taken care of the problem for the vast majority of family-owned businesses or ranchers in the country.”

The second question you seem to be asking is implied in the words “in full,” and that question is whether or not businesses should be taxed at all if they are part of an estate. And my answer to that is an emphatic “yes.”

Some clarification is needed here. To start, the business would not be paying a tax—the estate would, and those are two entirely different things since most estates include businesses as only one part of the assets that make up their total value. And my answer to the question of whether or not an estate worth far more than the assets the vast majority of Americans own at their death should be taxed is an emphatic “yes.”

As I’ve said before, this tax only applies to people who are by definition more than able to pay it. People who have amassed this much wealth in their lifetimes have done so by availing themselves of all the public goods and services this country has to offer—often a higher proportion of those resources. Transportation, education, high functioning court systems, and government subsidies are far more heavily used by the fortunate and wealthy than by low-income and working-class people.

More importantly, I answer with an emphatic “yes” because of the kind of country I thought I was a part of—the kind of country I was taught America aspired to be. That kind of country is a meritocracy. The America I grew up in taxed a worker less for labor than an owner for ownership, admired a builder more than a billionnaire, and believed that anybody anytime should be able, with work and a fair set of rules, to become the best possible version of themselves.

What we currently have, and lurch ever closer toward, is a society dominated by dynasties, by a class of people that start with such a massive head start that it would be impossible for anybody less fortunate to gain any ground on.

Roughly 40 percent of the names on the Forbes 400 list of the richest people are people who inherited a sizable asset from a spouse or family member; 21.25 percent of the Forbes 400 inherited enough to make the list without lifting a finger; 17 percent have other family members on the list.

The playing field isn’t just uneven. It’s a minefield for most Americans given high incarceration rates, failing public schools, and a job market that consigns 40 percent of American workers to below survival wage jobs.

The America I dream of is fair. But my advantages have not been. And my philanthropy is a drop in the bucket against the structural challenges that need addressing before it will ever be fair.

I do not want to live in a dynastic social structure, but we are fast on our way to building one, and the estate tax is one of the last taxes in place that at least uses some of the excess resources of those who do not need them to address the needs of other people who very much do. I’m pretty sure most Americans would agree with me.

DOUBLE TAXATION

Question. New York Democratic Representative Jerry Nadler recently tweeted, “No one should ever be taxed twice on the same income. It’s not fair and it’s not just.”

Do you agree with this view? If not, why not?

Answer. Representative Nadler has a point, it would be a terrible injustice for someone to pay the same income tax twice or the same capital gains tax twice.

But the government does reserve the right to tax transactions. That is where most of the revenues to do things like build roads and schools come from.

When I buy gas, I pay a tax. When I buy food, I pay a tax. No one asks me if the money I am using to pay for those things has already been taxed. The money I use to buy things sits most of the time in a bank account which is filled periodically by proceeds from work that I’ve done, assets that I own, and all sorts of other kinds of income.

These dollars arrive in my account due to many kinds of transactions—a sale, a dividend, a paycheck. Each of these is a separate and individual exchange of value for the value that the government taxes in exchange for the goods and services it provides to ensure that that transaction and the society within which it happens is running smoothly.

Besides, money is fungible, usable for any purpose in a uniform and indistinguishable way, and therefore impossible to distinguish as “already taxed” or “not yet taxed?” Money is just . . . money?

And isn’t an estate tax a tax on just another transaction, the transfer of assets from the deceased person to their heirs? So why should it matter if some of it was already taxed during a previous and unrelated transaction? It’s a sad transaction, of course, but a transaction, nevertheless. And the government does reserve the right to tax transactions.

What’s more, many estates are made up of appreciated assets—assets, in other words, that have never been taxed. But if, for instance, your estate owns a lot of shares in a car company, and if those assets are worth more today than they were worth in, say, 2009, that means that they would have been helped along by a massive government bailout that prevented the failure of that business along with many others. So, your shares rose alongside the rest of the stock market.

The money for that bailout, it should be emphasized, came out of the pockets of many other hardworking taxpayers who never were consulted about whether or not that car company should get that bailout nor about any other aspect of where massive government support for corporations has gone. These are taxpayers, many of whom are paying a higher marginal tax rate than I am, even if the only way I make my money is by lying around on my couch waiting for the checks to roll in.

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1 https://d3n8a8pro7ohmx.cloudfront.net/ufe/legacy_url/410/BornOnThirdBase_2012.pdf?1449056427.
If an estate has grown as the result of government intervention, does it not seem fair to you that that estate at the very least should pay its debt back upon the death of its beneficiary before it is passed along to anyone else?

**GIFTS TO THE U.S. TREASURY**

*Question.* In your written testimony you wrote, “And I can tell you from personal experience that too much money is a morally corrosive thing—it gnaws away at your character, it narrows your focus down onto your own well-being, it warps your idea of how much you matter, and rather than make you free, it turns you fearful of losing what you have.”

Current law allows for donations to the Treasury. Do you think that’s a viable option for those who are worried they have too much money?

*Where do you think is the correct place to draw the line in terms of how much is too much money?*

*Answer.* Thank you for your helpful suggestions here, Senator. I will take them under advisement. I feel the need to point out that I have given much of my wealth away and continue to labor away at the surprisingly hard work of giving it away well.

I don’t imagine I will be done until most of it is gone.

Of course, my philanthropic gifts are optional, whereas a tax is an obligation. There is a reason that, in some cases, taxes are referred to as “duties.”

I love writing a check to the IRS no more than the next person, but I do so gladly because I would be foolish to pretend that my wealth has nothing to do with a robust system of public goods and services.

My wealth is still my wealth, due to various things like a high-functioning legal system to protect me from theft, a publicly supported education system to draw a diversity of employees and colleagues, and a relatively satisfactory infrastructure which helps me, my colleagues, and the people who might watch the films that support the share price that keeps me wealthy get from place to place.

I hope that the checks that I gladly, if not joyously, write to the IRS grow in size because I know for a fact that I do not pay my fair share for these public goods.

What's more, I am painfully aware that because I do not pay my fair share, many people less fortunate than I end up shouldering the burden of an overstressed legal system, a public education system in steep decline, and a crumbling infrastructure.

Shouldering, in other words, my burden.

I find myself getting more comfortable every day as my brothers and sisters working minimum wage slowly sink into unacceptable poverty.

There is a level of poverty that is identifiable and unacceptable, just as there is such a thing as too much wealth. Easier, in fact, to identify. And easier, if we are willing, to address.

I would love to tell you what the precise level of wealth is that corrodes character.

And I am sure, were I to identify a specific amount, say, 50 million dollars, there would be heartbreaking cases of people right on the bubble who are hurt by that definition and would argue for it to be raised or lowered. Such has always been the case.

Wouldn’t it be wonderful if we could tailor our laws, laws with life-or-death consequences such as three-strikes laws, the death penalty, or abortion laws, to specific circumstances so that heartbreaking unintended consequences never arose?

But, alas, heartbreaking unintended consequences have a way of arising despite our best intentions.

Reasonable people can argue about the fairness of the application of laws. Still, sometimes circumstances lie so far outside of the spectrum of what might be called reasonable that to quibble about where the line might be would be a waste of our time. Such is the wealth we have seen build up in the hands of an ever-smaller group of billionaires.

Lest you think I exaggerate, consider that from 1982 to 2011, the net worth of the individuals on that Forbes list had increased by 15 times and that the cut-off for the list went from $75 million to over a billion.
I can’t tell you where wealth ends, and obscene wealth begins; I am content to let the politicians fight that out, but I do know that if a person has a billion dollars and they cannot find a way to live on $999,999,999.99, they don’t need better wealth definitions, they need a psychiatrist.

PREPARED STATEMENT OF DAVID GAMAGE, PROFESSOR OF LAW, MAURER SCHOOL OF LAW, INDIANA UNIVERSITY

Thank you, Senators, for your invitation to speak with you today. I am a professor of tax law at Indiana University Bloomington’s Maurer School of Law. I previously served in President Obama’s Treasury Department, in the Office of Tax Policy. I have advised on and helped draft a variety of tax reform efforts at the Federal and State and local levels. I have published over seventy articles and academic essays on topics related to tax reform.1

I am primarily devoting this written testimony to discussing the Ultra-Millionaire Tax Act of 2021 and the broader case for levying a Federal tax on extreme wealth holdings. As is well known, both wealth and income inequality have exploded over recent decades, with the gains from economic growth disproportionately going to the richest Americans.2 Meanwhile, as I will explain, our tax system is broken as applied to the ultra-wealthy, with many harmful consequences. A new Federal tax on extreme wealth holdings, like the Ultra-Millionaire Tax Act, should be a central component of reforms for fixing this disgraceful state of affairs.

Secondarily, I will more briefly write in support of both the Real Corporate Profits Tax Act of 2021 and proposals for improving IRS funding and for making it and other tax-enforcement funding less dependent on the annual appropriations process. All of these proposals go together as reforms for raising revenues needed for public investment while helping to fix some of the ways in which our tax system is currently broken and easily exploited by tax gaming by ultra-wealthy individuals and families and by large corporations. For the reasons I will explain, I strongly support all of these reform proposals.

I. THE CASE FOR A NEW FEDERAL TAX ON EXTREME WEALTH HOLDINGS

A. The U.S. Tax System Is Broken as Applied to the Ultra-Wealthy, With Many Harmful Consequences

The U.S. tax system does a very poor job of taxing the ultra-wealthy.4 The ordinary rich—say, well-compensated doctors—typically pay quite a lot of income tax, doing their part to support the Nation. By contrast, most billionaires and mega-millionaires pay tax on only a small portion of their true economic gains. Indeed, many working-class individuals, such as nurses, teachers or firefighters, pay tax on a much larger share of their economic gains than do most of the wealthiest Americans.

So how do billionaires and mega-millionaires escape paying their fair share? The answer is that our income tax generally does not reach large fortunes unless property is sold, or money is paid out in salaries or in stock dividends. Thus, by borrowing against appreciated assets and playing other financial games, the very rich can avoid taxation and still fund their lavish lifestyles.

1Most of my published and forthcoming scholarship can be found on SSRN, here: https://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm?per_id=364730. My academic bio and CV can be found here: https://www.law.indiana.edu/about/people/bio.php?name=gamage-david.


3This Section presents a summary of the analysis in Parts I and II of my forthcoming article, co-authored with John R. Brooks, Tax Now or Tax Never: Political Optionality and the Case for Current-Assessment Tax Reform, 100 N.C. L. Rev. (forthcoming), available at https://ssrn.com/abstract=3801164. Further support and elaboration of the arguments and analysis in this Section can be found in that Article.

4I use both the term “ultra-wealthy” and the phrase “billionaires and mega-millionaires” in this testimony to refer to households in the top 0.1 percent (more or less) of wealth in the United States, a group that is estimated to consist of approximately 175,000 households who collectively own between 15 percent and 20 percent of national wealth. Id. at 11–13.
Most Americans predominantly earn wage and salary income, which the U.S. income tax measures reasonably well. By contrast, the ultra-wealthy predominantly earn income that arises from the returns to owning wealth (or that can be made to appear as though it arises from the returns to owning wealth), which the U.S. income tax measures dreadfully.

This deep failure of the U.S. tax system has profound implications beyond just the resulting windfall for the ultra-wealthy. To begin with, this failure undermines the fairness of the entire tax system, especially by creating obstacles for members of historically disadvantaged groups to catch up to those who were born into greater privilege. As Palma Strand and Nicholas Mirkay—among many others—have documented, the Federal income tax operates "directly to increase wealth inequality, deepening preexisting historically based racial wealth disparities." Specifically, by heavily taxing wage and salary incomes, and only lightly taxing the returns to owning wealth, the tax system obstructs historically disadvantaged groups from building wealth and economic power, while protecting the comparative economic power of historically advantaged groups that started accumulating financial wealth and related social capital during more illiberal periods.

Beyond that, the failure of the U.S. income tax to meaningfully tax the ultra-wealthy creates massive inefficiencies and economic waste. The tax gaming strategies that ultra-wealthy taxpayers use to escape income taxation come at a cost, and these costs generally increase as the strategies get more complicated and aggressive to cover more economic income. Examples of these costs include reduced liquidity, the costs of taxpayer borrowing, transaction costs of tax-loss harvesting, deviating from taxpayers’ risk-reduction and diversification preferences, the excessive complexity of more sophisticated forms of tax gaming, and the cost to businesses from using inefficient capital structures in order to generate tax savings. As C. Eugene Steuerle explained in his seminal book on the topic, “insofar as capital income is concerned, the individual income tax is primarily a discretionary tax.” As a result, at least with respect to the investment income of the ultra-wealthy, the income tax is effectively just a tax on the limitations to tax gaming that deter wealthy taxpayers from gaming away all of their tax liabilities, so that “the discretionary income tax on capital income is a tax on liquidity, risk reduction, and diversification rather than a tax on income.”

A key takeaway here is that tax gaming by the ultra-wealthy typically involves real economic costs and so the flaws in the income tax harm the overall U.S. economy. While incurring these costs may be rational for individual taxpayers, it is exceedingly wasteful to an economy as a whole. In other words, the productive potential of the overall economy is diminished because scarce resources are devoted to tax gaming at the expense of productive investment and business activity.

Furthermore, the manner in which the personal income tax is broken and readily exploited by the ultra-wealthy’s tax gaming undermines the administrability of the entire tax system. This is because the ways in which the income tax fails with respect to the ultra-wealthy harm the integrity and functioning of the overall tax

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6 Id. at 4–8.
9 Id. at 279.
12 Id. at 19. My co-author John Brooks and I would add lack of complexity to Steuerle’s list, as we view the excessive complexity of tax-motivated investment strategies as perhaps the largest form of economic waste, because this complexity interferes with designing investment and business strategies so as to maximize economic productivity and related pre-tax returns. Gamage and Brooks, supra note 3, at 29.
13 Gamage, supra note 10, at 375–82.
system, generating excessive and unnecessary legal complexity and uncertainty to the detriment of a great many small businesses and ordinary Americans.

Finally, on top of all that, tax gaming by the ultra-wealthy deprives the government of much-needed revenues that could be used to fund public investment, undermines the public’s tax morale and compliance norms, and likely also harms the public’s faith in our overall economic and political system. For these and other related reasons, it is crucial that the tax system be reformed so that the ultra-wealthy cannot so easily escape paying their fair share. The revenues at stake are large and needed. But the many real social and economic harms that result from the ways in which our tax system is currently broken as applied to the ultra-wealthy are even stronger reasons for why we urgently need reform.

B. Limiting the Capital Gains Rate Preference and Stepped-Up Basis on Death Are Only Partial Fixes for the Deep Flaws in the Income Tax

President Biden is reportedly proposing to raise the top capital gains tax rate so as to end the capital gains rate preference for taxpayers with income over $1 million and also limiting the special-preference provision that steps-up basis upon death. If enacted, these reforms would be important partial steps toward fixing the deep flaws in the U.S. tax system and alleviating the harmful consequences of those deep flaws.

Unfortunately, as my co-author John R. Brooks and I explain in a forthcoming article, both history and theory imply that these reforms are unlikely to be fully successful or politically sustainable on their own. This is because the structure of the U.S. political system cretes pressures that tend to undermine reforms of this sort over time, making such reforms politically fragile, unless the reforms are accompanied by current-assessment reforms like an annual wealth tax.

These pressures include that Federal budget rules make it so that much of the tax revenue that might theoretically be raised by reforms like the ones President Biden is proposing—if those reforms were sustained—will show up outside of the budget scoring window. This then makes it much more politically difficult to legislatively bolster and strengthen such reforms, while making it much easier politically for future Congresses to legislatively weaken or repeal such reforms. Indeed, absent an accompanying current-assessment reform, a future Congress might well find that proposals for undoing Biden’s reforms by partially reenacting the capital gains rate preference would be scored as raising tax revenue within the relevant budget window, despite that the true effects would be large revenue losses outside of the budget window.

Moreover, because President Biden’s reforms would mostly retain the realization-based nature of the income tax, ultra-wealthy taxpayers would mostly continue to enjoy the choice of when to realize their tax liabilities—that is, when to exercise the option value of deciding in which future political regime a deferred tax liability would be realized, assessed, and paid. This creates strong incentives for ultra-wealthy taxpayers both to wait for (favorable to them) future legal or political changes and to lobby and exert other political pressures in the hopes of creating such future changes.

For these and related reasons, President Biden’s proposed reforms of limiting the capital gains tax rate preference and limiting the special provision offering step-up of basis upon death should be thought of as important steps toward fixing the personal tax system with respect to the ultra-wealthy, but not as complete solutions. A complete solution requires a current-assessment reform like an annual wealth tax, to accompany reforms like those proposed by President Biden.
C. An Ideal Tax System Should Tax Both Income (or Consumption) and Wealth

There are two major groups of philosophical theories about what a democratic nation should ideally tax. The first group of theories looks to taxpayers’ ability to pay. The second group of theories looks to the benefits that taxpayers receive from the State. Both groups of theories strongly support taxing both income (or consumption) and wealth, at least as an ideal matter.

Beginning with theories based on ability to pay, consider three sample taxpayers: imagine that in a given year that Taxpayer A has $50 million of wealth and $10 million of income, whereas Taxpayer B has $50 million of wealth and $1 million of income, and Taxpayer C has $20 million of wealth and $10 million of income.

Can there be any doubt that Taxpayer A has greater ability to pay as compared to either Taxpayer B or Taxpayer C? The reason that Taxpayer A has greater ability to pay is that both wealth and income are sources of economic power and well-being. All else being equal, having more of either wealth or income makes someone better off in the sense of ability to pay.

Over an infinite time horizon, wealth and income are highly related, and it is often said that income equals consumption plus changes in wealth. But neither humans nor tax regimes survive unchanged over infinite time horizons. As John Maynard Keynes famously quipped, “In the long run we are all dead.” Similarly, in the long run, tax rates and other tax rules will inevitably be changed. Thus, when considering ability to pay, the short run matters. And, in the short run, wealth and income provide distinct information on taxpayers’ ability to pay.

Moving on to theories based on benefits that taxpayers receive from the State, among the most important of such benefits are the protections the State provides to both accumulated wealth and to newly earned gains in the forms of military and police protections and protections from the legal system. Absent such protections provided by the State, it would be difficult and dangerous to accumulate and maintain billions or mega-millions in wealth. It would also be difficult to earn new millions or to increase the worth of one’s prior wealth holdings.

Much more could be said about the philosophies of what a democratic government should ideally tax. But this short discussion should suffice to explain why the major philosophical theories support that an ideal tax system should tax both wealth and income (or possibly both wealth and consumption instead).

Indeed, we can see an example of these justifications in the fee structures charged by private equity financiers. The typical fee structure charges both a 2-percent management fee on the total wealth invested plus an additional 20-percent fee on the profits earned from managed investments.23 There is good reason for this dual fee structure, on both the wealth invested and the income earned from that invested wealth. Private equity fund managers provide services both in the form of protecting and sustaining prior wealth accumulations and in the form of helping to grow new income from that wealth. The same is true of the services and benefits that the State provides to taxpayers—these services both help protect prior wealth accumulations and help with the earning of new income.

Overall then, when comparing two taxpayers who both have the same annual income, if one has much greater wealth, then—all else being equal—the taxpayer with much greater wealth should pay more tax.

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D. A Wealth Tax Is Definitely Constitutional

Despite misleading statements sometimes made to the contrary, the Constitution clearly and unambiguously grants Congress the power to levy an annual wealth tax. For sure, there are constitutional uncertainties surrounding wealth tax proposals, and there is no guarantee that the Supreme Court would uphold any particular design for an annual wealth tax. Nevertheless, it is important to understand that Congress clearly has the power to levy an annual wealth tax, and that the constitutional uncertainties are only in regard to how such a tax must be designed.

The primary question is whether the Constitution and Supreme Court precedent authorize a uniform wealth tax, or whether instead an annual wealth tax would be considered to be a form of direct tax that must be apportioned amongst the States by population. There are mixed Supreme Court precedents on this question. On the one hand, the holdings of two notable Supreme Court cases—the 1895 case of Pollock v. Farmers’ Loan and Trust and the 1920 case of Eisner v. Macomber—suggest that an annual wealth tax might be considered to be a direct tax that must be apportioned. However, both of these two Supreme Court cases have been at least partially overturned by subsequent Supreme Court decisions. Moreover, there is a long line of Supreme Court precedents supporting that an annual tax on extreme wealth holdings like the proposed Ultra-Millionaire Tax (in contrast to a tax based solely on the ownership of property itself like local government property taxes) should be considered a form of excise tax (as in the Supreme Court decisions upholding the corporate income tax and estate and gift tax, among others), that would not need apportionment. All sources considered, the most faithful interpretation of the overall body of Supreme Court precedents and of constitutional structure and history supports that the Supreme Court should uphold a uniform tax on extreme wealth holdings rather than requiring that it be apportioned.

Of course, the Supreme Court could decide otherwise, such as by reviving Pollock v. Farmers’ Loan and Trust or Eisner v. Macomber to require that a tax on extreme wealth holdings be apportioned amongst the States by population. But all this would mean is that the wealth tax would need to be so apportioned. Congress passed five different apportioned Direct Tax Acts in the late 1700s and early 1800s, each levied on specific forms of wealth based solely on their ownership, so that these partial wealth taxes were considered to be direct taxes. To my knowledge, no one has ever disputed that these early Direct Tax Acts were clearly and unambiguously constitutional. Thus, these early Direct Tax Acts provide guidance and precedent for how we could design a modern apportioned tax on extreme wealth holdings.

There are some complexities involved in designing a modern apportioned tax on extreme wealth holdings, and I cannot fully explain all of the relevant detail here. My co-author John R. Brooks and I are in the process of developing comprehensive recommendations and analysis in an unfinished manuscript. Partial summary of our recommendations would be to follow the approach used by the 1798 Direct Tax Act which accomplished apportionment by combining uniform taxes on buildings and enslaved persons with a residual tax on land value within each State, with that residual tax structured to make the apportionment formulas work. We would recommend modifying this approach somewhat by accompanying a uniform

34 See, e.g., John R. Brooks and David Gamage, Why a Wealth Tax Is Definitely Constitutional, available at https://ssrn.com/abstract=3489997; United States v. Pratynski, 462 U.S. 74, 79 (1983) (explaining that “Congress’s power to tax is virtually without limitation” but that there is “one specific limit on Congress’s power to impose indirect taxes” and that limit is the uniformity requirement).
36 252 U.S. 189 (1920).
31 John R. Brooks and David Gamage, The Indirect Tax Canon, Apportionment, and Drafting a Constitutional Wealth Tax (unfinished draft manuscript available upon request).
33 It is inescapable that the apportionment clause was largely (if not entirely) designed to protect the horrendous institution of slavery from what slaveholders would have considered to be excess taxation, and so analyzing the historical precedents for designing an apportioned direct tax requires—as disturbing as this is—analyzing how “property” in the form of enslaved persons was then taxed.
34 Act of July 14 § 2, 1 Stat. at 598.
tax on extreme wealth holdings (like the proposed Ultra-Millionaire Tax) with a residual tax on all real property within each State that is valued for purposes of local government real property taxes, and then adding in a substantial circuit-breaker so that—for example—individuals and families with annual household income of less than, say, four hundred thousand dollars would be exempt from the residual tax. It is also worth considering giving State governments the option to pay the residual tax via requisitions instead of having the tax levied on real property within the State, as was done in the Direct Tax Acts of 1813, 1815, and 1816.33

If the additional tax revenues raised by this residual tax or requisitions were used to fund general Federal Government expenditures, then this structure would arguably be inequitable, because larger revenues would be raised from States with less wealthy populations and smaller revenues from States with more wealthy populations. But such inequities are easily remedied by spending the revenues raised by the residual tax or requisitions primarily within States with less wealthy populations. One way of accomplishing this would be to use the extra residual tax and requisition revenues to fund grants to State legislatures, with sufficiently larger grants given to States with less wealthy populations so as to resolve any inequities, similar to what is done by other Federal nations like Canada and Australia through their fiscal equalization regimes. Another approach would be to use the residual tax revenues to fund a spending program that would primarily benefit States with less wealthy populations—this is in a sense how the Medicaid program currently works. Perhaps the easiest solution would be to fund new income tax credits. Such new credits could be designed so that most Americans with, say, annual income of less than $400,000 would receive credits larger than their liabilities under the residual tax or requisitions, and with Americans owning real property and having higher annual incomes then paying for the difference. In that manner, the overall structure—of a residual tax or requisitions funding tax credits—could be made progressive while resolving any potential interstate inequities.

As this short discussion suggests, there are some complexities involved in designing an apportioned wealth tax and choices must be made about how to spend revenues so as to resolve potential inequities. But these challenges are all surmountable. Congress could design the apportionment regime as a fallback clause to be added to a uniform tax on extreme wealth so that the fallback apportionment regime would only go into effect in the event of an adverse Supreme Court ruling. Alternatively, Congress might opt to wait and see what happens, and only legislate an apportionment regime later if it becomes needed in the event of an adverse Supreme Court ruling. There are pros and cons to either approach. Either way, any revenues that might otherwise be lost from a potentially adverse Supreme Court ruling could be made up for either by making the fallback apportioned wealth tax retroactive to the date of the original legislation or by levying sufficiently higher wealth tax rates for the initial years following the apportioned wealth tax coming into effect.

Again, the key takeaway is that Congress clearly and unambiguously has the power to levy an annual wealth tax. The constitutional uncertainties about how such a tax must be designed create some complexities and challenges, but these challenges are fully and readily surmountable. Properly designed, a Federal wealth tax is definitely constitutional.

E. The Proposed Ultra-Millionaire Tax Would Be Both Administrable and Superior at Valuation as Compared to the Existing Income Tax

Valuation and measurement are key challenges in designing any form of taxation, especially with respect to ultra-wealthy individuals and families. The existing income tax does a reasonably decent job at measuring and valuing wages and salaries paid in money—the primary form of income earned by most Americans. But the existing income tax does an abysmal job at measuring and valuing the true economic gains of most ultra-wealthy taxpayers.

Consider that the best evidence from the economics literature implies that the existing income tax only ever reaches less than a quarter of the true investment income of most ultra-wealthy taxpayers.34 This is abysmal indeed.

For comparison, although the existing estate and gift tax has been much derided for how easy it is to game around and avoid, the best evidence from the economics literature implies that the existing estate and gift tax reaches about half of the true investment income of most ultra-wealthy taxpayers.34 This is abysmal indeed.
value of the wealth transferred by the estates of ultra-wealthy taxpayers. Over sufficiently long time periods, investment income and wealth become similar, and so while these estimates are not directly comparable, the measurements are comparable enough to conclude that the existing estate and gift tax probably does a better job of valuation and measurement with respect to ultra-wealthy taxpayers as compared to the existing income tax.

The proposed Ultra-Millionaire Tax would almost certainly be much better at valuation and measurement as compared to either the existing income tax or estate and gift tax (with respect to ultra-wealthy taxpayers). To begin with, many of the most important forms of tax avoidance games for escaping the estate and gift tax involve making transfers through trusts, and most of these sorts of games would be ineffective for escaping an annual wealth tax like the proposed Ultra-Millionaire Tax. Furthermore, the proposed Ultra-Millionaire Tax includes anti-abuse rules for limiting many of the valuation games most commonly used to avoid the estate and gift tax. Specifically, in accordance with the recommendations that I and others have made in prior writing, the proposed Ultra-Millionaire Tax authorizes the Treasury Department to require formulaic valuations based on proxy measurements, prospective measurements, or retrospective measurements, as best balances the goals of valuation accuracy, preventing gaming, and ensuring administrative and compliance ease for different categories of assets. Working with law professors Brian Galle and Darien Shanske and economist Emmanuel Saez, I have been developing a model set of valuation and enforcement rules for a wealth tax reform. The proposed Ultra-Millionaire Tax authorizes the Treasury Department to review and adopt our model rules or perhaps to develop superior alternatives.

Ultimately, no form of taxation is completely immune to tax gaming responses, especially by ultra-wealthy taxpayers. But a proposal for tax reform should not be compared to some impossibly perfect ideal, but rather to plausible real-world alternatives. In that light, the proposed Ultra-Millionaire Tax is almost guaranteed to do a much better job at valuation and measurement with respect to ultra-wealthy taxpayers as compared to either the existing income tax or estate and gift tax. Moreover, because many of the tax gaming responses to a wealth tax would be distinct from the responses to an income tax, the overall costs of tax gaming can be minimized by levying both a wealth tax and an income tax (or, alternatively, both a wealth tax and a progressive consumption tax).

36 Jason S. Oh and Eric M. Zolt, Wealth Tax Design: Lessons From Estate Tax Avoidance, UCLA School of Law, Law-Econ Research Paper No. 20–01, at 1, available at https://ssrn.com/abstract=3526515 (“Second, other structures . . . work well to minimize estate taxes but are of limited use for structuring around an annual wealth tax. Projecting wealth tax revenue using estate tax revenue without considering the revenue consequences of these strategies will underestimate wealth tax revenue.”).
37 See Sec. 2902(d), authorizing the Treasury Department to establish valuation rules that may utilize "retrospective and prospective formulaic valuation methods" and which may "require the use of formulaic valuation approaches for designated assets, including formulaic approaches based on proxies for determining presumptive valuations, formulaic approaches based on prospective adjustments from purchase prices or other prior events, or formulaic approaches based on retroactive adjustments, adding deferral charges based on eventual sale prices or other specified later events indicative of valuation" and which may prohibit "the use of valuation discounts.".
39 Sec. 2902(d).
40 An explanation of a work-in-progress draft of these rules, as tailored for a wealth tax reform proposal designed for the State of California, can be found here: https://eml.berkeley.edu/~saez/galle-gamage-saez-shanskeCAwealthtaxMarch21.pdf.
41 In addition to the more general reasons why levying two tax instruments with distinct gaming responses (such as both a wealth tax and an income tax) reduces the overall costs from tax gaming—as explained in Gamage, supra note 10—it is also the case that generating annual information on taxpayers’ wealth assists in the enforcement of both an income tax and an estate and gift tax. See Jean-Blaise Eckert and Lukas Aebi, Wealth Taxation in Switzerland, Wealth Tax Commission Background Paper No. 133, at 12 (2020) (“Tax authorities also appreciate the fact that the wealth tax requires individuals to annually report their net wealth. The annual fluctuations in net wealth, together with statistical data on annual spending of individuals and households, allow the tax authorities the check the plausibility of the taxpayer’s declared income. Thus, one may argue that the wealth tax also has a control function for income tax purposes.”).
All of this can be achieved in a reasonably administrable manner. Our proposed model rules are based in part on the best features of the Swiss wealth tax, which has been a pillar of the Swiss tax system for well over 100 years and which is generally viewed as being both reasonably administrable and "difficult to avoid with standard tax planning techniques." For instance, our proposed model rules generally recommend using market-trading prices for valuing publicly traded assets, for which these prices are easily obtainable. For many other assets, our proposed model rules recommend using formulaic valuations based on readily available information—for example, we recommend that most privately held businesses be valued based on accounting information that is already being reported for Federal tax purposes. We recommend only relying on appraisals for the more limited sets of assets for which it is neither possible to calculate valuations based on market-trading prices or reasonable formulaic valuations. Even then, for assets for which we recommend that appraisals be required, we recommend only requiring an appraisal once every 10 years unless the taxpayer has engaged in a transaction that would substantially change the value of the asset, with the reported values from the appraisals then adjusted via formulas for subsequent years. Our overall proposed approach thus minimizes the use of appraisals and resulting administrative and compliance costs. We also recommend special allowance provisions for especially liquidity constrained taxpayers and for certain especially hard to value assets.

In summary, although no form of taxation is perfect, the proposed Ultra-Millionaire Tax is almost guaranteed to be superior at valuation and measurement with respect to the ultra-wealthy as compared to the existing income tax or estate and gift tax, and with limited administrative and compliance burdens.

II. THE CASE FOR TAXING "REAL" (BOOK) CORPORATE PROFITS

The U.S. corporate tax system is perhaps even more broken than the personal tax system. The Republicans’ 2017 tax overhaul—the "Tax Cuts and Jobs Act" (TCJA)—improved the corporate tax system in some ways but made it much worse in other ways. Arguably, the most profound change made by the TCJA was to slash the top statutory corporate income tax rate from 35 percent to 21 percent. Although this change has probably helped alleviate some of the international and financial-engineering pressures on the corporate tax system, it has come at a large cost to Federal revenues and to the progressivity of the overall tax system, and has opened the door to a new set of abusive tax games involving the use of the corporate form for tax sheltering purposes.

The corporate tax system is in dire need of comprehensive reform. In my view, a comprehensive reform package should do all—or at least most—of the following: (a) raise the overall top corporate tax rate back to a level close to the top individual rate, as it was prior to the TCJA; (b) reform the corporate tax so that it would be partially destination-based, and only partially source-based, with the effective top rate on the source-based component then being set similar to other nations’ source-based corporate tax rates, and with the effective top rate on the new border-adjusted destination-based component then making up the difference; (c) further incorporate carbon-based sustainable-development adjustments into the new border-adjusted destination-based component of the reformed corporate tax; (d) terminate the check-the-box regulations and abolish both subchapter K and section 199A, while reforming subchapter S, so that all large business entities would be taxed as corporations and without unnecessary and harmful preferences for remaining pass-through entities; (e) transform the corporate tax more fully in the direction of being a profits-only entity tax while equalizing the tax treatment of debt and equity financing, either through more comprehensive cost-of-capital allowance rules or by combining much tighter limitations on interest deductions with more generous expensing allowances; (f) more comprehensively limit the entity-level deductibility of high salaries and other forms of compensation; and (g) require partial, but only partial, book-tax conformity.

42 Eckert and Aebi, id. at 3.
43 Id. at 12.
45 Id. at 5–16.
46 I am in the process of developing these recommendations in an unfinished work-in-progress article.
I note this all as background, because a comprehensive reform package of this sort is not currently on the table. What is on the table are more limited sets of partial reforms. In the absence of more comprehensive reforms like those I note above, I will now explain why I support the Real Corporate Profits Tax Act of 2021 as a significant positive move toward improving the corporate tax system.

In my view, the best analysis of issues related to proposals for book-tax conformity can be found in a 2009 article by law professor Daniel Shaviro. As Shaviro explains:

One of the hallmarks of the “Enron era” in corporate governance was companies’ increasing proficiency in reporting high earnings to investors and low taxable income to the Internal Revenue Service. Enron has passed from the scene, and, perhaps, so have the worst abuses of the Enron era, but the book-tax gap, or excess of reported financial accounting income over taxable income, persists. In 2003, for example, all taxpaying corporations that filed U.S. returns were estimated to have reported pretax book income of $899 billion, as compared to net taxable income of only $455 billion, leaving a book-tax gap of $444 billion—an amount almost equal to the net taxable income that was reported. While the gap’s exact causes, though much studied, remain imperfectly understood, most analysts agree that its persistence offers suggestive evidence of two ongoing, distinct evils. The first is earnings management, or managerial manipulation of reported financial accounting income in the hope of favorably influencing one’s stock price or otherwise serving managerial goals. The second is tax sheltering, or reducing one’s U.S. Federal income tax liability through various maneuvers that, even if lawful when engaged in, would likely be barred if they drew the government’s close attention. Managerial incentives to engage in both remain strong, even if managers have grown less aggressive since the peak of the Enron era.

To summarize, corporate taxpayers generally keep two sets of accounting books: one for reporting earnings to the Securities and Exchange Commission and to shareholders and other investors and potential investors, and another for reporting earnings to the Internal Revenue Service for tax purposes. Most analysts agree that corporate taxpayers often try to inflate reported earnings in the first set of books, so as to appear more profitable to shareholders and to other investors and potential investors. Most analysts likewise agree that corporate taxpayers often try to deflate reported earnings in the second set of books, so as to pay less tax.

Some have proposed requiring full book-tax conformity, so that corporate taxpayers would be required to use the same set of books for both tax and financial accounting purposes. This has been the historical approach used by the German tax system, for example. However, as Shaviro persuasively explains, and as I suspect the Republican-invited witnesses to this hearing will emphasize, there are a number of problems and harmful consequences that might result from moving to full book-tax conformity that would probably make it not a good idea to do.

But we needn’t choose between all or nothing. Shaviro recommends an approach for accomplishing 50-percent book-tax conformity. Part of his reasoning—but summarized in my words—is that the potential harms and problems from book-tax conformity likely increase on the margin as the effective conformity percentage rises from 0 percent to 100 percent. By contrast, the advantages of book-tax conformity from reducing perverse incentives for inflating earnings reported to investors and for deflating earnings reported for tax purposes almost certainly do not similarly increase on the margin, and quite possibly decrease on the margin. It follows that there is probably an optimal percentage for requiring book-tax conformity of less than 100 percent but more than 0 percent. As Shaviro elaborates,

Taxable income and financial accounting income, while using a shared concept, serve very different purposes—determining current-year tax liability on the one hand, and providing a particular informational input to investors on the other. It is not surprising, therefore, that the two measures both ideally and actually have differences.

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48 Id. at 425–26.
49 Id. at 483–84.
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Yet the persistent book-tax gap, or excess of reported financial accounting income over taxable income, reflects not these differences but corporate managers’ incentives to engage in two socially undesirable activities: tax sheltering on behalf of shareholders and earnings management on their own behalf. Moving in the direction of requiring book-tax conformity would have the desirable feature of creating Madisonian tension between the managers’ twin aims, reducing the incentive to play games and the scope of what they could accomplish.

Absent political incentive problems, it might indeed make sense to adopt a one-book system or something close to it, notwithstanding the differences between the two measures’ purposes. However, Congress, for the most part, currently confines its dark arts to the design of taxable income, while largely leaving accounting income to FASB, which helps make the Madisonian strategy less promising with respect to its decisions than those of corporate managers. A more directly involved Congress might be expected to worsen financial accounting income more than improve taxable income and in any event could not be required to keep the two measures in lockstep when it wanted to add opposite tax and accounting preferences to each.

My suggested proposal, generally requiring a 50 percent adjustment of taxable income towards financial accounting income for large, publicly traded companies, is not a perfect solution to the competing considerations in this complicated but important area. Yet it would substantially improve current law if adopted, and even if just seriously considered, may help to advance the ongoing debate.

The Real Corporate Profits Tax Act of 2021 is similar to Shaviro’s proposal for partial book-tax conformity, but also different in important respects. To begin with, the Real Corporate Profits Tax Act would create a surtax of 7 percent of every dollar of book income above $100 million. As an addition to current law, this would effectively raise the top corporate tax rate on large corporations 28 percent (the current top statutory rate of 21 percent plus the new 7 percent surtax rate), with an effective book-tax conformity percentage of 25 percent (the 7 percent surtax rate/the 28 percent combined rate). The Real Corporate Profits Tax Act of 2021 would thus not go as far as Shaviro’s proposal in requiring book-tax conformity.

The underlying mechanics are also different, as the 7 percent surtax would be based on complete book-tax conformity, but the book-tax conformity rules would only apply to that 7 percent surtax. Nevertheless, as with Shaviro’s proposal, this should reduce the perverse incentives that corporate managers currently face to inflate earnings reported for financial accounting purposes and to deflate earnings reported for tax purposes, while largely avoiding the problems that might arise from more complete book-tax conformity. In particular, it seems rather unlikely to me that the mere existence of the 7 percent surtax rate would induce Congress to harmfully meddle with the FASB’s decision-making as to financial accounting rules.

Overall, there is a very strong case for moving to partial, but only partial, book-tax conformity for corporate taxpayers. The Real Corporate Profits Tax Act of 2021 is a reasonable approach for accomplishing this. All factors considered, the Real Corporate Profits Tax Act would raise substantial revenues needed to fund public investment, would significantly improve the progressivity of the overall tax system, and would reduce the perverse incentives corporate taxpayers currently face both to inflate earnings reported for financial accounting purposes and to deflate earnings reported for tax purposes so as to avoid tax. And it would accomplish all this while minimizing the potential harms that might result from more complete book-tax conformity. For all of these reasons, I support the Real Corporate Profits Tax Act of 2021 as an important and significant step toward a better corporate tax base.

III. THE CASE FOR IMPROVING IRS FUNDING AND MAKING TAX ENFORCEMENT LESS DEPENDENT ON THE ANNUAL APPROPRIATIONS PROCESS

There is general agreement amongst tax experts that the IRS has been starved of funding over the recent decade and that this has been enormously harmful to the tax system in a wide variety of ways.50 The need for improving IRS funding is overwhelming.

50 See, e.g., Leandra Lederman, Valuation as a Challenge for Tax Administration, 96 Notre Dame L. Rev. 1485, 1497 (2021) (Audit rates are generally low, due to resource constraints. The Internal Revenue Service (IRS) in particular has seen its audit rates decline since 2010, Continued
The most straightforward way to improve IRS funding would be to substantially increase the funding allotted through the annual appropriations process. And this should indeed be done, and promptly. But history suggests that this, alone, is insufficient. For instance, despite that the Affordable Care Act (ACA) required the IRS to take on substantial new obligations in order to enforce the tax provisions of the ACA, insufficient funding was granted to the IRS to accomplish these purposes, which harmed both the implementation of the ACA and the enforcement of the tax system more generally.

It is thus time to consider going beyond just relying on the annual appropriations process to also provide dedicated multi-year mandatory funding streams and other more reliable funding appropriations to the IRS and perhaps also to other agencies charged with substantial tax enforcement obligations. Promising approaches for accomplishing these goals include: (a) appropriating funding that is essentially exempt from general annual limits via what is typically referred to as an "allocation-adjustment" mechanism; and (b) creating a multi-year "mandatory" funding stream provided directly through new authorizing law.

In addition to these proposals for improving IRS funding, I would also strongly recommend: (a) increasing third-party information-reporting requirements; and (b) extending the Federal False Claims Act to tax claims (but with high exemption limits so that tax fraud by ultra-wealthy individuals and families and by large businesses and corporations would be liable for tax claims under the extended False Claims Act).

To further emphasize the need for increased and more-reliable tax-enforcement funding and for accompanying reforms to improve tax enforcement, I will close by quoting testimony recently provided to the House Ways and Means Committee by my colleague Leandra Lederman:

"Most important, enforcing the tax laws increases the fairness of the tax system. A progressive income tax tends to reduce income inequality. However, a recent study found that tax evasion unravels that effect. This is because higher-income taxpayers tend to have more opportunities for tax evasion. Taxpayer fairness thus calls for enforcement of the tax laws. It also calls for enforcement where there is more opportunity for noncompliance, even if these audits are more expensive to conduct because they cannot simply be done by correspondence, for example. Enforcement depends on IRS resources, so part of taxpayer fairness is adequately funding the IRS.

Thank you again for inviting me to speak with you today, on these critical issues and reform proposals for creating opportunity through a fairer tax system. I look forward to answering any questions you might have.

QUESTIONS SUBMITTED FOR THE RECORD TO DAVID GAMAGE

QUESTIONS SUBMITTED BY HON. BILL CASSIDY

ESTATE TAXES

Question. Senate Majority Leader Schumer has stated, with regard to the estate tax "... any organic business—a farm, a small business, and frankly a large business—that would have to be broken up because of the extent of the tax should not be. A business is an ongoing organism. It employs sometimes 10 people and sometimes 10,000 people. To have to break that business up to pay any tax, to me, is counterproductive." Do you agree that the tax code should not inhibit owners of any size business from being able to pass along that business, in full, to future generations?

as Congress has starved it of funding."; Natasha Sarin and Lawrence H. Summers, Shrinking the Tax Gap: Approaches and Revenue Potential, Tax Notes Federal, November 18, 2019.

51 The provisions of New York State's False Claims Act that apply to tax claims are a good starting point for a model for such reforms. I am also in the process of developing further recommendations as part of the model valuation and enforcement rules that I am developing for wealth tax and related reforms.

Answer. It is not difficult to include provisions in a wealth tax (or estate and gift tax) to mitigate liquidity issues for taxpayers like those who own or would inherit family businesses. That said, taken to the extreme, exempting privately held businesses from taxation is a recipe for both undermining our tax system and harming our economy because taxpayers would then engage in complicated and economically harmful tax gaming transactions to transform their wealth and income into forms made exempt from tax. These sorts of transactions are commonly done to escape both income taxation and estate and gift taxation today, and with many harmful consequences. For elaboration on this point, see David Gamage and John R. Brooks, “Tax Now or Tax Never: Political Optionality and the Case for Current-Assessment Tax Reform, 100 North Carolina Law Review (forthcoming), available at SSRN: https://ssrn.com/abstract=3801164.

DOUBLE TAXATION

Question. New York Democratic Representative Jerry Nadler recently tweeted, “No one should ever be taxed twice on the same income. It’s not fair and it’s not just.”

Do you agree with this view? If not, why not?

Answer. Without context, saying “double taxation” is meaningless. Inquiries into tax fairness and justice require examining real tax burdens and compared to ability to pay and benefits received from the State.

With that in mind, it should be understood that most ultra-wealthy American taxpayers avoid paying any tax on most of their true income and wealth. The effective tax rates on most ultra-wealthy American taxpayers (as measured based on true income) are typically very low, often in single digits, and much lower than the effective tax rates paid by most ordinary middle class Americans. This is unfair, unjust, and creates many harmful consequences including harms to the economy from tax gaming. See David Gamage and John R. Brooks, “Tax Now or Tax Never: Political Optionality and the Case for Current-Assessment Tax Reform,” 100 North Carolina Law Review (forthcoming), available at SSRN: https://ssrn.com/abstract=3801164.

ENDOWMENTS ACCUMULATING WEALTH

Question. Many universities have large, often multi-billion-dollar, endowment funds attached to them. Some of those funds have come from donations from people’s wealth and estates. Most universities with endowments do not use all of their endowment funds to help students or researchers. Rather, they carry some of those funds forward, presumably to help ensure that resources can be made available for future students and researchers. That is, universities, with their endowment funds, build dynastic wealth.

Families in the United States wish to do the same, yet some people deride bequest motives as some undue benefit to the “rich” or “ultra-rich.” People wish to accumulate wealth over time, using savings of some of their already-taxed income, and they choose not to consume all the accumulation in their lifetimes so that future members of their family can benefit. While that seems like altruism to me, it apparently seems like some sort of undeserved dynasty building to others.

Since you are in the academic world, and must be aware that many universities hold large endowments that they build to effectively accumulate dynastic wealth. Should Congress increase taxation of university endowments and use the proceeds to spend on what some may view as more worthy social investments?

Answer. Tax-exempt organizations like universities and churches are granted exemptions from taxation so as to advance their charitable purposes. These organizations are thus quite different from wealthy individuals and families. In my view, the tax benefits that Congress has provided to tax-exempt organizations (and to donors through the charitable contribution deduction) are probably somewhat too generous and should be reformed so as to prevent abusive forms of tax gaming and to better ensure that these tax benefits fulfill their intended purposes.

PREPARED STATEMENT OF SCOTT A. HODGE, PRESIDENT, TAX FOUNDATION

Thank you, Madame Chairman, Ranking Member Cassidy, members of the committee. I appreciate the opportunity to speak to you today about tax fairness, economic growth, and funding government investments.
A famous economist once said, “There are no solutions, there are only trade-offs.” That lesson is especially true in tax policy and in the choices lawmakers must make in funding public investments.

The scales of justice may have two trays, but tax policy has three trays that lawmakers must balance: revenues, equity, and economic growth. But, these factors cannot be balanced equally.

In other words, lawmakers must decide which is most important: (1) how much revenues a tax will raise, (2) progressivity, or who bears the burden of the tax, or (3) what impact those tax changes will have on economic growth.

Extensive economic modeling and empirical evidence tells us that there is a clear trade-off between progressivity and economic growth. This is especially true with so-called success taxes—taxes on capital and business income.

Understanding these dynamics matters in how you fund government investments. Research by the Congressional Budget Office (CBO) has found that government investments deliver only half of the economic returns of private sector investments. Given the opportunity costs that come with government spending, lawmakers must be careful in choosing offsets that don’t do more harm to the economy than the modest benefits generated by the public investments.

Indeed, the U.S. tax system is already very progressive and redistributive, so making the tax code even more progressive through proposals such as a wealth tax, a minimum tax on book income, or an increase in the corporate tax rate are among the most economically damaging options that lawmakers could use to fund government investments. Inevitably, these tax policies would slow the economy and reduce the living standards of the very people the new government investments are intended to help.

There are less economically harmful options to fund new government investments. These include cutting wasteful spending, expanding user fees, eliminating tax expenditures, and shifting the tax burden to consumption-based taxes.

**IS THE TAX SYSTEM FAIR?**

Before we explore the trade-offs in tax policy, we should first address the perceived lack of fairness in the tax code.

By any objective measure, the U.S. tax code is extremely progressive and very redistributive. Indeed, a study by economists at the Organisation for Economic Co-operation and Development (OECD) found that only Israel has a more progressive and more redistributive income tax system than the U.S. among the leading industrialized nations.¹

As I outlined recently in testimony before the Senate Budget Committee,² Internal Revenue Service (IRS) data indicates that the wealthy in America are bearing the heaviest share of the income tax burden than in any time in recent history.

According to the latest IRS data for 2018—the year following enactment of the Tax Cuts and Jobs Act (TCJA)—the top 1 percent of taxpayers paid $616 billion in income taxes. As we can see in Figure 1, that amounts to 40 percent of all income taxes paid, the highest share since 1980, and a larger share of the tax burden than is borne by the bottom 90 percent of taxpayers combined (who represent about 130 million taxpayers).³

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The tax and fiscal system are also very redistributive. A recent CBO study, The Distribution of Household Income, 2017, provides an insight into the tax code’s progressivity and the redistributive effects of Federal fiscal policy—both taxes and direct Federal benefits.

Figure 2 shows that households in the bottom three quintiles collectively receive more than $1 trillion more in direct government benefits than they paid in all Federal taxes in 2017. In other words, 60 percent of American households received more in benefits than they paid in Federal taxes.

By contrast, we can see that households in the top 20 percent paid $1.7 trillion more in taxes than they received in direct benefits, of which $728 billion came from households in the top 1 percent.

These are the results that you would expect from a highly progressive fiscal system.

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Millions are off the tax rolls. Because of the expansion of various credits and deductions over the past 3 decades, millions of taxpayers pay no income taxes when they file their tax returns, and many receive sizable refunds despite having no tax liability.

IRS data for 2018 indicates that more than 53 million low- and middle-income taxpayers paid no income taxes after benefiting from record amounts of tax credits, or nearly 35 percent of all filers. Indeed, the doubling of the Child Tax Credit (CTC) from $1,000 to $2,000 in the TCJA increased the number of non-payers by more than 4 million.

The recently enacted American Recovery Plan Act (ARPA) allows households with children to claim up to $3,600 for children under age 6 or $3,000 for children 6 through 17 regardless of income. Our model estimates that this expansion of the CTC will increase the number of non-payers to 58.4 million—meaning 39 percent of all filers will have no income tax liability in 2021.

CORPORATE TAX IS MOST ECONOMICALLY HARMFUL, ESPECIALLY FOR WORKERS

Any discussion of corporate tax policies must begin with two economic realities. First, the corporate income tax is the most harmful tax for economic growth because capital is the most mobile factor in the economy and, thus, most sensitive to high tax rates.6 Second, academic research indicates that workers bear at least half of the economic burden of the corporate tax through reduced wages, especially for “the low-skilled, women, and young workers.”7

So, raising corporate taxes hurts workers and economic growth.

It is also worth noting that the number of traditional C corporations in the U.S. has fallen to less than 1.6 million, fewest since 1974, and 1 million fewer than 3 decades ago. They have been supplanted by a dramatic rise in the number of pass-through business forms, such as S corporations and LLCs. As a result, there is more

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business income taxed on individual 1040 tax forms than traditional 1120 corporate tax returns.\(^8\)

We can see from Figure 3 that corporate tax revenues have been highly volatile over the past 40 years, rising and falling with the business cycle.\(^9\) This volatility is despite the U.S. levying one of the highest corporate tax rates in the industrialized world, until the TCJA lowered the Federal rate from 35 percent to 21 percent.

We can also see that income tax collections from pass-through businesses have been steadily rising and now largely equal the collections from traditional C corporations, each amounting to roughly 1 percent of GDP.

The U.S. tax system is most “business dependent.” While business tax collections can rise and fall due to economic conditions and changes in tax policies, the U.S. tax system is still one of the most “business dependent” systems anywhere according to a 2017 study by OECD economist Anna Milanez.

Her report found that U.S. businesses either pay or remit more than 93 percent of all the taxes collected by governments in the U.S.\(^10\) As Figure 4 illustrates, this includes taxes paid directly by businesses, such as corporate income taxes, property taxes, and excises taxes, as well as the taxes businesses remit on behalf of employees and customers, such as payroll taxes, withholding taxes, and sales taxes.

Without businesses as their taxpayers and tax collectors, American governments would not have the resources to provide even the most basic services.

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TCJA policies reduced corporate collections but boosted capital investments. Many lawmakers are pointing to the fact that corporate tax collections have declined since the TCJA as evidence that corporations are not “paying their fair share of taxes.”

Considering the rhetoric surrounding the TCJA’s corporate tax provisions, most people would never know that they comprised just 22 percent of the TCJA’s $1.45 trillion in total tax cuts. According to the Joint Committee on Taxation’s scoring of the TCJA, the corporate tax reforms (which included the rate cut to 21 percent and the expensing provisions) were estimated to reduce tax revenues by about $654 billion over 10 years. However, half of this amount was offset by the TCJA’s international tax provisions which were designed to raise over $324 billion, thus cutting the net amount of corporate tax relief to $328 billion over 10 years.

If we consider the winners and losers from the various provisions, it is fair to say that the winners are largely the domestic firms that benefited from the lower corporate rate and bonus expensing, while the losers were the multinational firms that were targeted with higher taxes on their foreign income.

Furthermore, as can be seen in Figure 5, the corporate tax relief was front-loaded in the first 5 years of the plan as the lower corporate tax rate and the bonus expensing provisions took hold to boost capital investment. These revenue “losses” were scheduled to turn to revenue increases after 2022 as the bonus expensing provision began to phase out and other planned tax increases (such as the amortization of Research and Development (R&D) expenses) kicked in.
Although the political focus has been on the drop in corporate tax revenues post-TCJA, it appears that the combination of the bonus expensing provision and the lower corporate tax rate did spur an increase in corporate investment in things like equipment, buildings, and research and development. Table 1, shows that corporate fixed investment jumped 9.0 percent in nominal terms in 2018 following enactment of the TJCA, and increased an additional 4.4 percent in 2019.11

While there are always a lot of factors that contribute to economic data, these results should not be surprising based on the empirical evidence from past expansions of bonus expensing of capital investments or other evidence from corporate tax changes around the world.12 With bonus expensing, it is important to remember that the only way firms can claim the tax benefit is to invest in new capital equipment.

Moreover, unlike depreciation, which spreads the deduction for capital investments over time, bonus expensing is taken only in the year the purchase is made. So, a deduction for capital investment taken today does not translate into deductions taken in future years.
TRADE-OFFS IN TAX POLICY: BALANCING REVENUES, EQUITY, GROWTH, AND SIMPLICITY

Over the past decade, Tax Foundation economists have modeled hundreds of changes to the tax code and found that it is nearly impossible to balance revenues, equity, and growth equally. Lawmakers will have to decide which of these factors is most important based on their values and priorities.

For example, if lawmakers want to make the tax code more progressive and raise revenues, our model shows that they will likely have to give up some economic growth, because higher tax rates dampen economic activity, especially higher taxes on capital and labor.

And slower growth often raises less revenues.

On the other hand, simplifying the tax code, say by eliminating certain tax expenditures, not only can raise revenues, but it also can increase the progressivity of the code while doing less economic harm than raising marginal tax rates. The tax base matters just as much as tax rates.

If lawmakers want to generate more economic growth, our model shows that they will likely have to give up some progressivity, and maybe some tax revenues too. Although, all things being equal, a larger economy will tend to generate more tax revenues than the baseline. But, contrary to what some advocates profess, tax cuts rarely pay for themselves.

THE ECONOMIC CONSEQUENCES OF A WEALTH TAX

"Tax Fairness" and economic growth may not be compatible goals. A wealth tax is a good example of the trade-off between making the tax code more progressive and slower economic growth. Senator Elizabeth Warren's (D–MA) proposal would impose a 2-percent tax rate on every dollar of net wealth between $50 million and $1 billion, and a 6-percent tax rate on net wealth over $1 billion.

Tax Foundation economists modeled the economic effects of this proposal using our Taxes and Growth (TAG 2.0) General Equilibrium Tax Model. On a conventional basis, the model determined that the proposal could raise nearly $2.2 trillion over 10 years and reduce the after-tax incomes of the top 1 percent of taxpayers by 13.5 percent.

This new revenue and increased progressivity come with an economic cost. The model found that the wealth tax would reduce the size of the economy by 0.8 percent in the long run, shrink the capital stock by 2.0 percent, wages by 0.7 percent, and eliminate 149,000 full-time equivalent jobs. It would ultimately reduce after-tax incomes across the board, and by 0.6 percent for the bottom quintile.13

To put this in perspective, the wealth taxes’ hit to GDP is greater than the effect of raising the corporate tax rate to 28 percent and four times the economic impact of levying a $25 per-ton carbon tax.

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Interestingly, the TAG 2.0 model found that the wealth tax would reduce national income, measured by GNP (gross national product), by 1.5 percent, nearly twice the impact to the broader economy as measured by national output, or GDP. Why is that?

It turns out that the model determined that the wealth tax would force the wealthy to sell their assets to pay the tax, often at discount prices. Because the U.S. is an open economy and capital markets are global, the model indicated that foreign investors would purchase those assets, which is why national output (GDP) does not fall by as much as national income (GNP). But what this does mean is that the wealth tax would result in the transfer of ownership of those assets from wealthy Americans to wealthy foreigners.14

Thus, the unintended impact of a wealth tax is that it would transfer wealth from U.S. millionaires and billionaires to foreign billionaires and mean that American workers could increasingly be employed by foreign employers. Now owned by foreigners, these assets would be out of reach of the wealth tax.15

Equity and simplicity may also not be compatible goals.

The various proposals to levy a minimum tax on corporate book income are also good examples of taxes aimed at making the system more progressive, but which would add considerable complexity to the code and ultimately retard economic growth.

Senator Warren has proposed a “Real Corporate Profits Tax” to be levied at 7 percent of a corporation’s profits as reported on financial statements after the first $100 million in profits.16 It would be assessed in addition to the standard corporate income tax.17

President Biden proposed a minimum tax of 15 percent on the financial income of corporations reporting more than $100 million in book income. Unlike Warren’s proposal, Biden’s proposal would operate as an alternative minimum tax that would be applied to large corporations if their effective tax rate falls below 15 percent on income as reported on financial statements.

A minimum tax on book income would introduce significant complexity into the corporate tax code while outsourcing key aspects of the corporate income tax to unelected decision-makers at the Financial Accounting Standards Board (FASB), who establish the standards for corporate book income.

Our 2019 scoring of the Warren book tax proposal found that it would reduce the size of the economy by 1.9 percent, lower the capital stock by 3.3 percent, trim wages by 1.5 percent, and cost the economy over 450,000 jobs. And while those at the top of the income scale would see the largest declines in after-tax incomes, taxpayers in every income group would see their incomes fall as a result.

Interestingly, our model estimated that the plan would raise $872 billion over 10 years on a conventional basis, but after accounting for the economic impact of the tax, the model lowered that revenue estimate by nearly 50 percent to $476 billion. This is an indication that progressive taxes don’t always deliver the amount of revenues that are predicted.

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The Biden book tax proposal would not have as severe of an economic impact as the Warren version, nor would it raise as much revenue. However, I should note that we did not model the proposal separately from Biden’s other corporate tax plans, such as raising the rate to 28 percent. Still, our TAG 2.0 model estimates that the Biden book tax proposal would raise about $203 billion over 10 years when combined with Biden’s other tax proposals and reduce the size of the economy by 0.21 percent.

The economic effect of a tax on book income depends on whether the tax is assessed as a minimum tax, like the Biden proposal, or if it is a tax applied to book income on top of the existing corporate income tax, like the Warren proposal. Both add complexity to the tax code, and both would slow economic growth.

**TRADE-OFFS IN INFRASTRUCTURE**

Lawmakers need to be very careful in deciding how to fund government investments because when the CBO reviewed the academic literature on the economic returns to public investments, it found that the economic benefits are relatively modest and about half the returns to private investments.\(^{18}\)

CBO estimates that the average rate of return on private sector investment is currently about 10 percent—that is, that a $1 increase in private investment, all else being equal, increases output by 10 cents over a year. As a result, the average rate of return on Federal investment in the illustrative policies examined in this report is about 5 percent.

In other words, a $100 million Federal investment would increase GDP by $5 million, whereas the same private investment would boost GDP by $10 million.

Various factors explain why Federal investments deliver smaller economic returns than private-sector investments. According to the CBO:

That is because public investment is not driven by market forces; its goals include not only achieving positive economic returns but also improving quality of life, reducing inequities, and addressing other objectives. In addition, an increase in Federal investment spending is often partially offset by a decrease in investment spending by States and localities.\(^{19}\)

Thus, the CBO cautions, “the macroeconomic effects of an increase in Federal investment would depend on how that spending is financed.”\(^{20}\) In particular, CBO modeling of large infrastructure spending financed by different tax approaches determined that progressive income taxes would have the most harmful impact on economic growth and, thus, do the most harm to future generations.\(^{21}\)

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\(^{20}\) Ibid.


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**TABLE 2**

<table>
<thead>
<tr>
<th>Economic Impact of the “Real Corporate Profits Tax”</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Domestic Product (GDP)</td>
</tr>
<tr>
<td>Capital Stock</td>
</tr>
<tr>
<td>Wages</td>
</tr>
<tr>
<td>Service Price of Capital</td>
</tr>
<tr>
<td>Full-time Equivalent Jobs</td>
</tr>
</tbody>
</table>

Source: Tax Foundation General Equilibrium Model, March 2019
For example, it found that a progressive income tax (on all income) large enough to fund a 5-percent increase in spending would reduce the lifetime consumption of Americans born from 1980 to 1999 by 10.8 percent and those born from 2000 to 2019 by 13.3 percent.22

This strongly indicates that if lawmakers want to avoid reducing the living standards of the next generation of Americans, they should avoid using progressive taxes to finance new government investments or programs.

MODELING OPTIONS FOR FINANCING INFRASTRUCTURE SPENDING

Tax Foundation economists recently modeled different funding mechanisms to pay for a stylized $1-trillion infrastructure plan. These include debt financing, increasing the corporate tax rate to either 28 percent or 32 percent, and user fees and excise taxes.

As Table 3 illustrates, the harmful effects of increasing the corporate tax rate swamp any benefits from the infrastructure spending. The 28-percent rate option would reduce the size of the economy by 0.5 percent, while the 32-percent rate option would reduce the economy by a full 1.0 percent—clearly making the benefits of such a package not worth the costs.

By contrast, our model found that the economic gains from spending with the debt financing option and the user fee/excise tax option outweighed the economic harm to GDP from the increased borrowing or the taxes (increased borrowing would reduce national income as measured by GNP).

However, the only option that resulted in positive employment gains was the debt financing option. Again, this points to the trade-offs lawmakers must consider when financing Federal spending. Tax options have economic consequences, even if those effects don’t outweigh the benefits of the Federal investments. That said, borrowing costs increase the overall cost of the debt financing option to over $1.2 trillion. These costs will have to be paid back by future taxpayers.

<table>
<thead>
<tr>
<th>Financing Options</th>
<th>Borrowing (issuance of federal debt)</th>
<th>Increase the corporate rate to 28 percent</th>
<th>Increase the corporate rate to 32 percent</th>
<th>User Fees Excise Taxes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long-Run Gross Domestic Product (GDP)</td>
<td>0.20%</td>
<td>-0.50%</td>
<td>-1.00%</td>
<td>0.01%</td>
</tr>
<tr>
<td>Capital Stock</td>
<td>0.20%</td>
<td>-1.60%</td>
<td>-2.80%</td>
<td>0.10%</td>
</tr>
<tr>
<td>Wage Rate</td>
<td>0.20%</td>
<td>-0.40%</td>
<td>-0.80%</td>
<td>-0.60%</td>
</tr>
<tr>
<td>Full-time Equivalent Jobs</td>
<td>43,000</td>
<td>-96,000</td>
<td>-192,000</td>
<td>-126,200</td>
</tr>
<tr>
<td>Ten-Year Static Deficit</td>
<td>-1294.9</td>
<td>-406.7</td>
<td>40.3</td>
<td>-37.2</td>
</tr>
<tr>
<td>Ten-Year Dynamic Deficit</td>
<td>-1167.7</td>
<td>-403.1</td>
<td>-62.7</td>
<td>-82.9</td>
</tr>
</tbody>
</table>

Notes: We assume additional infrastructure spending of $1 trillion over five years, resulting in a gradual increase in the amount of infrastructure in place. Following the initial investment, we assume it generates a 5-percent return in line with Congressional Budget Office (CBO) estimates.

We assume the infrastructure requires an increase in depreciation-related outlay to maintain the assets over time, requiring resources to be redirected from other types of output when the economy is in full-employment equilibrium. Roads and bridges are assumed to have at least a 30-year life and require about 2 percent of their initial cost in annual maintenance.

The carbon tax option is imposed at $33 per ton in 2022, rising at 5 percent annually to $91.19 per ton by 2031.


CONCLUSION

It may be a cliché, but there is no such thing as a free lunch in government spending or tax policy. Government investments are often sold to the public with the promise that they will improve lives and improve the economy. But, in fact, research finds that they deliver half of the economic benefits of private-sector investments.

That means lawmakers must take great care in deciding how to finance government investments. Economic research and Tax Foundation modeling indicate there is a negative trade-off between progressive taxes on capital income—such as the wealth tax, minimum book tax on corporate income, and a higher corporate tax

22 Ibid, Table 3, 30.
rate—and economic growth. These are among the most harmful taxes lawmakers could use to finance government investments. In every case, the economic harm caused by the taxes would swamp any of the benefits from the new spending, leaving taxpayers and the economy worse off.

QUESTIONS SUBMITTED FOR THE RECORD TO SCOTT A. HODGE

QUESTIONS SUBMITTED BY HON. BILL CASSIDY

ESTATE TAXES

Question. Senate Majority Leader Schumer has stated, with regard to the estate tax “. . . any organic business—a farm, a small business, and frankly a large business—that would have to be broken up because of the extent of the tax should not be. A business is an ongoing organism. It employs sometimes 10 people and sometimes 10,000 people. To have to break that business up to pay any tax, to me, is counterproductive.”

Do you agree that the tax code should not inhibit owners of any size business from being able to pass along that business, in full, to future generations?

Answer. On a personal level, I find the estate tax immoral. I remember the sad feeling I had when I heard that Jackie Onassis’s estate had to auction off JFK’s humidor and rocking chair to pay the estate tax. Forcing families to sell off heirlooms to pay a tax just seems wrong to me.

Similarly, most family businesses have been built up over a lifetime and are often asset-rich and cash-poor. To force a family to sell the business in order to pay the estate tax is wrong on many levels. In some cases, the only buyers are much larger firms, so the estate tax effectively punishes small business and favors larger ones.

Using our Taxes and Growth General Equilibrium Tax Model, we found that repealing the estate and gift taxes would boost GDP by 0.1 percent, increase the capital stock by 0.3 percent, and create 22,000 jobs. Increasing GDP by 0.1 percent may not seem like much, but in a $20-trillion economy, that is more added GDP than the estate tax raises in a year. Another way of looking at this is that the estate tax costs more in lost GDP than it raises in taxes each year.

DOUBLE TAXATION

Question. New York Democratic Representative Jerry Nadler recently tweeted, “No one should ever be taxed twice on the same income. It’s not fair and it’s not just.”

Do you agree with this view? If not, why not?

Answer. Yes, a basic tenant of good tax policy is that income should be taxed only once and as close to the source as possible. Unfortunately, there are many taxes that are simply second and third layers of tax on income that has already been taxed. The estate tax, discussed above, is a good example of that. In order to build wealth or a successful business, income is taxed first when it is earned as personal or business income. It is then taxed again as capital gains or dividends. Then taxed for a third or fourth time by the estate tax.

In particular, capital gains and dividends are second layers of tax on corporate income. Corporate income is first taxed by the corporate income tax. These after-tax profits are taxed a second time at the shareholder level by the taxes on dividend and capital gains. Integrating the corporate and individual income taxes would remove this double layer of tax.

THE WALT DISNEY COMPANY

Question. As I mentioned at the hearing—paraphrasing Professor Hoopes—too often politicians use rhetoric like “tax cheaters” in order to shade political arguments. As another witness told us, to the extent taxpayers pay less tax in certain areas, they are doing so because of laws that Congress passed. Yet we are told that if a taxpayer follows the law, and its tax burden decreases, then somehow that taxpayer is a little immoral and we should go after it.

And in fact, at the hearing, we had a live example of what appears to be the totally unfair and unsubstantiated disparagement of a taxpayer for simply following the law that Congress wrote. The Walt Disney Company is an iconic American com-
pany that, as far as I am aware, has never been accused by the IRS of being a “tax cheat.” And yet, one witness, Abigail Disney, suggested that, among other things, The Walt Disney Company used “trickery” to avoid paying taxes.

It appears that Ms. Disney has no official connection with or position at The Walt Disney Company. I know that you are likewise not affiliated with The Walt Disney Company. Based on publicly available information, however, I would like to ask your thoughts on the validity of several of the claims made at the hearing.

When I look at their financial reports, it certainly looks like The Walt Disney Company is a prolific taxpayer. In the years before passage of the TCJA, its effective tax rate appears to regularly be at or near 35 percent, and in the several years after, its effective tax rate similarly tracks the statutory rate. Based on publicly available information, is there any credibility to the suggestion made at the hearing that The Walt Disney Company has “gotten away without paying one cent in Federal income taxes”?

Answer. Full disclosure Senator, I am a Disney shareholder. I own 32 shares of Disney stock in a rollover IRA. So, I have a small personal interest in Disney’s finances and profitability. That said, if any company has an effective tax rate either near or above the pre-2017 statutory corporate tax rate of 35 percent, as appears to be the case here, then it would be incorrect to say that they are not paying their fair share or somehow “getting away with it.”

Question. Professor Hoopes testified that when a company issues stock options, it is “literally just compensating [its] employees,” and “that is a perfectly legitimate thing to deduct on your tax return.” And yet, Ms. Disney calls that “trickery.” Can you clarify for the record the appropriate characterization of this practice?

Answer. I would agree with Professor Hoopes that giving employees a stake in the company through stock options is a perfectly legitimate expense to deduct on a corporate tax return. It is no different than allowing companies to deduct salaries, wages, health-care costs, training, and other employee-related costs.

Let’s also not forget the symmetry in the tax code on stock options. While companies are allowed to deduct them, employees who take advantage of the options much either pay taxes on them as income or as capital gains. So, stock options don’t go untaxed as critics imply.

Question. When asked about so-called “profit shifting schemes,” Ms. Disney accused The Walt Disney Company of saving $315 million in 2013 alone in what was described as an effort to shift money earned in the U.S. to lower-taxed countries. Based on publicly available information, did the company in any way use an illegal “scheme” to “artificially lower” its tax obligation?

Answer. This statement seems like a clear misunderstanding of how the U.S. corporate tax system worked before the changes made in the 2017 Tax Cuts and Jobs Act. Prior to TCJA, companies could defer U.S. tax on their foreign earnings until those earnings were repatriated. However, when companies reinvested those foreign profits in their foreign operations—such as building a theme park or factory—they would declare those profits as “permanently reinvested.”

Prior to the 2017 tax changes, some companies may have reported on their financial statements how much U.S. tax they would have paid had they repatriated those profits dividends rather than permanently reinvest the earnings in their overseas operations. That seems to be the case here. Expanding the company’s operations abroad should not be seen as a tax dodge or anything illegitimate. Indeed, it is a mistake to think that a company’s foreign operations and profits won’t be taxed, they will be simply be taxed by the country in which the profits are earned, just not a second time by the U.S.

IMPACT OF WEALTH TAX ON OWNERSHIP OF DOMESTIC ASSETS

Question. You mentioned in your testimony that a wealth tax would create incentives for American assets to be owned by foreigners.

What effects could this have on both tax revenues and the broader economy?

Answer. This may be one of the least understood and unseen aspects of the wealth tax. The wealth tax is supposed to reduce inequality, but our tax model finds that it would lead to a shift in ownership of assets from rich Americans to rich foreigners.
The opinions expressed here are my own, and not that of any organization with which I am currently, or have been, affiliated, in any capacity (the University of North Carolina, the Kenan-Flagler Business School, the UNC Tax Center, the Internal Revenue Service, etc.).

Fairness is often used in reference to our tax system or the tax code. Presidents Joe Biden (https://joebiden.com/two-tax-policies/), Donald Trump (https://www.treasury.gov/press-center/press-releases/Documents/Tax-Framework.pdf), Barack Obama (https://obamawhitehouse.archives.gov/issues/taxes), George Bush (https://www.treasury.gov/press-center/press-releases/Documents/report30652.pdf), and Bill Clinton (https://clintonwhitehouse5.archives.gov/WH/Ac-complishments/eightyears-03.html) have all advocated for a tax system that is "fair," but have advocated for different tax systems that would produce different outcomes. As a result, it is difficult to know precisely what people are referring to when they reference a "fair" tax system, as perceptions of fairness are subjective.

I avoid the term "loophole." A loophole is "an ambiguity or omission in the text through which the intent of a statute, contract, or obligation may be evaded" (see https://www.merriam-webster.com/dictionary/loophole). Very frequently people speak of loopholes that are simply provisions in the tax code that they do not like, but which were intended to provide exactly the outcome the provision is observed to provide. As Senator Russell B. Long noted, "A tax loophole is something that benefits the other guy. If it benefits you, it is tax reform." The use of the word "loophole," in my opinion, is a clear flag of political rhetoric rather than serious discussion about tax policy, and it obscures what the real flaws in the tax code are. Certainly true loopholes in the tax code exist, but they are infrequent and rarely represent the kind of dollars that provisions intentionally legislated do (in my opinion, a back-door Roth IRA would be an example of a well-known true tax loophole).

PREPARED STATEMENT OF JEFFREY L. HOOPES, PH.D., ASSOCIATE PROFESSOR, KENAN-FLAGLER BUSINESS SCHOOL, UNIVERSITY OF NORTH CAROLINA, CHAPEL HILL

Chairperson Warren, Ranking Member Cassidy, and distinguished members, I appreciate the opportunity to participate in this hearing about creating opportunity through a fairer tax system. I am an associate professor at the Kenan-Flagler Business School at the University of North Carolina. I am also the research director of the UNC Tax Center. My research focuses on corporate and individual taxation, and how taxation affects taxpayer behavior.

My testimony will focus on perceptions of fairness in the tax code and recent proposals to fix such perceived unfairness; specifically, a tax on book income and the wealth tax. My main message is that corporations and individuals remit the taxes they do, including in situations some perceive as unfair, frequently because of explicit allowances in the tax code. In other words, the largest holes in our national tax revenue bucket are ones Congress has, itself, poked, and not the product of elaborate tax planning schemes, as is a current misperception. If members of Congress seek to change the tax system, they should do so in ways that make the tax code simpler, rather than layer on additional taxes that will add complexity to the tax code, be difficult to administer, have unintended negative consequences, and, ultimately, likely be eventually eliminated, making our tax system less stable. Taxing book income and the wealth tax are two examples of two such inadvisable taxes.

PERCEIVED UNFAIRNESS IN THE CORPORATE TAX SYSTEM

There are widespread perceptions that corporations do not pay their "fair share" of tax, and there are current proposals to increase corporate tax revenue in order
to expand government programs and services. If Congress seeks to raise more revenue from corporations, it has the option to either raise the corporate tax rate, expand the corporate tax base, or do both.

Increasing the corporate tax rate is legislatively and administratively simple—firms would multiply their current tax base by a higher rate, and remit more tax. The distortions caused by the corporate tax would increase as the rate is increased, and because that higher tax is borne by consumers, capital owners, and/or employees, individuals will be affected by the increased corporate tax rate. However, no additional regulations, administrative procedure, etc., would be required. Raising the corporate tax rate is a trade-off between balancing the generation of additional revenue and the well-known economic distortions associated with taxation. And while it certainly has fairness implications, I believe most concerns over fairness relate to misperceptions about the tax base.

When I hear concerns that corporations are not paying their “fair share” of taxes, many relate to the tax base. That is, to some it feels unfair to see a company that is perceived to be “big,” “successful,” or “profitable” not paying what one views as enough in taxes. These perceptions are frequently spurred by political rhetoric, because on their own, very few people spend much time pondering the size of corporate tax payments (Asay, Hoopes, Thornock, and Wilde 2021).

PERCEIVED UNFAIRNESS CAUSED BY MISPERCEPTIONS ABOUT FINANCIAL AND TAX ACCOUNTING

Much of the perception about corporate tax fairness follows from the fact that corporations compute profits in more than one way. One way in which corporations compute profits is according to the rules of the Internal Revenue Code. Congress creates these rules with at least three different goals: (1) raise revenue, (2) change taxpayer behavior, for example by incentivizing activities such as the R&D tax credit and the immediate expensing of investments in capital assets, and (3) redistribute income. Another way in which corporations compute profits is according to Generally Accepted Accounting Principles (GAAP). These rules, created by the Financial Accounting Standards Board (FASB), lay out rules for calculating income, the purpose of which is to inform stakeholders, such as investors, about the firm. The FASB is not concerned with collecting revenue, and, if firms change their behavior because of specific accounting rules, to some extent, the FASB considers it a failure—the FASB seeks only to accurately measure income produced by firms (Belnap, Dyreng, and Hoopes 2019).

This mismatch between financial accounting income and taxable income frequently leads to allegations of “unfairness.” In my view, focusing on the gap between taxable and book income belies a fundamental misunderstanding of the purpose of the two different accounting systems. Expecting a firm to be profitable under the U.S. tax code because it is profitable under U.S. GAAP is akin to asking two different artists to draw the same picture, but give them different sized paintbrushes and different color paints, and expecting the pictures to look the same. Further, the reasons many U.S. firms can show profits under GAAP but remit no tax are well-known, well-understood, and, often created explicitly by Congress. Surely some companies engage in aggressive, sometimes even illegal, tax practices, but the estimates we have available to us suggest that the revenue loss from illegal practices is not as large as from tax expenditures and other legal allowances of the tax code. Further, these allowances are not secrets. U.S. firms above a certain size have to file a Schedule M–3 with the Internal Revenue Service which outlines the differences in taxable income calculated under the tax code and financial accounting income (Mills and Plesko 2003). The aggregate values of these differences are dis-

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4 See https://www.pewresearch.org/politics/2017/04/14/top-frustrations-with-tax-system-sense-that-corporations-wealthy-dont-pay-fair-share/ for evidence on perceptions of tax fairness from 2017. Since then, the statutory corporate tax rate was reduced.

5 Interestingly, Amazon, a specific case which has drawn much attention, especially in 2018, and was one motivation for the Real Corporate Profits Tax (see https://elizabethwarren.com/plans/real-corporate-profits), reported much less in Federal tax than one might expect from their accounting income as a result of flawed financial accounting rules, rules flawed as a result of political pressure being put on the FASB (Zeff 2005). Such political pressure on the FASB would likely intensify if we were to tax book income. For details, see https://tax.unc.edu/index.php/news-media/why-didnt-amazon-pay-any-taxes-despite-having-huge-profits/.

6 Further, public firms in the U.S. must publicly disclose the difference between 21 percent of their pretax income calculated according to U.S. GAAP, and, their actual GAAP effective tax

Continued
closed by the Internal Revenue Service. Below, I describe some of the biggest differences. I use data from the 2017 Statistics of Income Line Counts, as these are the most recent data available from the IRS.7

The M–3 lists many different items of revenue and expense (deductions) that are different for tax and financial accounting purposes. The largest difference is depreciation. U.S. corporations claimed $470 billion of depreciation expense according to their income statements (after adjusting for consolidation difference between book and tax accounting, which is also outlined on the M–3).8 However, due to rules for depreciation deductions (cost recovery) set by Congress, U.S. firms claimed $617 billion in depreciation deductions on their tax returns, a $147 billion difference. Over time, increasing with the Tax Cuts and Jobs Act, Congress has made the rules for tax depreciation more and more generous, allowing for faster and faster depreciation. This was an intentional act of Congress, aimed at increasing investment among U.S. firms. Research suggests that more generous depreciation increases investment, especially for smaller firms (e.g., House and Shapiro 2008; Zwick and Mahon 2017).

After generating a preliminary computation of taxable income by offsetting receipts against deductions, firms include the effects of any net operating losses. U.S. tax law gives the ability to offset tax losses against the income of other periods.9 This allows firms to use tax losses from other years recognizes that a 1-year accounting period is an arbitrary feature of our tax code. Research suggests that the use of NOLs does encourage corporate investment in risky investments, which is important for economic growth (Langenmayr and Lester 2017). In 2017, firms used a total of $155 billion in net operating losses to reduce their taxable income before NOLs.

After subtracting net operating losses, businesses multiply this tax base by the corporate statutory tax rate. After arriving at this preliminary tax amount, firms subtract tax credits. One such example is the R&D tax credit, which provides incentives for companies to engage in research and experimentation. Academic studies suggest the credit is effective in spurring additional research (e.g., Bloom, Griffith, and Van Reenen 2002; Rao 2016).10 This credit was intentionally enacted into law by Congress to change corporate behavior.11 In 2017, $12 billion of R&D credit were claimed by U.S. firms. The sum of all general business tax credits in 2017 was $32 billion. As these are credits that reduce taxes on a dollar by dollar basis, at a 35 percent tax rate (which was the rate in the year these data are from), that is equivalent to a $32/0.35 = $91 billion tax deduction.

Of the $388 billion in corporate taxes reported on Form 1120 in 2017, just these three items, NOLs, depreciation deductions, and general business credits, account for the equivalent of $394 billion in tax deductions, creating $138 billion in lost revenue in 2017. This lost revenue is the result of explicit allowances in the Internal Revenue Code made by Congress.

The differences between book and taxable income discussed above are all legal and simple applications of U.S. tax law, as passed and intended by Congress. To

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7 These values will certainly change as a result of the tax reform of 2017, but the message I am trying to convey with these values remains the same. These data can be found here: https://www.irs.gov/pub/irs-pdf/p5108.pdf.
8 While accelerated depreciation is allowed in many other countries for some types of assets, the U.S. is somewhat more generous than other nations with regards with its depreciation rules. See https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/tax/guides/ey-worldwide-capital-and-fixed-assets-26-aug-2020.pdf?download. Recognizing the incentives it creates, several nations have enacted more generous depreciation rules in response to the COVID–19 pandemic, at least with regards to some types of assets.
9 The use of losses from one period to offset income in another period is extremely common in other countries (Bethmann, Jacob, and Muller 2017), as well as U.S. States (Ljungqvist, Zhang, and Zoë 2017). Many countries, including the U.S., made these rules more generous in response to the COVID–19 pandemic (Gallemeer, Hollander, and Jacob 2020).
11 Incidentally, the R&D tax credit was enacted more than a dozen different times, as this is one law that Congress historically only maintained on a temporary basis, historically contributing to tax policy uncertainty (Hoopes 2018). The R&D credit has been made permanent, but many other corporate tax laws are temporary. I know of no reasonable economic rationale for these provisions being temporary.
my knowledge, there is no widespread demand for the repeal of these measures. Yet, they create the large gap that some decry as "unfair." However, some firms certainly engage in tax planning solely with the purpose of reducing their taxable income. Most of this planning is plausibly legal by large, public corporations, but, may not be what Congress intended when they passed the tax law. And, certainly, some corporate tax planning ultimately is determined to be illegal tax evasion. Many of these planning strategies involve shifting income to foreign jurisdictions. Most estimates of income shifting come from before the 2017 regime shift. One estimate suggests that the U.S. loses 4–8 percent of corporate tax revenues from income shifting (Blouin and Robinson 2021). In 2017, corporate tax revenue was $388 billion, suggesting $16–31 billion in revenue was not collected.12, 13 Even the most extreme of estimates of profit shifting pin 2017 estimates of profit shifting at $100 billion, still less than the three tax provisions I mention (Clausing 2020a). To be clear, amending the tax code and stronger enforcement of the tax code may help stem profit shifting to some extent, but, that is simply not where most revenue is lost.

Note that these estimates are generated from before the 2017 tax reform change, before what Clausing (2020b) calls "adjustment to the legislation."14 The primary motivation for international tax planning is facing a high tax rate, and prior to 2017 the U.S. statutory corporate tax rate was one of the highest in the world. Further, the U.S. was one of the only developed countries with a worldwide tax system, which imposed this high tax rate on earnings abroad. Now, with a nominally territorial system and a lower corporate statutory tax rate, companies are reconfiguring their structures, and, determining how to operate in response to the current tax code.15 Further, the estimates of income shifting I mentioned above were generated before the OECD had fully implemented its BEPS project, which may also have curtailed some profit shifting. It is too early to know the TCJA’s net effect on aggregate profit shifting until more time lapses (although estimates that included 2020 data would be useful, but, to my knowledge, do not exist). As such, these estimates from before 2017 are not fully informative regarding the size of the problem now. However, even if tax-motivated income shifting by U.S. multinationals is as large a problem as it was before the TCJA, the estimates of income shifting are smaller, and some significantly smaller, than the figures I previously reported associated with the use of NOLs, tax credits, and accelerated depreciation.

**TAXING BOOK INCOME**

Owing to the perception that corporations don’t pay a “fair” amount of tax after arriving at taxable income according to the tax code and financial earnings according to U.S. GAAP, one solution to ensure that this perceived unfairness does not persist would be to fix whatever perceived flaws there are in the tax code so that firms pay a higher amount in tax. However, recently, rather than directly addressing the problem, several proposals have been floated that would include financial accounting income, in some form, in the corporate tax base—proposals that would tax book income. The intuition asserted by proponents of taxing book income is that corporations are incentivized to report high financial accounting income to shareholders, but a low taxable income to the IRS, such that incorporating financial accounting income directly into the tax base would net the two opposing incentives out. The empirical evidence, however, does not support this. Among other reasons, we should not include financial accounting in the tax base because to do so would distort the financial accounting process and politicize the FASB. Further, it is highly unlikely that it would persist as a permanent feature of the U.S. system, contributing to tax policy uncertainty, as evidenced by the fact it has been tried before as part of the Tax Revenue Act of 1986 but was soon after allowed to expire.

12 Consistent with this narrative, recent research highlights more precisely why many seemingly profitable firms pay nothing in tax (van der Geest and Jacob 2020). The paper finds that these “zero-tax firms” account for nearly 15 percent of listed firms in recent years. However, these firms achieve this outcome not as result of tax planning, but, rather, through NOLs and nontaxable income. International tax planning plays a minor role in the outcomes of these zero-tax firms.

13 These estimates, although regarding a different underlying construction, are consistent in terms of the order of magnitude of the problem with the IRS’s own estimates of the total net tax gap for corporations being $32 billion for the most recent time period covered by the tax gap estimates (see https://www.irs.gov/pub/irm-pdf/p5365.pdf).

14 There are some estimates for income shifting following 2017, but, many involve numerical simulations, and none use data from after the tax system actually settled into its new equilibrium.

15 The lower tax rate should encourage less income shifting, while the territorial tax system may encourage more planning, but, that increase should be checked, at least to some extent, with features like BEAT and GILTI.
Including financial accounting income in the tax base would distort financial accounting income. For example, when GAAP income was previously included in the tax base, companies made financial accounting choices that altered the communication of financial information and deteriorated the financial information available to investors (Kamlin 1991; Dhalliwal and Wong 1992; Hanlon, Dobbins, and Plesko 1992; Manzon 1995). Recent reevaluation of previous studies of the issue confirm their original findings, and suggests financial accounting income may be even more sensitive to the tax rate than is taxable income, because the accrual estimation process affords more subjectivity to book reporting (Dharmapala 2020). These types of accounting choices lower the quality of financial accounting income, making it harder for investors to really understand what is happening at a firm (Blaylock, Gaertner, and Shervin 2015; Hanlon, Laplante, and Shervin 2005).

This discussion of taxing book income is not the first time the U.S. has attempted to include book income in the tax base. The Tax Reform Act of 1986 included a tax that included book income in its base, the Business Unreported Reported Profits (BURP), and is the setting of some of the previously mentioned research papers. The financial accounting literature is unified in finding that, in response to the BURP, firms managed earnings to lower financial accounting income.16 This short-lived provision altered firm’s financial accounting choices. There is reason to believe that if book income was once again included in the tax base, the same results would occur. In fact, it is likely that the manipulations to financial accounting income would be even more severe now, since, unlike in the late 1980s, firms now have a popular and credible alternative method of reporting their success to shareholders, which would reduce the financial accounting costs of lowering book income in response to a tax on book income. This alternative method of reporting income to investors, called pro-forma, non-GAAP, or street earnings, is much more common now that in the late 1980s, and, would be difficult to regulate. Non-GAAP disclosures would provide an alternative method for firms to communicate profits unaffected by the tax on book income, but would damage the comparability and effectiveness of financial reporting, and negatively impact capital markets.

Further, while the tax on book income has been advertised as simple, its actual implementation would be administratively difficult. Many important nuances would arise that need to be sorted out in a costly regulatory process, and, this regulatory process may well make the system much more favorable to firms than at first anticipated.17 With the BURP, for example, regulatory guidance for implementation of the tax was still actually occurring after the BURP was no longer law.18

Finally, while a tax on book income would decrease the value of the financial accounting earnings signal to financial markets, it may also have the side effect of politicizing the Financial Accounting Standards Board (FASB), the creators of U.S. GAAP. The SEC does have official oversight of the FASB, but the FASB has, with a few notable exceptions (Zeff 2005), remained politically neutral. Its independence and political neutrality are key to its status as a highly respected standard setting body throughout the world. If the product of FASB deliberation was included in the tax base and had the ability to alter cash flows for firms, it seems plausible that the decisions of the FASB may be less independent. This would further erode the value of the earnings signal (Hanlon and Shervin 2005).

Finally, like the BURP, and the corporate AMT generally, I do not think a tax based on book income would persist as a viable tax instrument for long, in large part as a result of the negative outcomes outlined above. While corporations, as ev-

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16 In addition to the academic accounting literature being unified in finding negative effects of taxing book income, academic accountants themselves are also fairly united in opposing taxing book income. In 2018, I did an informal, but anonymous, survey of about 100 accounting academics, and of the 39 that responded, 39 opposed a tax on book income. See https://tax.unc.edu/index.php/news-media/what-do-academic-accountants-think-of-senator-warrens-real-corporate-profits-tax/ for more details.

17 As You (2017) notes, nearly half of lobbying activity aimed at specific legislation takes place after actual legislation as groups lobby to sway the implementation of the bill.

18 For a detailed understanding of the tax, it would be important to know the details of the tax proposal, and we simply don’t have enough information. For example, how are private firms taxed? If the tax only applies to public firms with GAAP audited financial statements, that would provide incentives for public firms to go private, eliminating the possibility of investing in these firms to average retail investors, while preserving this opportunity for the wealthy, which can invest in private equity. If the law allowed other bases other than GAAP audited pretax income, then the base would be much more manageable, and, the tax less effective. For other examples, see https://tax.unc.edu/index.php/news-media/what-to-do-with-danaos-an-application-of-the-real-corporate-profits-tax/ and https://tax.unc.edu/index.php/news-media/what-to-do-with-disney-an-application-of-the-real-corporate-profits-tax/.
Wealth taxes

Like with corporations, there is a common perception that wealthy people do not pay their fair share of taxes. And, like with corporations, this outcome is often an unintended consequence of the tax system, not, in large part, because of tax planning in ways not intended by Congress. For example, the tax system in the U.S., and elsewhere, is based on the principle of realization, meaning that taxpayers do not pay taxes on unrealized income. For example, no matter how high a stock’s price soars, under current tax law, a taxpayer would not be liable to pay taxes on that gain if she persisted in holding the stock—she is taxed only at the time of sale. This fundamental principle of taxation is responsible for many of the most commonly cited examples of wealthy individuals paying relatively little tax. When large wealth is observed for individual taxpayers without a concomitant payment of tax, one proposal has been to tax wealth directly. This is, incidentally, another alternative would be to simply refine the taxation of the current ways that the very wealthy are able to access cash without actually immediately realizing capital gains, such as variable prepaid forward contracts. However, such limitations on the very wealthy accessing tax-free cash may not have a large impact on tax revenue or perceptions of fairness, as the cash that the very wealthy need to finance consumption can sometimes be a very small fraction of their total wealth. Nevertheless, such options should be considered.

The wealth tax, as proposed, has been described as simple. In practice, these taxes are not simple. For example, Schueer and Slemrod (2021) note, “all wealth taxes exempt wealth below a certain threshold, which varies considerably across countries. Some wealth taxes do not apply to wealth held in a pension or life insurance account. Some have exemptions or reduced tax rates for the wealth in one’s primary residence; more generally, wealth tax rules often differ across real estate and financial assets. There are reduced or deferred wealth taxes for certain business assets—for example, to prevent a situation where a family owned firm would need to be liquidated to satisfy a wealth tax liability. Wealth tax bases often leave out trusts established to pass wealth to later generations. Finally, wealth taxes have not been applied to implicit wealth in the form of an individual’s human capital, although this is sometimes hard to disentangle from the value of business partnerships (such as law firms or doctors’ practices).”
There are also concerns that wealth taxation would cause unintended consequences, and, when thought of as income taxes, wealth taxes would be perceived by many as themselves “unfair.”

Broad wealth taxes depend on wealthy individuals disclosing and valuing their assets. These valuations are highly subjective, and it would be administratively very costly and time-consuming for the IRS to challenge.\textsuperscript{24, 25} Similar valuations are currently done in the context of the current estate tax, and, are often contentious and costly to challenge.\textsuperscript{26} However, unlike the estate tax, where each taxpayer only dies once, such that the estate tax is triggered only once, such valuations would need to be done on an annual basis for the wealth tax.\textsuperscript{27} Recent research confirms that the wealthiest individuals are able to hide their wealth in ways that even the most rigorous IRS audits (more rigorous than standard operational audits) simply cannot find, and, confirms that the wealth tax would be ripe for income tax evasion for those willing engage in such activities (Guyton, Langetieg, Reck, Risch, and Zucman 2021). The evadability of this tax would also make its application inequitable, with those holding wealth in forms that are difficult to conceal, and those unwilling to illegally conceal, bearing more of the burden of this tax than those holding other types of wealth. In short, the administrative and enforcement costs, compared to the revenue generated make this tax an unattractive option to raise revenue.

There is also some empirical evidence on the effects of wealth taxation with regards to taxpayer mobility. As the U.S. has never really had a wealth tax, this evidence comes from other countries, where the intuitional setting may be very different, so it is hard to know how generalizable these findings are.\textsuperscript{28} But, in general, as summarized by Scheuer and Slemrod (2021), “Studies of the European wealth taxes often, but not always, find a substantial behavioral response.” The U.S. case may be different because the U.S. is a larger country and potentially harder to flee, but, on the other hand, the dollar values at stake are much, much larger in the U.S. context.

Next, the wealth tax, when thought of as an income tax, would be perceived by many to be unfair. To convert a wealth tax on the total value of ones assets, one need simply divide the wealth tax rate by the rate of return on the assets being taxed. So, for example, if assets grow at 20 percent, and the wealth tax rate is 2 percent, that is equivalent to a 20-percent annual income tax rate. Alternatively, if asset growth is slow in a year, and returns are 2 percent, and the wealth tax is 4 percent (within the realm of proposed rates in the U.S.), that would be equivalent to a 200-percent income tax in that year.\textsuperscript{29, 30}

Many of these considerations have played a role in the historical failure of wealth taxation. Like the tax on book income, wealth taxes have been implemented in the past, and generally have not persisted. A dozen high-income EU countries have tried wealth taxes, and this form of taxation persists in very few of these countries.

\textsuperscript{24}For one example of a particularly difficult to value asset in an estate tax setting, see https://tax.unc.edu/index.php/news-media/dead-birds-and-taxes/.

\textsuperscript{25}Some have proposed narrowing the scope of the wealth tax to include only assets that are easy to value. This would erode the base subject to tax, as well as create distortions in asset holdings, and difficult to value assets would become tax favored. For example, this would place a tax on bringing a private firm public, and creating a market price for its equity. This would deprive normal retail investors of the ability to invest in as broad an array of firms, leaving some new firms who chose not to IPO to the purview of wealthy investors able to invest the large sums often required to invest in private equity.

\textsuperscript{26}A valuation in one year would certainly be informative for the next year, but taxpayer may intentionally invest in higher-volatility assets that are more difficult to value as a way of avoiding wealth taxation.

\textsuperscript{27}A valuation on one year would certainly be informative for the next year, but taxpayer may intentionally invest in higher-volatility assets that are more difficult to value as a way of avoiding wealth taxation.

\textsuperscript{28}There are also papers on income taxes on high-income individuals, but, as I view an income tax as fundamentally different than a wealth tax, I do not find this evidence as particularly relevant. However, this literature does find some mobility effects with regards to high-income taxpayers facing taxes targeting high income taxpayers. See https://tax.unc.edu/index.php/news-media/do-billionaires-move-to-avoid-taxes-what-does-the-evidence-say/ for examples.

\textsuperscript{29}Some wealth tax systems have capped the wealth tax at measures of disposable income. While this can eliminate the problem of absurd tax rate, it adds complexity to the system, and, generally would lead to the ultra-wealthy being perceived as undertaxed, as the disposable income of a multi-billionaire may not be that different than the disposable income of a mere multi-millionaire.

\textsuperscript{30}In general, these extremely high income tax-equivalent rates would happen in bad economic times, which is the opposite of the pro-cyclical nature of the income tax.
The wealth tax failed to succeed in these countries even when the stakes were relatively low—in EU countries in which wealth taxation existed, never was the tax levied at the level considered in recent proposals in the U.S. (Scheuer and Slemrod 2021).

Finally, the tax would be subject to claims of unconstitutionality. Constitutional scholars have asserted that the wealth tax may be unconstitutional (Jensen 2019; Hemel 2019), or constitutional (Johnsen and Dellinger 2018; Glogower 2020). In my opinion, all the arguments of these scholars really confirm is that there are arguments to be made on both sides of a hotly contested issue, and, if legislated, the wealth tax would end up being tried in court, and would create administrative havoc as the case wound its way through the court system. Further, regardless of whether the law would be struck down in court, like the tax on book income, the law has so little bipartisan support that it seems extremely likely that it would be eliminated legislatively if the courts did not eliminate it. This would contribute to the instability in our tax system.

CONCLUSION

My message is that most of the ways in which large corporations and wealthy taxpayers remit taxes at a level the general public may perceive to be “unfair” are legal methods intentionally legislated by Congress. The income tax in actuality is very broad. However, Congress has legislated many exceptions to its broad ability to collect taxes. If members of Congress seek to raise additional revenue in order to expand the size and scope of government and combat perceptions of fairness, they should start by examining the many items that are currently labeled as “tax expenditures” by the Treasury. Rather than layer on fundamentally new tax systems, members of Congress should call out specific provisions they believe should be changed, take them to the court of public opinion, and, change those provisions. Plastering over a broken tax code with other fundamentally flawed laws, which have been used previously and failed, is not good tax policy.

REFERENCES


31 For example, according to Scheuer and Slemrod (2021), the Sanders wealth tax would raise 1.56 percent of GDP in taxes, and the Warren wealth tax would raise 1.34 percent. For comparison, the wealth tax in Demark raised 0.06 percent of GDP, in Iceland 0.48 percent, and in Switzerland raises 1.08 percent. For more details on why specific EU countries decided to abandon these taxes, see https://www.oecd.org/publications/the-role-and-design-of-net-wealth-taxes-in-the-oecd-9789264290303-en.htm.

32 This exact scenario is currently playing itself out in Argentina, which recently passed a wealth tax. See https://news.bloombergtax.com/daily-tax-report-international/wealth-tax-sends-argentinas-rich-to-court-in-last-minute-fight.

33 In my view, the opinion of Larry Summers on this point is useful: Summers recently noted that spending time on “a proposal that the Supreme Court has better than a 50-percent chance of declaring unconstitutional, that has very little chance of passing through the Congress, whose revenue potential is extraordinarily in doubt . . . seems to me to potentially sacrifice an immense opportunity.” See https://thehill.com/policy/finance/466813-former-clinton-treasury-secretary-knocks-wealth-tax-very-little-chance-of.


My direct ancestors, regrettably, were never successful enough farmers, or successful at anything, for that matter, to have anything of great monetary worth to pass down to any future generation.

According to 2019 IRS data, there were 269 estate tax returns with a positive tax liability that had any farm assets. A farm asset is very different than a farmer—for example, Bill Gates has billions of dollars of farm assets (https://nypost.com/2021/02/27/why-bill-gates-is-now-the-us-biggest-farmland-owner/). Many, if not most, if not all, of these “farm assets” could simply be held as part of a real estate portfolio by people who have no active involvement with actual farming. And, even if it does include some farmers who actively farm on real farms, all this says is that they paid some estate tax, not that they lost their farm as a result of the estate tax. Farm assets from taxable returns appear to be a tiny fraction (1.72 percent of all assets). The average “farm asset” is worth $4.9 million. I emailed the American Farm Bureau asking if they had any examples of farmers who lost their farms because of the estate tax, but received no reply. In 2001, they could allegedly provide no examples of a farm being lost because of the estate tax (https://www.nytimes.com/2001/04/08/us/talk-of-lost-farms-reflects-middle-of-estate-tax-debate.html).


Questions Submitted for the Record to Jeffrey L. Hoopes, Ph.D.

Questions Submitted by Hon. Bill Cassidy

Estate Taxes

Question. Senate Majority Leader Schumer has stated, with regard to the estate tax “… any organic business—a farm, a small business, and frankly a large business—that would have to be broken up because of the extent of the tax should not be. A business is an ongoing organism. It employs sometimes 10 people and sometimes 10,000 people. To have to break that business up to pay any tax, to me, is counterproductive.”

Do you agree that the tax code should not inhibit owners of any size business from being able to pass along that business, in full, to future generations?

Answer. My children’s great, great, great, grandfather, Lot Adams, after whom my youngest son is named, was born in England, but, after having immigrated to the U.S., and facing religious persecution, went to the safety of the Rocky Mountains. He filed a Homestead Act claim, and, established a farm in Riverside, ID. My wife’s grandfather, Bill Adams, as hard-working a man as I ever knew, celebrated a century of his family being on that same farm in southeastern Idaho, with the designation of an Idaho Century Farm, in 1986. He lived there until he died, with his work gloves on, in 2018, and, his son now lives at the farm. I have at least some understanding of what it means to keep a farm in the family. The current Federal estate tax has many provisions enacted with the intention to allow farmers to not have to liquidate farm assets to satisfy the estate tax, and, given these provisions, as well as the very high current threshold below which no estate tax is owed, family farms are rarely, if ever, liquidated to satisfy the estate tax. This is not to say farmers are not burdened by the estate tax, and would be better off without it—they are burdened, and would be better off without it. I support provisions that allow for some assets to be transferred between generations tax-free, as currently exist. Assuming the need for an estate tax, I also support provisions that allow those estate taxes to be paid over long periods of time for those with non-liquid, closely held assets, such that returns from assets may be used to satisfy the tax debt, as opposed to the proceeds from the sale of the assets themselves, as currently exist.

My direct ancestors, regrettably, were never successful enough farmers, or successful at anything, for that matter, to have anything of great monetary worth to pass down to any future generation.

According to 2019 IRS data, there were 269 estate tax returns with a positive tax liability that had any farm assets. A farm asset is very different than a farmer—for example, Bill Gates has billions of dollar of farm assets (https://nypost.com/2021/02/27/why-bill-gates-is-now-the-us-biggest-farmland-owner/). Many, if not most, if not all, of these “farm assets" could simply be held as part of a real estate portfolio by people who have no active involvement with actual farming. And, even if it does include some farmers who actively farm on real farms, all this says is that they paid some estate tax, not that they lost their farm as a result of the estate tax. Farm assets from taxable returns appear to be a tiny fraction (1.72 percent of all assets). The average “farm asset" is worth $4.9 million. I emailed the American Farm Bureau asking if they had any examples of farmers who lost their farms because of the estate tax, but received no reply. In 2001, they could allegedly provide no examples of a farm being lost because of the estate tax (https://www.nytimes.com/2001/04/08/us/talk-of-lost-farms-reflects-middle-of-estate-tax-debate.html).
In my opinion, claims of businesses, farms, etc., being broken up because of the estate tax are generally overstated. Business are rarely broken up because of the estate tax, partly because of costly and counterproductive estate planning that those subject to the estate tax engage in. In my view, opposition to the estate tax should not hinge on the fact that it, in fact, breaks up business, as this is relatively rare, but that it engenders costly and counterproductive tax planning for relatively little revenue ($12 billion or so a year), that it disincentivizes saving, and other reasons.

**DOUBLE TAXATION**

**Question.** New York Democratic Representative Jerry Nadler recently tweeted, “No one should ever be taxed twice on the same income. It’s not fair and it’s not just.”

Do you agree with this view? If not, why not?

**Answer.** Accounting, economics, or tax law, those areas in which my knowledge qualifies me to opine on this question, do not define “fair” or “just,” so I cannot opine on whether double taxation is fair or just.

In some contexts, the term “double taxation” is meaningful. For example, corporate income is taxed at least twice, once as a result of the corporate income tax, and the second time as a dividend or capital gains tax. The term “double taxation” is useful in this context because there are alternatives to corporations which are taxed only once, at the individual level (instead of twice, at the entity and individual level). But, as applied to individuals in many cases, such as the example from Representative Nadler, generally when people talk about being taxed twice, they really mean they are facing taxes they don’t agree with, and need some rhetorical devise to use against the unliked tax. You often can’t meaningfully count the number of times income is taxed.

For example, I work for UNC, and am compensated by UNC. I pay Federal and State taxes on that income. With that income, for example, I have bought a used truck. I paid a sales tax on the truck upon purchase, plus recurring taxes/fees to the State to license the vehicle. I pay gas taxes at the Federal and State level to keep the truck running on roads I sometimes pay taxes (tolls) for the privilege to drive on. I could also buy stock with that same income. As an owner of a corporation, the income of my corporation is subject to the corporate income tax at the State and Federal level. Even if I realize no real increase in value (my rate of return is less than the interest rate), I may pay capital gains taxes on the illusionary capital gain when I sell the stock. In some alternative world where I had more than $22 million in net estate that would be subject to the estate tax, all that was left of that income, and all I bought with it, would be taxed upon my death. In yet another alternative reality where a future democratic Congress passed a wealth tax, I may pay annual taxes on all assets I own.

How many times would my UNC income, which enabled all of the activities above, be taxed? It does not matter. Good tax policy should not be evaluated on the number of times income is taxed, but, rather, whether any given tax meets the objectives that society has for a good tax. Another way to think about this is this: is taxing the same income twice at 10 percent any different than taxing it once at 20 percent? Not really. But we would all prefer 10 percent to 20 percent, at least if it is our income being taxed!

Incidentally, Representative Nadler was speaking of the limitation on the SALT deduction when talking about double taxation. The Republican-passed Tax Cuts and Jobs Act limited the ability of the very wealthy to deduct their State and local taxes. That Democrats often lament that the wealthy are not paying their “fair share” of tax, while simultaneously arguing that the wealthy should get a tax deduction for paying property taxes on houses far out of reach of the middle class, represents the support of two inconsistent ideas.

**HISTORY OF ULTRA-WEALTHY TAXES**

**Question.** Some taxes have been passed by Congress on the basis that they would largely target the ultra-wealthy and then have gradually been expanded to include a larger set of taxpayers.

Can you comment on this history?

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Answer. Taxes are often aimed at the very wealthy initially, to get buy-in in a democracy, and then applied to more and more taxpayers. We have seen evidence of this buy-in seeking process recently with promises by Democratic politicians that they would not raise taxes on anyone making under $400,000,\(^4\) that a wealth tax would only apply to 75,000 households,\(^3\) or, that the tax on book income would only apply to only 45 companies.\(^6\) The main virtue of these taxes seems to be that someone else will pay them. As Senator Russell Long noted, a mantra of Democratic tax reform seems to be “Don’t tax you, don’t tax me, tax that fellow behind the tree!”

However, these taxes often expand to affect more taxpayers. This certainly happened with the income tax. Initially, less than a few percent of the population had an income tax liability, and the top rates were very low. Then, that rate crept up and up as the government expanded, more and more activities fell into its scope, and, politicians realized they could spend more money. World War II dramatically exacerbated this effect, turning the tax from a class tax, into a mass tax.\(^7\) Another example is the individual AMT, which started as a tax aimed at only the very rich, but, which ended up affecting millions of taxpayers each year in 2017\(^8\) (before it was changed by the TCJA,\(^9\) which dramatically reduced the number of taxpayers affected).\(^10\)

**TAXING BOOK PROFITS**

*Question.* U.S. companies generally prepare two measures of income each year, financial accounting or book income and taxable income. These two measures of income are distinct and separate as they serve different purposes and are intended for different audiences.

Can you explain the reason for these two standards, and do you think a difference between these two measures necessarily means that companies are doing something nefarious?\(^2\)

*Answer.* Financial accounting standards exist so that investors, and others, can judge the economic well-being of a company. The tax law exists to collect revenue from taxpayers, to change taxpayer behavior, and to redistribute income. A difference between these two measures is built into the system because of their different purposes, and if the two measures were identical, I would suspect something odd was going on at a company. They are not meant to be the same, as they are different measures. Anyone observing a difference in the two measures and suggesting something nefarious fundamentally misunderstands the tax system, or is deceptive.

**TAX INCENTIVES**

*Question.* In order to incentivize U.S. investment in capital expenditures like machinery and equipment, the Tax Cuts and Jobs Act provided the ability for American businesses to expense certain capital assets, like manufacturing equipment. Businesses may also receive a tax credit for R&D expense, which has historically received significant bipartisan support. On the other hand, book income requires deducting assets over a longer period of time, and it does not allow credits, which creates significant differences between book and taxable income.

If Congress has provided a tax incentive, like expensing of capital assets or R&D credits, what is the effect of imposing a minimum tax on book income?\(^2\)

**Answer.** It depends on whether you allow those items to be added back to a minimum tax on book income. Currently, President Biden’s proposal allows taxpayers to adjust for the value of general business credits, which, in my mind, admits that financial accounting income is not a proper base for taxing income, as it has to be adjusted to look more like taxable income before it can be used. If those adjustments were not allowed, it would dampen the incenting effect of these tax incentives with

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\(^1\)https://www.wsj.com/articles/why-biden-would-start-tax-increases-at-400-000-a-year-11601730000.


\(^4\)https://americancentury.omeka.wlu.edu/exhibits/show/creating-the-modern-taxing-sta/from-a-class-tax-to-a-mass-tax.


regards to the entire tax system. Other adjustments may also be added\(^\text{1,1}\) to adjust for the awkward fact that under President Biden’s current tax on book income, settling sexual harassment lawsuits, illegally dumping nuclear waste, or any other illegal activity, is tax deductible.

**BURDEN ON NEW INVESTMENT**

*Question.* Would imposing a tax on book income raise the effective tax burden on new investment and what might be the impact on levels of investment?

*Answer.* Assuming a positive time value of money and that adjustments were not allowed for accelerated depreciation, relative to the current tax code, the tax burden on new investment would be increased. With no assumptions, added corporate income tax could affect investment, especially for financially constrained firms. Net investment would decrease.

**LOSERS**

*Question.* Who are the likely losers if the U.S. was to adopt a “book” income tax like the real corporate profits tax?

*Answer.* Companies who would pay more tax would be losers. Investors who depend on the integrity of the current financial accounting system would be losers. Society which depends on well-functioning capital markets would be losers.

To be clear, the world will not end if we tax book income. Often detractors from a tax proposal make it seem as if not passing that law is the only thing keeping society from spiraling into some kind of Hobbesian nightmare. But, tax book income is an ill-advised tax, and would make us worse off relative to collecting the same amount in tax from corporations in some other way, for reasons I outline in my written testimony.\(^\text{1,2}\)

**BURP**

*Question.* A short-lived tax on book profits was implemented in 1986, and studies have shown that companies altered accounting practices in response to the tax, causing a deterioration in the information environment for both investors and the IRS.

Is it possible to tax book profits without affecting the information environment? Would a worse information environment be a worthwhile price to pay for implementing a tax on book profits?

*Answer.* No, it would not be possible. Companies respond to incentives and will face incentives to manipulate book income if it is taxed. Since a similar amount of revenue could be generated many other ways which, in my opinion, would not impose as large a burden, it would not be a worthwhile price to pay.

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**PREPARED STATEMENT OF KYLE POMERLEAU, RESIDENT FELLOW, AMERICAN ENTERPRISE INSTITUTE**

**FAIR AND EFFICIENT TAX POLICY**

Chair Warren, Ranking Member Cassidy, and members of the committee, thank you for the opportunity to speak today. My name is Kyle Pomerleau, and I am a resident fellow at the American Enterprise Institute, where I research Federal tax policy.

In my testimony, I provide an overview of tax policies lawmakers are currently discussing. I then consider the challenges of two recently proposed policies: a wealth tax and a tax on the book income of corporations. I conclude by discussing alternative revenue sources that I think lawmakers should consider.

**BACKGROUND**

Two major spending packages are currently under consideration. The first, the “American Jobs Plan,” is a $2.7 trillion proposal that includes increased spending on traditional infrastructure, research and development, job training, and long-term...
care. The second proposal is the “American Family Plan.” Although the plan’s details are not yet released, news outlets report that it will include spending on child care, paid family leave, universal pre-K, community college, and an extension of the recently expanded Child Tax Credit.

Lawmakers are contemplating tax increases on corporations and high-income households to finance this new spending. President Joe Biden has proposed raising the corporate income tax rate to 28 percent, raising the tax burden on the foreign profits of U.S. multinational corporations, and enacting a minimum tax on the book income of corporations. The proposal would also replace the base erosion and anti-abuse tax (BEAT) with a new provision called “SHIELD,” which is aimed at preventing profit shifting to low-tax jurisdictions. Finally, it would eliminate several tax provisions for fossil fuel companies.

In addition, the administration plans to increase the top individual income tax rate from 37 percent to 39.6 percent. It will also raise the top capital gains rate from 20 percent to 39.6 percent and make death a realization event for capital gains.

Other lawmakers have introduced proposals to increase taxes on corporations and high-income households. The Senate Finance Committee chairman, Senator Wyden (D–OR), has suggested taxing capital gains mark-to-market for high-income households. Senator Elizabeth Warren (D–MA) has also suggested taxing corporations based on their book income and has a proposal to enact an annual, progressive wealth tax. President Biden, during the campaign, also proposed raising the estate and gift tax.

These proposals would raise trillions in new revenue for the Federal Government and would be highly progressive. However, a few of these ideas pose considerable challenges.

TAXING BOOK INCOME

President Biden has proposed enacting a 15-percent minimum tax on the book income, or financial statement income, of U.S. corporations. Corporations would be required to pay the greater of their ordinary corporate tax liability or 15 percent of their book income. The proposal would only apply to corporations with net income of $2 billion or more. It would allow corporations to reduce their book income with net operating losses and offset their book-tax liability with the foreign tax credit and general business credits such as the research and development credit and green energy credits.

Senator Elizabeth Warren has also proposed an add-on book tax. Warren’s proposal, in contrast, would not be a minimum tax. Corporations would be required to pay a tax equal to 7 percent of their book income each year in addition to the ordinary corporate income tax. The proposal would exempt the first $100 million in net income. It is unclear how Warren’s book tax would interact with the ordinary corporate income tax. Nor is it known whether corporations would be able to offset their book-tax liability with any credits.

**TAXING BOOK INCOME Does Not Necessarily Address Tax Avoidance**

Both proposals are driven by the perception that the large corporations that report low effective tax rates are engaged in aggressive tax avoidance. Recently, the Institute on Taxation and Economic Policy (ITEP) released a report highlighting 55
corporations that reported positive net income but zero or negative Federal tax liability in 2020. Although this result is striking, it is not necessarily evidence of aggressive tax avoidance.

Each year, corporations prepare two measures of income: book income and taxable income. Although both are measures of income, they serve different purposes and are intended for different audiences. Book income follows generally accepted accounting principles (GAAP), as set by the Financial Accounting Standards Board (FASB), and is meant to provide information to investors and creditors about a corporation’s performance. In general, book income tries to align the recognition of income with its associated expenses. And while the FASB prescribes standards, corporations have some leeway in how to account for certain expenses and income.

Taxable income is set by the Internal Revenue Code (IRC) and is prepared for the IRS and is meant to determine a corporation’s tax liability. In addition, the tax code includes provisions that are meant to accomplish other goals, such as encouraging or discouraging certain behaviors. In contrast with book income, taxable income is calculated based on strict rules with little leeway in how revenue or expenses are realized.

In any given year, corporations may have differences in book and taxable income that have little to do with tax avoidance. For example, corporations that benefit from accelerated depreciation may receive large upfront deductions for new investments. In the first year, this will result in lower taxable income than book income. In the following year, the corporation would no longer have any deductions but would continue to deduct the asset for book purposes. This could result in taxable income that is higher than book income.

Taxing book income may result in corporations adjusting book income to avoid taxes. Empirical evidence suggests that taxing book income could reduce the informational quality of book income for investors and creditors. Between 1987 and 1989, the Federal Government used book income to calculate the corporate alternative minimum tax. As a result, firms shifted sales outside the window during which book income impacted tax liability.

**Taxing Book Income Could Undermine Congress’s Policy Goals**

Taxing book income would outsource a portion of the tax code to an unelected nonprofit organization. As mentioned previously, financial accounting income is regulated by the FASB. Any changes that the FASB makes to accounting standards would have a direct impact on the book tax base and Federal tax revenue. These decisions would be made without Congress’s fiscal or other goals in mind. Creating a link between the FASB decisions and Federal revenue will create an incentive for Congress to lobby the board to make or refrain from making changes.

It is unclear why Congress would desire to link tax collections to book income as it would undermine many of Congress’s own policy goals. For example, Congress wanted to limit executive pay by limiting the deduction for compensation. Some limit has been in place since the 1990s. However, companies would be able to fully deduct executive compensation against their book income. A pure book income tax would also disallow credits such as green energy credits.

The Biden administration has already scaled back its book tax for this reason. As mentioned above, Biden’s proposal for a minimum tax on book income allows corporations to offset book-tax liability by using general business credits. This maintains the incentive effects of the credits but weakens the book tax and means it will raise little revenue.

**Taxing Book Income Would Distort Investment Incentives**

Taxing book income would also impact investment incentives in the United States. The impact on investment incentives will depend on whether the tax is a minimum tax or an add-on tax that corporations are required to pay each year.

If a corporation were subject to an add-on book tax each year, as they would be under Senator Warren’s proposal, it would raise the tax burden on new investment.

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Pomerleau, “Joe Biden’s Alternative Minimum Book Tax.”
A significant difference between book income and taxable income is the treatment of capital expenditures or investments. In calculating taxable income, corporations can expense or fully deduct the cost of short-lived assets. Expensing eliminates the tax on marginal investments. In contrast, book income would require businesses to deduct all investments over their useful lives, which would increase the effective tax burden on new investment.

The impact on investment incentives of Biden’s proposal for a minimum tax, on the other hand, would depend on how businesses interact with the tax. Corporations would not be perpetually subject to either the book or the ordinary income tax. They would move between the two systems and may make an initial investment under one tax and face taxes on the returns on that investment under the other tax. Since the tax rates on these taxes are different, the minimum tax may either reduce or increase the tax burden on new investment (Table 1).12

### Table 1. Marginal Effective Tax Rate by Asset, Ordinary Corporate Tax, and Book Tax, 2021

<table>
<thead>
<tr>
<th>Asset</th>
<th>Ordinary Corporate Tax (Current Law and 28% Statutory Rate)</th>
<th>15% Book Tax</th>
<th>Three Years Ordinary Corporate Tax, Switch to Book Tax for Five Years, Back to Ordinary Tax</th>
<th>Five Years on Book Tax, Back to Ordinary Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overall</td>
<td>3.53%</td>
<td>8.75%</td>
<td>−2.15%</td>
<td>13.59%</td>
</tr>
<tr>
<td>Machinery</td>
<td>−10.57%</td>
<td>9.47%</td>
<td>−22.80%</td>
<td>14.07%</td>
</tr>
<tr>
<td>Intellectual Property</td>
<td>−29.06%</td>
<td>−1.99%</td>
<td>−42.22%</td>
<td>0.46%</td>
</tr>
<tr>
<td>Structures</td>
<td>6.37%</td>
<td>9.47%</td>
<td>3.45%</td>
<td>12.66%</td>
</tr>
<tr>
<td>Land</td>
<td>20.38%</td>
<td>9.47%</td>
<td>18.98%</td>
<td>18.64%</td>
</tr>
<tr>
<td>Inventory</td>
<td>25.20%</td>
<td>12.41%</td>
<td>21.06%</td>
<td>20.04%</td>
</tr>
<tr>
<td><strong>Standard Deviation</strong></td>
<td><strong>18.23%</strong></td>
<td><strong>3.91%</strong></td>
<td><strong>22.74%</strong></td>
<td><strong>7.64%</strong></td>
</tr>
</tbody>
</table>


TAXING WEALTH

Several lawmakers have proposed an annual tax on the wealth of very high-net-worth households. During the presidential campaign, Senator Elizabeth Warren proposed a progressive wealth tax that would levy a 2-percent per year tax on net wealth between $50 million and $1 billion and 6 percent per year on net wealth of $1 billion and more. Similarly, Senator Bernie Sanders proposed levying an annual tax on net wealth from 1 percent to as high as 8 percent.

**TAXING WEALTH Would Place a High Burden on Saving**

Supporters of a wealth tax typically argue that the tax places only a low-rate tax on wealth. Senator Warren famously argued that her 2-percent annual wealth tax is a “2 cent” tax. This is highly misleading. A wealth tax taxes a stock of wealth each year. As a result, even at what seems to be a low tax rate, a wealth tax places a significant burden on saving.

The burden a wealth tax places on saving can be measured by the tax wedge it places between pre-tax and after-tax returns. Take, for example, an asset with a pre-tax rate of return of 3 percent. A wealth tax of just 0.2 percent would reduce the return on that asset to 2.8 percent, resulting in an effective tax rate of 7 percent. A more substantial tax rate of 2 percent would reduce the return to 1 percent, for an effective tax rate of 67 percent. A 3-percent wealth tax would result in an effective tax rate of 100 percent.

Reducing the after-tax return on saving could lead to a reduction in national saving. The impact lower savings would have on the economy depends on how open the

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12 Pomerleau, “Joe Biden’s Alternative Minimum Book Tax.”
U.S. economy is to foreign investment. In a closed economy, a reduction in national saving would reduce the amount of saving available to finance productive capital. This would result in a smaller capital stock, lower labor productivity, and, ultimately, lower wages for workers. In contrast, if the economy is very open to foreign investment, the reduction in national saving would result in an inflow of capital from abroad. This increase in lending would lead to an increase in the trade deficit, an increase in foreign ownership of U.S. assets, and ultimately a reduction in national income.

The U.S. economy is open, but it is implausible that the U.S. economy is perfectly open. As a result, we would see a combination of both effects. The wealth tax would likely have a negative impact on the domestic capital stock, wages, and economic output. In addition, it would result in an inflow of foreign capital, an increase in the trade deficit, and a reduction in national income.

Two groups have estimated the wealth tax's impact on the economy and found it would have a negative impact. The Penn Wharton Budget Model found that Senator Warren's wealth tax proposal would reduce gross domestic product (GDP) by 1.2 percent by 2050. The Tax Foundation found that a wealth tax like Warren's campaign proposal would reduce GDP by 0.8 percent in the long run, but because they assume the economy is very open to foreign capital, the wealth tax would reduce national income by 1.5 percent.

**A Wealth Tax's Revenue Potential Is Uncertain**

Proponents of a progressive wealth tax argue that it could raise a large amount of revenue progressively. It would indeed be a very progressive source of revenue, but the amount of revenue a wealth tax will raise remains uncertain. Revenue estimates of wealth tax proposals vary significantly. At the low end, Larry Summers and Natasha Sarin estimate that a wealth tax could raise as little as $366 billion over a decade. In contrast, Lily Batchelder and David Kamin estimate that a wealth tax could raise as much as $5.3 trillion over the same period. The large range of estimates reflects the wide variation in several assumptions.

The amount of revenue that a highly progressive wealth tax will raise depends on how much wealth is held by the wealthiest households. Unlike with income, no administrative data on wealth exists. As a result, researchers must develop methods to estimate the share of wealth held by high-income households. These methods produce a range of estimates of the share of wealth by the top 0.1 percent. For example, using estate tax returns, researchers estimated that the top share of wealth was 10 percent in 2014. In contrast, research that capitalized income reported on tax returns found that the share could be as high as 20 percent.

The amount of revenue that the Federal Government will raise also depends on how taxpayers respond to the wealth tax. In the presence of the wealth tax, taxpayers would have an incentive to reduce their reported wealth. Researchers use elasticities of taxable wealth with respect to the wealth tax rate to estimate this effect. Studies of taxpayer response to the wealth tax have a wide range of elasticities, and some estimates are unrealistically small and imply levels of avoidance that are far lower than the avoidance response we expect from the income tax.

A wealth tax would also reduce the accumulation of wealth and reduce the amount a wealth tax would raise in the long run. One of the stated goals of the wealth tax is to reduce the amount of wealth held by the wealthiest individuals in the United States. For example, economists Gabriel Zucman and Emmanuel Saez estimated that Warren's wealth tax proposal would have eroded the share of total wealth held by the Forbes 400 by more than half if the tax had been in place since 1982. Taxing away this wealth would raise revenue in the near term, but it would erode its own base.

A reduction in wealth would also have a negative impact on other sources of Federal revenue. A large source of individual income tax receipts comes from capital income: capital gains, dividends, interest income, and business income. This income...
represents the returns to wealth. If the total amount of wealth falls due to evasion, avoidance, or reduced saving, total capital income reported to the IRS would also fall.

The wealth tax risks not raising any revenue at all. This is because the wealth tax, if enacted, is likely to face a constitutional challenge. The U.S. Constitution requires that all “direct taxes” be apportioned by the States by population. The 16th amendment exempts the income tax. If courts determine that the wealth tax is a direct tax, it would either need to be apportioned by State population, which would be undesirable, or would be struck down altogether.17 Other taxes would not face this risk.

LAWMAKERS SHOULD FOCUS ON BROADER-BASED TAXES

Given the downsides of taxing wealth and book income, lawmakers should consider other sources of revenue that would be simpler to administer and more economically efficient. Below, I discuss three options: a gas tax or vehicle miles traveled (VMT) tax, a carbon tax, and a value-added tax (VAT).

Gas Taxes and VMT Taxes

A portion of President Biden’s spending proposals include an expansion of infrastructure. Currently, the Federal Government finances most of its infrastructure spending through the Highway Trust Fund (HTF). The HTF provides funding for highways and other capital projects primarily through grants to State and local governments.18 The HTF receives most of its revenue from the 18.4 cents per gallon tax on gasoline and 24.4 cents per gallon tax on diesel fuel.

The taxes and spending associated with the HTF are based on the “benefit principle” of taxation. This principle states that the fiscal costs of a government service should be borne primarily by those who benefit. Since the consumption of gasoline roughly corresponds with the use of roads, it is seen as a fair way to finance road construction and repair. This is not only fair, but it is more efficient. Financing roads with taxes and fees that correspond with driving effectively sets a price on road use. This helps address many of the costs, or externalities, associated with driving such as congestion, noise, and pollution.

According to the Congressional Budget Office, raising the gas and diesel tax by 15 cents per gallon and adjusting it for inflation going forward would raise $291 billion over the next 10 years. Raising the taxes by 35 cents would raise $627 billion over the same period.19 This amount of revenue would cover the current HTF shortfall and raise additional revenue that could be used to finance new infrastructure spending.

That said, the gas tax is not perfect. Motor vehicles are becoming more fuel efficient and can now use less gasoline per mile driven. Motorists can drive as much or more but pay less in tax. In addition, the gas tax does not address road congestion. The cost a driver places on others in an urban area is much higher than in a rural area. As a result, a fixed Federal gas tax will underprice driving in the city and overprice driving elsewhere.20

To address these shortcomings, lawmakers could also consider a VMT tax in combination with a gas tax. A VMT tax would charge drivers based on the miles they travel. As a result, the tax would be less sensitive to increases in fuel efficiency of vehicles. In addition, the VMT tax could vary by location and time of day to address congestion in densely populated areas.21

A Carbon Tax

The Biden administration has also expressed interest in addressing climate change in their spending package. A policy that would simultaneously address this

19 Kile, “Testimony on Addressing the Long-Term Solvency of the Highway Trust Fund.”
21 Congressional Budget Office, Alternative Approaches to Funding Highways.
issue and raise additional Federal revenue would be a carbon tax. A carbon tax is an excise tax levied on the production of greenhouse gas emissions. Most proposals would set the tax at some rate per metric ton, such as $50 per metric ton, and would collect the tax directly from businesses who emit carbon dioxide and other greenhouse gasses.

If considered, a carbon tax should also include a border adjustment that would apply to the embedded carbon emissions from imports and exempt exports from the tax. This would eliminate the incentive for U.S. producers to shift emissions out of the United States and would put a price on goods produced in countries such as China and India that end up being consumed in the United States.

Research from various economists and analysts has found that a carbon tax would reduce greenhouse gas emissions. For example, one economist found that even a $15 per metric ton carbon tax could reduce greenhouse gas emissions by 14 percent. Other researchers found that carbon taxes in European countries have reduced emissions by 15 percent.

While reducing greenhouse gas emissions, a carbon tax also would raise revenue for the Federal Government. The amount of revenue will depend on the rate. However, the Tax Policy Center estimated that a $50 per metric ton carbon tax would raise $2.1 trillion between 2020 and 2029.

A Value-Added Tax

Even before the pandemic and President Biden's spending proposals, the Federal Government faced a fiscal imbalance. A tax favored by economists that could finance new spending and address the fiscal imbalance is the value-added tax, or VAT.

A VAT is a broad-based tax on goods and services. A VAT is like a sales tax, but it is collected in stages along the production process. Take, for example, the process of making bread under a 10-percent VAT. When a farmer sells wheat to the baker for $40, he charges the baker $44 ($40 for the wheat plus $4 for the VAT that the farmer remits to the government). The baker then sells the bread to the consumer for $110 ($100 for the bread plus $10 in VAT). However, the baker gets a credit for the $4 VAT it already paid on the wheat, for a net VAT burden on the baker of $6. The total tax ends up being $10 ($4 paid by the farmer and $6 paid by the baker) on the $100 loaf of bread.

VATs are common globally. Every country in the Organisation for Economic Co-operation and Development (OECD) except the United States raises revenue through a VAT. In fact, more than 160 countries have a VAT. Among OECD countries, the average VAT rate is 19.3 percent and ranges from 5 percent to as high as 27 percent.

A VAT would raise a significant amount of revenue for the Federal Government, but the revenue will depend on how broad the tax base is. According to research by William Gale, a broad-based VAT that covered most domestic consumption could raise $842.4 billion each year or $10 trillion over the next decade.

A VAT would be more economically efficient than the income tax or a wealth tax. A VAT is a tax on consumption. As a result, it does not distort saving or investment decisions like the income tax does. In addition, the VAT is border-adjusted, which means it avoids distorting business' location decisions—businesses cannot avoid the tax by shifting certain assets or income out of the United States.
Enacting a VAT would be equivalent to applying a one-time tax on wealth. Households finance part of their consumption with existing wealth. When the VAT is enacted, the price level would rise by the amount of the tax. This would immediately reduce the value of all existing wealth, and the Federal Government would collect revenue as individuals spend down their wealth. Since this would be a one-time tax on existing wealth, it would not distort saving and investment decisions like an annual wealth tax.

**Addressing Regressivity**

Lawmakers have expressed concerns that taxes such as the gas tax, a VMT tax, a carbon tax, or a VAT would be regressive. Indeed, these taxes would place a larger burden on lower- and moderate-income households as a share of income than high-income households. The Tax Policy Center estimates that in the first year after implementation, a carbon tax would reduce the after-tax income of households in the bottom 20 percent by 2.1 percent. At the same time, the top 20 percent of households would see a reduction in after-tax income of 1.4 percent.

Lawmakers should consider the distribution of the entire fiscal system, not just one tax in isolation. The regressivity of these taxes could be offset with transfers or other tax reductions for low-income households. For example, many advocates of the carbon tax have suggested using some of the carbon tax revenue to reduce taxes or send rebates to low-income households. This would make a carbon tax proposal, on net, highly progressive. In addition, without these taxes, lawmakers would need to make even larger future reductions in programs such as Medicare and Social Security, which would be far more regressive than these taxes.

**CONCLUSION**

President Biden and other lawmakers have proposed a host of tax increases on corporations and high-income households to finance spending. Two revenue-raising proposals have gained prominence over the last couple of years: a wealth tax and taxing the book income of corporations. These taxes come with notable downsides. Lawmakers should consider broader-based taxes to finance new government spending and address the Federal Government’s fiscal imbalance. Raising the gas tax or enacting a VMT tax would be a reasonable way to pay for infrastructure. A carbon tax would help address climate change while raising revenue. A VAT could raise additional revenue with a limited negative impact on the economy.

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**QUESTIONS SUBMITTED FOR THE RECORD TO KYLE POMERLEAU**

**QUESTIONS SUBMITTED BY HON. BILL CASSIDY**

**ESTATE TAXES**

*Question.* Senate Majority Leader Schumer has stated, with regard to the estate tax, “. . . any organic business—a farm, a small business, and frankly a large business—that would have to be broken up because of the extent of the tax should not be. A business is an ongoing organism. It employs sometimes 10 people and sometimes 10,000 people. To have to break that business up to pay any tax, to me, is counterproductive.”

Do you agree that the tax code should not inhibit owners of any size business from being able to pass along that business, in full, to future generations?

*Answer.* The primary goal of a tax system is to raise revenue to finance government spending. Levying taxes requires making tradeoffs because taxes impose costs on the economy and distort economic decision making. Some taxes have a large impact on taxpayer decisions and the economy for each dollar in revenue they raise.

The estate tax, while a highly progressive tax, is a tax that raises relatively little revenue for the distortions it causes. One issue with the estate tax is that it could require taxpayers to sell assets, including business assets, to pay the tax. As a re-
sult, the tax can lead to businesses changing ownership simply for tax purposes. Lawmaker should avoid instituting taxes that can greatly influence taxpayer behavior.

**DOUBLE TAXATION**

*Question.* New York Democratic Representative Jerry Nadler recently tweeted, “No one should ever be taxed twice on the same income. It’s not fair and it’s not just.”

Do you agree with this view? If not, why not?

*Answer.* Whether income is taxed twice or once isn’t necessarily the most important issue. Rather, it’s the total tax burden on that income.

Under current law, the Federal Government levies multiple taxes that apply to the same income. For example, the income tax and the payroll tax both apply to wages and both taxes can apply to the same exact income. However, this is not necessarily a problem. This is because the income tax funds general government services while the payroll tax funds Social Security and Medicare. Likewise, individuals pay Federal income taxes and receive benefits provided by the Federal Government and pay State and local income taxes to receive benefits provided by State and local governments. Two taxes for two sets of benefits.

Rather, lawmakers should pay close attention to the total tax burden they are placing on certain activities. Placing multiple taxes on the same income can raise the effective tax burden on that income and can impact incentives. For example, the total tax burden on corporate income can be high because it faces both the entity level tax and the individual income tax on capital gains and dividends.

A tax like the wealth tax would place an additional tax on the return to saving, which is already taxed under the individual income tax. As a result, the total tax burden under a system with an income tax and a high-rate wealth tax like the one Sen. Warren is proposing could apply effective tax rates over 100 percent on some income.

**EFFECTIVE RATES IF BIDEN TAX PROPOSALS ARE ADOPTED**

*Question.* President Biden has proposed a number of changes to the tax code that would significantly increase tax rates.

Could you estimate the marginal rate a successful medium to large size business of $50 million should expect to face if all of the Biden tax proposals were to become law today?

*Answer.* Under current law, the top marginal income tax rate is 37 percent. In addition, business owners generally need to pay self-employment taxes on income of 2.9 percent plus the 0.9 percent Medicare surtax. On top of that, business owners need to pay State and local income taxes that vary significantly from State to State, but the average is about 5 percent. Considering deductions that taxpayers receive for self-employment taxes and section 199A, the top marginal tax rate on self-employment income under current law is about 37 percent.

Under Biden’s proposal to raise the top marginal tax rate to 39.6 percent, the all-in marginal tax rate on self-employment income would rise to about 39.7 percent.

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**PREPARED STATEMENT OF CHERYL STRAUGHTER, OWNER, SOLEIL RESTAURANT**

Senator Warren, Ranking Member Cassidy, and members of the committee, I want to thank you for allowing me to testify today.

I am not a billionaire, or an ultra-millionaire. I’m not even close. During my life, there have been times where I worried about my status as a thousandaire. I’m the chef and owner of Soleil, a small restaurant located in Boston, MA. I am also a social worker and member of the Boston Black Hospitality Coalition.

I opened my restaurant in 2018, in an area of Boston called Nubian Square. This was a thriving commercial district when I was younger, and I fondly remember shopping with my mother Shirley and boarding the elevated train that once operated all the way downtown.
Over the years, disinvestment the community led businesses and families to leave. But when an opportunity arose to take over a vacant space in the neighborhood, I knew that I wanted to be part of the future of Nubian Square.

I'm proud to run this small business. Along the way to my current role, I've been an employee, a student, and a caregiver. I work hard for myself, my family, my employees, and my community, and I care deeply about all of their well-being.

And that's why it's so important that we have a fair tax system.

I can't say that I enjoy paying taxes, but I am proud to pay them. The revenue collected from our taxes is what we use to pay for the government services we care about: schools, health care, Social Security.

I value those services, and I know they make my community and our Nation better. But the unfairness of the current tax system is what drives people crazy.

At Soleil, and I've got eight employees that work for me. Their incomes are reported to the IRS, and they pay their taxes based on that income, including paying a percentage of their income for Social Security and Medicare. But I know the ultra-rich are different. Their income doesn't usually come from a paycheck, it comes from investments and other holdings. That means that they often pay less in taxes than my own employees. And I know the ultra-rich have a bunch of ways to hide their income or avoid paying taxes on it. That is unfair.

Asking ultra-millionaires and billionaires to pay a small percent of their massive wealth is a no-brainer. If you have a huge fortune, and you benefit from all that this country has provided, you ought to be paying your fair share. It's more than fair that they be asked to pay a small percent of their wealth—and I just can't understand why the wealthiest and luckiest people in the world would be complaining about it being such a hardship.

It's the same with the big businesses that I compete with. They're able to use their resources to lower the amount of tax they pay—like hiring expensive lawyers and accountants, or shifting some of their profits overseas. Many Fortune 500 companies don't pay any taxes at all! It's hard enough to compete and run a business during a pandemic—it's nearly impossible to do that when the tax system is rigged against you.

Our country has many needs right now. A fairer tax system would give us the opportunity to provide affordable child care, create a better education system, and repair our roads. We could provide more support to small businesses, especially those owned by African Americans and other groups that do not have easy access to financing, and make housing more affordable.

These are important national priorities, and they're also things that I want for my family. I know that these investments will make our communities better and stronger, and help our economy grow. That will be good for me, good for my employees, good for my customers, and good for my business and businesses all over the country.

I am happy to answer any of your questions. Thank you for inviting me to today's hearing, and thank you for your work to make our tax system fairer and our Nation stronger.

QUESTIONS SUBMITTED FOR THE RECORD TO CHERYL STRAUGHTER

QUESTIONS SUBMITTED BY HON. BILL CASSIDY

ESTATE TAXES

Question. Senate Majority Leader Schumer has stated, with regard to the estate tax “... any organic business—a farm, a small business, and frankly a large business—that would have to be broken up because of the extent of the tax should not be. A business is an ongoing organism. It employs sometimes 10 people and sometimes 10,000 people. To have to break that business up to pay any tax, to me, is counterproductive.”

Do you agree that the tax code should not inhibit owners of any size business from being able to pass along that business, in full, to future generations?

Answer. I believe the tax code should support small businesses that serve the needs of our communities. For the vast majority of business owners in this country,
I do not believe the tax code inhibits them from passing along their businesses to future generations. It is my understanding that the biggest estates in our country—those that meet the $11.7 million threshold to be subject to the estate tax—are provided with special accommodations to pay any tax they owe in the form of extended time periods and lower interest rates, especially if the estate consists of a farm or small business. Senator Warren's ultra-millionaire tax also includes accommodations for anyone subject to the tax (wealth of more than $50 million) who has liquidity constraints. These kinds of accommodations seem reasonable to me.

DOUBLE TAXATION

Question. New York Democratic Representative Jerry Nadler recently tweeted, “No one should ever be taxed twice on the same income. It's not fair and it's not just.”

Do you agree with this view? If not, why not?

Answer. I believe a fair and just tax system is one that doesn't privilege wealth over work—my employees shouldn't be paying higher tax rates than the wealthiest people in this country just because they work for a paycheck rather than grow their wealth through holding stocks. My small business shouldn't be paying more in taxes than the big corporations just because we don't have expensive lawyers or accountants to help us eliminate our tax liability. We should not have a tax system that allows Fortune 500 companies to not pay federal income tax at all. A fair and just tax system is one that would ensure that everyone is paying their fair share and we have the money we need to invest in communities like mine.

PREPARED STATEMENT OF HON. ELIZABETH WARREN, A U.S. SENATOR FROM MASSACHUSETTS

Good afternoon. Welcome to this year's first hearing of the Finance Committee's Subcommittee on Fiscal Responsibility and Economic Growth. I want to thank our ranking member, Senator Cassidy, for working with me and my team to make this hearing successful.

This subcommittee will focus on how we can create opportunities for every American, build a more equitable economy, and invest in our future prosperity.

President Biden has proposed a $2-trillion infrastructure package, outlining the benefits of investing in roads, bridges, broadband, housing—the things people need to get to work. He's also about to unveil a plan for the caregiving economy, including child care, universal pre-K, and free community college. Current estimates put the price tag of that package at $1.5 trillion.

All these investments would make the lives of millions of people better, but they carry a total price tag of $3.5 trillion, so how would we pay for them? Today, we will address that question by talking about revenues—where the money comes from to build a stronger future.

There are a variety of proposals that would help move us toward that stronger future. I will highlight just three that I have put forward.

First, a wealth tax would impose an annual 2-cent tax on fortunes over $50 million. It would not raise taxes on 99.9 percent of Americans by a single penny. That one tax would bring in $3 trillion.

Second, the Real Corporate Profits Tax would force companies like Amazon, FedEx, and Nike, that make billions of dollars in profits and pay little or nothing in Federal income taxes, to pay more. The Real Corporate Profits Tax would apply only to corporations that report profits to their shareholders and the public of more than $100M. These companies would pay 7 percent of those reported profits—which they use to justify the big salaries and bonuses they pay their CEOs—no matter how many tax loopholes they find or how many scams they run. President Biden has a similar approach. My version would raise about $1.3 trillion.

Finally, I have proposed increasing tax enforcement for wealthy individuals and giant corporations. This plan provides mandatory funding for the IRS that is focused on making sure the rich and powerful get caught when they break the law. Estimates from the Commissioner of the IRS indicated we lose $1 trillion a year from tax cheating. If we stepped up enforcement to cut the cheating by only 20 percent, we could raise as much as $1.8 trillion over the next decade.
These three big ideas alone would raise more than $6 trillion, enough to pay for every single penny of President Biden’s American Jobs Plan, then pay for every single penny of his American Families Plan, and still have more than $2 trillion left over. As these numbers show, our Nation can do both—invest in American families and pay for it without raising taxes on those same families. We can build a country that creates opportunity, not just for those at the top, but for everyone.

These ideas have their critics. In fact, I invited one of the loudest critics—billionaire Leon Cooperman—here today to discuss these proposals with the members of this committee and the American public. After all, that is how democracy is supposed to work: citizens and stakeholders discuss ideas, and then our elected representatives vote. I’m disappointed that Mr. Cooperman decided he was more comfortable taking softball questions on cable news than subjecting his views to debate in the U.S. Senate.

Mr. Cooperman may have been too frightened to come here today, but others were not. Today we are joined by a panel of distinguished witnesses, including several academics and tax policy experts, millionaire Abigail Disney, and small business owner Cheryl Straughter, who have a variety of views on these proposals and are willing to discuss and debate them in public.

A fairer tax system is about making our country better and stronger. It’s about allowing us to make investments in our economy by asking the wealthiest Americans and biggest corporations to pay their fair share.

I’m looking forward to this discussion today, and I thank our witnesses and my colleagues for joining us.
The Association of American Residents Overseas (AARO) welcomes this opportunity to inform the Senate Committee on Finance of the deep concerns of Americans abroad in relation to existing and future U.S. legislation and regulation. AARO is a Paris-based, non-partisan, volunteer, not-for-profit organization that represents the interests of Americans abroad throughout the world, including stateside residents who share our concerns.

Thanks to communication with its active membership of over 1,000 and constant contact with many other overseas Americans throughout the world, AARO is particularly familiar with the issues of interest to Americans abroad. AARO periodically conducts extensive surveys of overseas Americans to determine precisely the nature of these issues and the real-life effect of burdens borne as a result of U.S. legislation, regulation, and the lack of access and support for Americans abroad from public and private entities.

AARO has very recently completed such a survey, which clearly demonstrated that certain U.S. legislation and regulations, particularly in the areas of taxation (as a consequence of citizen-based taxation) and access to financial services (aggravated by the Foreign Account Tax Compliance Act—FATCA—and the current regulations for filing the annual Financial Bank Account Report—FBAR), create serious issues of fairness for overseas Americans. This has led to discrimination against overseas Americans in terms of access to governmental and private sector services as well as the abrupt withdrawal of such services due to the cost of compliance, inherent and irreconcilable conflicts with the law of the country of residence, and access mechanisms that cannot be used because they are solely designed for those resident in the U.S. Our survey data on taxation and banking can be found here\(^1\) and on FATCA and FBAR here.\(^2\)

The increasing seriousness of this situation is demonstrated by the unfortunate sharp increase over recent years of the number of Americans considering or deciding to renounce American citizenship. AARO emphasizes that the decision to renounce citizenship is not solely or entirely taken out a reluctance to avoid U.S. taxation but can reflect the extreme difficulties American taxpayers face when faced with their obligations to the U.S. government as well as the government wherever they reside. This becomes even more acute and potentially decisive when, for example, marriage or other family relationships involving different nationalities and thus conflicting fiscal obligations.

AARO often hears from Americans overseas for a multitude of reasons, including those who feel frustrated in their attempts to familiarize fellow Americans, including their representatives in Congress, with the real-life burdens, resulting from

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their status. Denial of local banking services due to the U.S. imposing extra-territorial compliance obligations for American customers due to FATCA or the forced closure of U.S. investment or bank accounts due to residence outside the U.S. have occasionally caused enough personal stress to bring on emotional problems. We believe that the lack of empathy among members of Congress and U.S. officials is in large part the result of a patently false idea of just who American "expats" are combined with a tendency of "experts" to evaluate issues from an often inaccurate and purely quantitative perspective that ignores or is dismissive of the difficulties that Americans abroad must confront in real-life.

Both our surveys and real-life experience living abroad, often for decades, belie the notion that the American community abroad is comprised of wealthy, tax-dodging, unpatriotic expats living in splendid isolation from the local community as personified in old novels and films. On the contrary, many Americans overseas are persons of very modest means who have difficulty coming up with the funds (exceeding $1,000 at a minimum, according to our survey) to hire the often essential accounting/tax experts to counsel and prepare the several declarations required even for the majority of filers who do not owe tax and maintain “foreign” bank accounts in their country of residence for their daily needs. We believe that the dismissive attitude towards the problems of Americans abroad as evidenced in the testimony of Professor Gamage before the Committee on April 27th results from an unintentional but real discriminatory attitude coined as “placism” by one of our board members, Laura Snyder “Taxing the American Emigrant,” 74(2) Tax Lawyer 299 (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3795480.

Other Americans find themselves living abroad through corporate transfers, opportunities sought in line with our typically American entrepreneurial spirit, or for more personal reasons. The most notable in the latter category include retirement and following one’s spouse. Americans pursuing professional opportunities may be better off financially but not always. Younger Americans in particular, seeking education, adventure, romance, and professionally enriching opportunities overseas, are often of modest means. The same can be said of retirees. Whatever their personal situation, however, Americans considering life abroad or already established overseas must expend considerable time and may need to pay high consulting fees when confronting the extreme complexity inherent in navigating between two legal and regulatory frameworks (that of the U.S. and their country of residence). Too often, commentators offer conclusions that ignore the reality that tax treaties, foreign country FATCA compliance agreements, and the like do not resolve many problems resulting from the inevitability of individuals and small American-owned businesses being “caught in the middle” between the U.S. and their country of residence. The unanticipated, unjust, and devastating effects of the Global Intangible Low-Taxed Income (GILTI) and “transition tax” provisions of the 2017 Tax Cuts and Jobs Act have crippled this particular group.

Americans abroad are loyal, patriotic citizens who do their best to comply with American law within an increasingly complex regulatory framework. They encounter discrimination, for example, in the forced closure of banking and investment accounts abroad and in the U.S. They are denied access to governmental services that are provided to their fellow Americans living in the U.S. (for example, obtaining a “transcript” of their tax filing situation from the IRS or obtaining locally relevant tax counsel after the U.S. government closed IRS offices in a number of embassies).

Our members and the larger community of Americans who contact us increasingly look to Congress for solutions on how best to alleviate unnecessary burdens while preserving the overall objectives of U.S. policy. This does not take into account foreign governments and the European Union, which find themselves under pressure to respond to American unilateralism from dual nationals and citizens who, for various reasons acquired American nationality “accidentally” or unintentionally.

We hope that legislators are concerned about the welfare and interests of Americans abroad, whose estimated number may be as high as nine million, rivaling the population of most U.S. states. We are, however, not convinced that Congress is studying and debating sufficiently the potential negative effects on individual Americans living overseas when it considers new legislation and regulation.

We therefore urge members of Congress, and, in particular, members of this important committee to support the initiative of Representative Maloney, co-chair of the Americans Abroad caucus, to pass HR 2710 which would establish a Commission on Americans Living Abroad.
Thank you for offering us this opportunity to make our views known. We remain
at your disposal.

Paul Atkinson
Chairman, Banking Committee

Fred Einbinder
Vice-President for Advocacy

William Jordan
President

LETTER SUBMITTED BY VANIA K. BAKER

U.S. Senate
Committee on Finance

To Whom It May Concern:

I am a citizen of the United States of America—a supposed citadel of liberty and
justice. However, today, I am writing to call attention to the extreme injustice of
the U.S. extraterritorial tax regime and how it severely limits the freedoms of indi-
vidual U.S. citizens living outside of the United States. This system is profoundly
unfair and it is high time that the extraterritorial tax system be abolished with the
goal of “Creating Opportunity Through a Fairer Tax System”.

For the record, I (like most U.S. emigrants) did not move away from the United
States to avoid U.S. taxation, but rather for mundane pursuits pertaining to work,
study and/or family as life does not necessarily have to happen only within the
United States. In fact, I have discovered that through living outside of the United
States, I am not only subject to (1) taxation in the country where I live, but also
to (2) a more punitive form of taxation than what is imposed upon U.S. residents!
My only crime seems to be that I have chosen to live outside of the United States
and so, perplexingly, my income and assets are now considered foreign to the United
States while they are in actuality local to me.

Moreover, I am writing to express my great concern regarding the failure of the
Senate Finance Committee in considering the impact of this proposed tax legislation
upon U.S. Americans living abroad. We are average, ordinary, and everyday people.
Because we are flesh and blood humans, we need to eat. Because we will get old
and retire, we need to invest in and develop pensions. Because we are individuals
with responsibilities to our families, our communities, and our countries of resi-
dence, we may need to operate our own small businesses. We are definitely NOT
mini multinational corporations and we are tired of being treated as though our nor-
mal day-to-day activities are somehow “offshore” and deserving of punishment. We
ARE tax compliant in our countries of residence. We pay a lot of tax. We pay our
fair share. We do this even though it is almost impossible for U.S. to be both tax
compliant in our country of residence and be compliant with U.S. tax laws. We don’t
understand why U.S. tax laws are being applied in an extraterritorial manner to
income and assets which are not in the United States. Other countries do not tax
their citizens who live in the United States? Why should the United States tax U.S.
citizens living in other countries?

As a fellow U.S. emigrant (who will go unnamed) has previously described:

“Imagine you were born in Canada, but moved to Texas as a young person, obtained
U.S. citizenship and built your family life and career in Texas. You love your life
in Texas, but there is one BIG catch: you have to pay higher Canadian tax rates
on your income, often on top of the taxes you’re already paying in the U.S., for serv-
ces such as Canadian nationalized healthcare which you never personally benefit
from. You can’t take advantage of U.S. tax programs such as 401K plans or edu-
cation deductions because they are not ‘Canadian approved’ programs, so you have
to pay even higher tax to Canada on the income you are supposed to be able to de-
duct. Furthermore, Texas banks have to report all of your financial records to the
Canadian tax authorities and, as a result, very few banks will accept you as a client
so you can’t shop around for a better mortgage or a higher savings interest rate.
On top of all this, jobs in which you would have bank authority or signatory power
don’t want to hire you even if you are the best candidate because all of the organiza-
tion’s financial information would have to be sent to the Canadian financial authori-
ties. Finally, you are effectively barred from investing in any kind of mutual funds
or investment instruments in Texas because they are treated by Canada as ‘offshore’
accounts, overseen by the Canadian Financial Crimes Unit, with onerous reporting requirements and punitive tax rates. All of this because you were born in Canada and so therefore, due to your place of origin, you are treated differently from AND more punitively than other Americans—even those born in other countries who are living in the U.S. Then, imagine that your repeated calls to change the system to something more equitable were systematically ignored by both Canadian and U.S. authorities. Sound unfair? This is the reality I have to contend with every day as a U.S. person residing in Switzerland.”

Our situation is bad. It is unique. Only the African dictatorship of Eritrea follows the lead of the United States by imposing worldwide taxation upon its citizens who live outside of the country.

The Senate Finance Committee’s sheer indifference regarding this situation is incomprehensible. Interestingly, in 2015, the Senate Finance Committee recommended changes to the U.S. extraterritorial tax regimes. There have been no changes for the better, but rather many changes for the worse.

So far, the 2021 Senate Finance Hearings have been astoundingly incompetent. The Committee is so focused on corporations that it does not acknowledge at all the changes such corporate tax will have upon ordinary individuals. It has not been mentioned how this obsession with the taxation of corporations will, instead, produce a greater-reaching impact upon countless individuals rather than on those few corporations the Committee is fixated on.

The hearing on April 27, 2021—about a wealth tax—took the treatment of U.S. citizens abroad to a whole new level. The bottom line is this:

As was described, Elizabeth Warren’s proposed wealth tax will result in (1) taxation of assets earned outside of the U.S. and (2) the taxation of our non-U.S. citizen spouses who we share our lives with.

Question: Would the U.S. be okay with China imposing taxes upon all property situated within the United States owned by Chinese citizens? Would you think it fair to be forced into the tax system of your foreign spouse’s country of birth when you’ve never even step foot in said country?

If any of this comes as a surprise, it is either because adequate time has never been set aside to consider such important ramifications or it is simply being ignored how this translates into the U.S. having an extraterritorial tax regime—a regime imposed upon U.S. Americans abroad. All indications are that Warren’s proposed wealth tax will actually leverage the injustice of U.S. citizenship-based taxation to make the whole world part of its tax base.

There are no other words for what is trying to be done to ordinary U.S. emigrants other than predatory, obscene and unjustifiable. These tax practices must stop. If not, we will all eventually acquire another citizenship AND be forced to take the traumatic act of renouncing the citizenship we were born with. I would like to believe the U.S. is better than this.

LETTER SUBMITTED BY CODY GENTRY BARROW

U.S. Senate
Committee on Finance

Sir/ma’am,

I am an American citizen living in The Netherlands, effective August 2019. I vote in the State of Massachusetts because it is my most recent U.S. residence. I spent most of my career prior to moving abroad in Virginia. I believe my profile is unusual among individual submissions from Americans abroad you may receive, as I will explain below. It is certainly extraordinary for an individual with my security clearance and government service experience to permanently reside abroad as a private citizen and express this level of concern with our nation’s extraterritorial policies.

1 Between 2004 through approximately 2020 I held a Top Secret—Sensitive Compartmented Information (SCI) security clearance with Single Scope Background Investigation adjudicated by the Defense Intelligence Agency (DIA), National Security Agency (NSA), and United States Air Force (USAF), including full-scope and counterintelligence polygraphs adjudicated by NSA. I was additionally responsible for Special Access Program and Special Access Required compartmented programs and indoctrinated into numerous such compartments, some of which were otherwise exclusive to Agency directors and Senior Executive Service personnel.
I ask you and your staff members take my statement seriously as someone who served more than half his adult life to this nation.

As you know, the United States is the only developed nation in the world that taxes its citizens based on citizenship rather than where they reside and work. As a lifelong American patriot who has simply elected to work for a Dutch company and permanently reside abroad in the “second act” of his life, your committee’s inattention to extraterritorial taxation and citizenship-based taxation issues has caused this military and intelligence veteran extreme and unnecessary financial distress. These issues also reflect poorly diplomatically with our Allied partners, including the Kingdom of the Netherlands, struggling with “accidental Americans” and the undue hardships posed upon U.S. citizens abroad due to FATCA and PFIC laws’ unfortunate inadequate accounting for individual citizens pursuing middle-class lives.

For background, I am a former senior grade intelligence officer (GG/GS–14) and military veteran with experience in Afghanistan countering Taliban information operations on behalf of United States Cyber Command, of which I am a plank-holding (founding) member; the National Security Agency; and the Pentagon, where I worked with the Office of the Undersecretary of Defense for Intelligence, the Office of the Secretary of Defense for Policy, and was responsible on behalf of the Defense Intelligence Agency for strategic information operations program policy and special operations programs in direct engagement with the Secretary of Defense and in some cases the President, at the time President Barack Obama. You may also find several of my publications with the government/intelligence/academia think tank, the Intelligence and National Security Alliance (INSA), in the footnotes.2, 3

As you can imagine, this makes it all the more painful and excruciating that U.S. extraterritorial taxation policy has placed me in the highly unusual position of tax advisors suggesting I consider “unthinkable” options, such as citizenship renunciation, simply to pursue an ordinary life with a retirement plan, investment options in standard vehicles like ETFs, and other norms afforded to other American citizens without the extreme duress placed upon citizens abroad because of PFIC, FATCA, and other rules that classify middle-class individuals abroad as second-class citizens. This is not the course I will take. My intention is to remain an American citizen and to work through my elected officials to make our policies fair to Americans. It is always possible I will return to the U.S., my home country, and I should not be in a position of tax advisors suggesting I consider permanent separation simply to experience a normal life while residing abroad.

I assure this honorable committee that no American ever fled to Europe to evade taxes. European tax rates are among the highest in the world, including in wealth and capital gains unprotected from any double taxation exemption treaty, which is yet one more reason why U.S. citizens ought not be taxed both by their adopted nation and their home nation.

Here are some of the issues faced with citizenship-based taxation instead of residency-based taxation:

- Each treatment of U.S. citizens’ abroad bank accounts, pensions, and other ordinary tenets of a healthy financial life are treated as “foreign” by the Internal Revenue Service (IRS), but for us these are local institutions. The United States’ highly irregular and unique citizenship-based taxation system inadequately accommodates American citizens permanently living abroad.
- PFIC regulations similarly classify U.S. citizens’ investments as “foreign,” levying an extreme tax on middle-class Americans simply trying to invest in local equities, either for retirement or in the hope of improving their situation with capital gains investments. We cannot even invest in exchange-traded funds (ETFs), because European-based ETFs are classified as “foreign”—they are local to us—and local institutions will not allow investment in U.S.-based ETFs.
- The 2014 FATCA law, well-intentioned to prevent tax evasion and schemes, is a crushing regulatory burden on ordinary Americans. Foreign institutions are

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2 Please see my 2018 publication, Getting Ahead of Influence Operations, coauthored with the former Director of the National Security Agency and former Deputy Director of the Central Intelligence Agency, here: https://www.insaonline.org/getting-ahead-of-foreign-influence-operations-may-2018/.

3 Please see my other publication, A Framework for Cyber Indications and Warning, co-authored with other industry leaders and former intelligence officials here: https://www.insaonline.org/a-framework-for-cyber-indications-and-warning/.
not willing to conduct business with middle-class U.S. citizens solely because of the burden levied here.

- U.S. tax treaties and policies to help prevent double taxation like FEIE and FTC are ineffective and incomplete. They have capped wage limits too low for professionals working and paid in Euro currencies and in professional fields. While my earned wage income may be higher than median, I am also taxed at a 49% rate by my country in Europe and I am paid at the market rate for a cybersecurity professional—my industry after leaving the government. I am not, nor likely ever will be, “wealthy” or a “fat cat.” I am a working cyber intelligence professional. I am simply taxed twice, unlike any of my colleagues who are citizens of other developed nations—they are taxed based on where they reside and work, not based on their passport.

- Not in my case, but in other cases many American citizens have not been to the U.S., or in some cases have never been to the U.S., in many years. Many do not have any ties to the U.S. They do not have employment in the U.S. Yet the U.S. taxes them based on their passport, leading to a painful stigma against U.S. citizenship and resulting in more “burden” than gift. This is especially painful for me to witness as a former service member.

- This has led to an increasingly negative diplomatic image for the United States through what has become “Accidental Americans,” who contend with citizenship-based taxation’s unintended negative effects regularly.7

While U.S. citizenship brings global protection and diplomatic services and it is a privilege to be a citizen of what is frankly still the greatest country on Earth, these U.S. citizens receive no benefits, use no services, and pay double taxes based on their passport. Citizens of every other developed country—in fact, every country save the African dictatorship of Eritrea—pay taxes based only on where they reside and are employed.

There is simply no excuse for citizenship-based taxation and immense distress wrangling with the IRS each year for citizens that use no services and have no connection to the United States besides their passport.

There is no excuse for classifying home sales, investments, and other aspects of normal financial planning as “foreign” investments and incurring a 40% tax penalty that other American citizens do not endure. For U.S. citizens abroad, these are local investments.

These are local homes where U.S. citizens abroad have purchased homes to raise their families, just as Americans domestically, but we are subject to highly irregular “foreign” tax penalties simply because we hold U.S. citizenship.

These policies like PFIC and FATCA are well-intentioned and typically designed to prevent tax evasion, yet they have a severe effect of harming ordinary citizens while corporations and wealthy individuals find other ways to avoid taxes, such as leveraged borrowing. Neither the IRS nor the U.S. tax code acknowledges how much unnecessary burden these policies place on ordinary Americans who happen to live abroad. Many, perhaps most of these citizens have no affiliation with American employers or corporations in any capacity and are simply trying to live normal lives.

There must be a more fair and equitable solution that would identify how many days a citizen has worked in the United States, or has visited the United States, and incur tax liability only in such circumstances. I am certain all U.S. citizens would be happy to pay taxes when working for American employers, residing in the United States, or using American services, et cetera. As it stands, American citizens abroad are in a unique and the most situation possible among developed nations—hamstrung with retirement, investment, home ownership, and other options—merely based on our passport.

Americans should be proud of our passport, not afraid of how it will harm our futures or our families because of highly irregular tax policies. As well-intentioned as

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5 France’s “accidental Americans” file new suit over bank refusals: https://www.thelocal.fr/20200706/frances-accidental-americans-file-new-suit-over-bank-refusals/.


they may be, it is important to distinguish much more effectively between corporate entities evading taxes and individuals simply trying to live normal lives abroad.

Please feel welcome to reach out to me with further engagement.

Sincerely,

Cody Gentry Barrow

LETTER SUBMITTED BY CLAUDE BEAUREGARD

U.S. Senate
Committee on Finance
To Whom This May Concern:

I am a proud citizen of the United States of America—that great citadel of freedom and justice. But, I am writing today to call attention to the extreme injustice of the U.S. extraterritorial tax regime and how it severely limits the freedom of individual U.S. citizens living outside the United States. This system is very unfair and it’s high time that the extraterritorial tax system be abolished with the goal of “Creating Opportunity Through a Fairer Tax System.”

The only thing that makes me different as an American from U.S. residents is that I live outside the United States. For the record, I did not move from the United States to avoid U.S. taxation. In fact, I have discovered that by living outside the United States I am subject to (1) taxation in the country where I live and (2) a more punitive form of taxation that what is imposed on U.S. residents. My only crime seems to be that I live outside the United States—and therefore my income and assets are foreign to the United States. But, the income and assets are actually local to me.

I am writing to express my great concern about the failure of the Senate Finance Committee to consider the impact of proposed tax legislation on me and on Americans living abroad generally. We are average, ordinary, every day people. Because we are flesh and blood humans, we need to eat. Because we will get old and retire we need to save for retirement. Because we are individuals with responsibilities to our families, our communities and our countries of residence we may need to operate our own small businesses. We are definitely NOT mini multinational corporations and we are tired of being treated as though our normal day-to-day activities are somehow “offshore” and deserving of punishment. We are tax compliant in our countries of residence. We pay a lot of tax. We pay our fair share. We do this even though it is almost impossible for us to be both tax compliant in our country of residence and be compliant with U.S. tax laws. We don’t understand why U.S. tax laws are being applied in an extraterritorial manner to income and assets that are not in the United States. Other countries don’t their citizens who live in the United States? Why should the United States tax U.S. citizens living in other countries? Our situation is bad. It is unique. Only the African dictatorship of Eritrea follows the lead of the United States by imposing worldwide taxation on its citizens who live outside the country.

I really don’t understand the indifference of the Senate Finance Committee to this situation. Interestingly, the Senate Finance Committee in 2015 recommended changes to the U.S. extraterritorial tax regimes. There have been no changes for the better, but many changes for the worse.

So far, the 2021 Senate Finance Hearings have been very, very bad. The Committee is obsessed with corporations without acknowledging that changes to corporate tax will have a huge effect on individuals. You haven’t mentioned that your obsession with the taxation of corporations will have a bigger impact on the many individuals than on the few corporations.

The hearing on April 27, 2021—about a wealth tax—took the treatment of U.S. citizens abroad to a new level. The bottom line is this:

As described Elizabeth Warren’s proposed wealth tax will result in (1) taxation of assets earned outside the USA and (2) the taxation of our non-U.S. citizen spouses who we share our lives with.

And to add insult to injury, Senator Warren’s proposed wealth tax would bring assets acquired by U.S. citizens, after having moved from the United States, into the wealth tax system. Come on! My house was acquired after I moved from the United
States. My local business has nothing to do with the United States. My non-U.S. citizen spouse's assets have nothing to do with United States.

Question: Would the United States like it if China imposed taxes on all property situated in the United States that was owned by Chinese citizens?

If this comes as a surprise to you it's because you either don’t understand or are conveniently ignoring that the U.S. has extraterritorial tax regime—a regime imposed on Americans abroad. All indications are that the Warren wealth will actually leverage the injustice of United States citizenship-based taxation to make the whole world part of its tax base.

Seriously, these predatory, obscene and unjustifiable tax practices must stop. It's simply not fair!!

God Bless the United States of America!

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LETTER SUBMITTED BY JANEEN BUTLER, CPA

As a CPA practicing in tax, I have been following the tax debate for some time now. Sometimes I agree with Democrats and sometimes I agree with Republicans. I recognize that a tax policy that sounds good in theory can often times fall apart when working through the practicality of it. I absorb all the complaints and all the complex discussions, but at the end of it, I cannot help but think—if the bottom 95% were paid more this would solve so many problems. I appreciate the push for a higher minimum, but I believe it needs to go further than that. I often ask myself—is it a policy issue or a cultural issue? If a cultural issue, is there a policy that could nudge the cultural trend needed to strive towards sustainability. The key point is higher wages will help local economies and raise taxes. In order for trickle down to work, it has to actually trickle down. So how do you convince those at the top to start the ripple effect? I really think it can be done through a combination of cultural and policy shifting. Is it a matter of who goes first?

There is a recent working paper from Rand Corporation that studies the declining trends in wages compared to GDP over the last three decades: https://www.rand.org/pubs/working_papers/WRA576-1.html. The bottom 95% is much worse off than in prior decades. Take that, combined with rising costs of healthcare, childcare, education, etc. and it is easy to see why Americans are frustrated. A middle class family should be able to pay their bills without stressing and go on a vacation or two a year without charging it all on the credit card. A strong middle class family allows individuals to move up on Maslow's hierarchy of needs and contribute to their local communities, either with time or money. Those that you would think "should" be middle class based on their jobs are still struggling to pay their bills without stressing or go on those family vacations. I blame the entire economic ecosystem and below is my summary for how to look at it holistically and brainstorming ideas for shifting it.

Let’s look at the ripple effect of higher wages in the U.S. I hear that small companies cannot afford to pay higher wages and I believe them. I also believe that if we start with the big companies, the small companies will be able to pay higher wages. Take the example of a Walmart or some other big company into a neighborhood (I don’t mean to just pick on Walmart). Think about how much money they extract out of that town only to put back in by way of low wages. Now, let’s imagine Walmart starts paying more to every level of employee. People in that town now have more money. What might that achieve?

1. Able to pay for child care.
2. Get out of debt.
3. Able to enroll children in extracurricular activities.
4. Dine out at local restaurants.
5. Explore more—mini and big vacations which stimulates economies.
6. Fix up their homes (supports local contractors).
7. Eat healthier (reduce healthcare costs).
8. Less stress (reduce healthcare costs).
9. Start choosing to shop locally and not just big box stores.
10. Donate to local charities.
11. Pay more in income taxes, sales taxes, and payroll taxes.

While I cannot guarantee how an individual will spend their money, I can say that I have seen a large cultural shift in the desire to support local businesses. Those that can afford it, recognize it costs more to have ethically sourced items from well-
paid labor—they are willing to pay for it. Plus it’s the cool thing to do! Here in my state of Arizona, we have an organization called Local First AZ that does a fantastic job of elevating local businesses and towns to explore. People are not solely driven by price, they will care about how they spend their dollars if they can afford to.

So now that the big companies have started pushing those extra dollars into that town, what happens next? Now some of the smaller companies will inevitably see an increase to their bottom line and will have the money to pay their employees more and I imagine have more to keep for themselves as owners and so the virtuous cycle continues. I acknowledge that a strong cultural message has to be pushed out by local towns to promote shopping local vs. ordering everything on Amazon. I still order plenty on Amazon, but a conscious effort to support local can do wonders for our hometown economies.

So how do you get the first ones to pay more wages? Here is my rough draft brainstorm....

No one likes to pay taxes. I wish that wasn’t the case, but it just is. I would say owners like paying employees more than paying taxes, so let’s make that happen. So what if we raise taxes as planned, but then offer a credit for increasing wages in which the government basically subsidizes the extra wages to get them to a point where they are in the same (or close) position they would be in under current TCJA tax law. I’m not going to go through how the math would work at this time, but I know a formula could be devised to come to that result. This would still have a positive net impact on tax revenues due to the increase income and payroll taxes on the recipients of the increased wages (not to mention increased sales taxes). In logistical terms, I think this is achievable through information already provided by businesses. You could look at the average increase in wages by taking the total wages per the W-3 less officer compensation on form 1125–E (highly compensated officer wages should be subtracted out of the formula) and divide by total employees as reported on W-3 (less the number of officers), then compare year over year.

I know it seems drastic to offer this type of credit, but I believe it will result in the intended result. I worry that raising taxes doesn’t get to the root of the problem. Somehow we have to get every day Americans to be paid more. I try not to be too cynical, but I wish companies would do the right thing and see how it would improve the economy as a whole, but maybe the big companies see how dependent people are on their low prices? I think what most Americans were thinking when they heard “Make America Great Again” was a longing for the days before big companies, where you had cute downtown areas full of local shops and communities were very connected. I think most of us would love that, liberal or conservative. I’m not trying to destroy the big companies; they do provide jobs, economies of scale, and conveniences; but we could all benefit from a better balance. More money in our paychecks would provide us with the power to make those consumer choices and support our own communities to make them better.

LETTER SUBMITTED BY ANNE-MARIE YARBROUGH BUZATU

Dear Committee Members,

Imagine you were born in Canada, but moved to Texas as a young person, obtained U.S. citizenship and built your family life and career in Texas. You love your life in Texas, but there is one BIG catch: you have to pay higher Canadian tax rates on your income, often on top of the taxes you are already paying in the U.S., for services such as Canadian nationalized health care that you never personally benefit from. You can’t take advantage of U.S. tax programs such as 401K plans and education deductions because they are not “Canadian approved” programs, so you have to pay Canada tax on the income you spend on those. Furthermore, Texas banks have to report all of your financial records to the Canadian tax authorities, and as a result very few banks will accept you as a client, so you can’t shop around for a better mortgage or a higher savings interest rate. On top of this, jobs in which you would have bank authority or signatory power don’t want to hire you even if you are the best candidate because all of the organization’s financial information would have to be sent to the Canadian financial authorities. Finally, you are effectively barred from investing in any kind of mutual funds or investment instruments in Texas because they are treated by Canada as “offshore” accounts overseen by the Canadian Financial Crimes Unit, with onerous reporting requirements and punitive tax rates. All of this because you were born in Canada, and because of your place of origin you are treated differently from/more punitively than other Americans—
even those born in other countries who are living in the U.S. Then imagine that your repeated calls to change the system to something more equitable were systematically ignored by both Canadian and U.S. authorities. Sound unfair? This is the reality I have to contend with every day as a “U.S. person” residing in Switzerland.

I am an American citizen, born and raised in Texas, who has resided in Switzerland for more than 15 years, and who has recently obtained Swiss citizenship. Because of my status as a “U.S. person”, I am discriminated against in Switzerland, my place of residence and now nationality, because of the U.S. practice of taxing “U.S. persons” on their worldwide income, and the Foreign Account Tax Compliance Act (FATCA) and the bilateral agreement that the U.S. negotiated with Switzerland in order to enforce FATCA. Furthermore, because I reside outside of the U.S., I am discriminated against as compared to my U.S.-based compatriots and am unable to benefit from a whole host of social benefits, tax deductions and banking services. Here are a few examples:

- **I am effectively banned from opening an investment account in Switzerland**, my place of residence and nationality, because financial institutions do not want to assume the onerous reporting requirements that come with a potential withholding fee of 30%.
- **Nearly all banks in Switzerland will not accept me as a client for regular banking services** for the same reasons, so there is no way for me to compare banking services or take advantage of offers that are not provided by the one bank that will accept me (UBS).
- **Nearly all U.S.-based investment firms and banks will not accept me as a client** because I am not a resident of the U.S.
- **I pay into a retirement fund that is very similar to a 401K program**, and which provides similar tax advantages in Switzerland because I am only taxed on that income when I take it out at retirement; but both my and the employer’s contributions are taxed by the U.S. in the year I earn them meaning I am taxed at a punitive rate.
- **I cannot take deductions for my sons’ university tuition** because they go to are not on the U.S. Department of Education’s Database of Accredited Post Secondary Institutions and Programs (DAPIP) or the Federal Student Loan Program list.
- **I am not able to benefit from a whole host of tax deductions and credits that my U.S-residing compatriots do** because I am not a resident of the U.S.
- **Many IRS services are only available to U.S. residents**, meaning that they are not available to me as a U.S. person residing abroad.
- **Being a “U.S. person” has impacted me professionally** because any Swiss institution I work and have bank signatory rights for would have to have their finances reported to the IRS. I have only worked for non-profit NGOs in Switzerland.
- **In many cases Swiss taxes are assessed in a manner that is fundamentally incompatible with the U.S. income tax approach**, meaning that in some cases I am double-taxed by both systems; the current U.S.-Swiss tax treaty does not effectively address these inconsistencies (see more below).

U.S. taxation on my and my husband’s income is disastrous for us, for numerous reasons which are laid out in detail in the below submission. However, before wading into the weeds, I wanted to put up front my recommendations for how to overhaul international taxation so that it is fairer and reduces discrimination against folks like myself:

1. **Change the system of citizen-based taxation of individuals to that of individual taxation on only income earned from U.S. sources, and not worldwide taxation, also known as resident-based taxation for individuals**, the kind of income taxation that most of the rest of the world practices (for a relatively simple and fast interim fix to this issue by the U.S. Treasury while waiting on lengthier legislative processes, please read this article);
2. **Create a special committee that looks at the impacts of U.S. taxation on its nationals residing abroad** so that any changes made to the tax code are reviewed by this body to ensure that our situations are taken into consideration, including analyses of how they are (in)compatible with the tax sys-
tems of the other 190+ countries in which U.S. persons live in order to protect against unintended negative consequences; and finally.

(3) To include formal representation of Americans living abroad in our representative bodies, as the approximately 9 million of us living abroad need a voice. Switzerland and France include seats for their citizens residing abroad in their Parliaments, and the U.S. can and should do the same.

To understand why I am making these recommendations, please read the more personal account below.

I was born and raised in Texas, where I lived most of my life until I and my family moved to Switzerland more than 15 years ago. We didn't feel we had much choice. In August 2005, my husband was laid off from his job in the high-tech sector. We had two young boys aged 4 and 7, and I was working as a part-time consultant and a more than full-time mom. Once my husband lost his job, we suddenly were faced with extremely high health insurance costs (COBRA), significant student loan debts and a high monthly rent with no income. My husband applied for several jobs and had a few interviews, but the one he got was working in IT for the International Computing Center, a UN-affiliated computer services organization, located in Geneva, Switzerland.

In Switzerland, I went back to school studying the impact of war and on international security and human rights. I subsequently managed to carve out a really fulfilling career working for Swiss-based NGOs where I strive to limit the negative impacts of businesses on human rights, as well as work with the private sector to foster positive change, both on the ground as well as in the halls of international policy.

I love the U.S. and have close ties with family members and several good friends who live there. Both of my elderly parents are alive, but have been experiencing some serious health issues of late. Before the pandemic, I typically would visit them at least once a year, and it has been tough waiting on the sidelines, hoping that I will be able to see them again before too long. It is important to me that I am able to visit them, and to be able to spend more time with them should they need extra care and support, and more generally I love getting back to the U.S. There are definitely things that I miss, like really good Tex-Mex (!) in an affordable restaurant, infinite sunsets over a West Texas sky, and easy, laid-back conversations with good friends and family.

What I do not love is the U.S. taxation of people like me who live, work and pay taxes in a completely different tax system, which in many areas is completely incompatible with the U.S. tax system. As a matter of fact, you could say that the U.S. has three different distinct income tax regimes which creates different, unequal classes of taxation: 1. Residence—For U.S. residents, 2. U.S. Source—For non-resident aliens, 3. Extraterritorial—For Americans Abroad. This last regime to which I and my family are subject means that we don't get the same kinds of deductions and tax credits as our homeland-based compatriots. For example: I participate in an employer-contribution retirement program which is very similar to U.S. 401K programs: the employer matches my contributions, and I do not have to declare the employer nor my contributions on my Swiss taxes as they are paid, only when I take them out after retirement when I am likely earning much less. However, the U.S. taxes me on the employer contributions as well as my own contributions to the tax plan in the year that they are paid, so I am taxed by the U.S. on money I haven’t even received, and likely at a higher tax rate than I would be at during retirement. Another example: my son is going to a university located in Berlin, Germany, however the school is not on the list of U.S. recognized educational institutions, so we are unable to deduct his tuition from our taxes.

Furthermore, Swiss income taxes are structured completely differently from those of the U.S., and they are in most cases lower than the U.S. income tax rates. However, the cost of living in Switzerland is one of the highest in the world and is considerably higher than we were paying in Texas. People who visit from the U.S. are shocked at the prices in the stores and restaurants here, and renting/buying homes is extremely expensive. However, because of the relatively high salaries (in Geneva we have an approximately $25/hour min wage) and low taxes, these prices are generally affordable to people who work here. Less so for us: as “U.S. persons”, because we are unable to take many of the same deductions as our homeland compatriots, we essentially have to pay higher U.S. taxes than Americans living in the U.S., higher taxes than others who live and work in Switzerland and pay the higher Swiss prices. And to be very clear, we are not earning very high salaries, but rather are at that sour spot of earning just a little more than the Foreign Earned Income
Exemption (FEIE) once things like our employer contributions to pensions and other benefits—much of which we don’t get in pocket—are taken into account. As such, we pay U.S. taxes at a pretty high rate on income that doesn’t make it into our bank account and given the high cost of living we have here, this means we are penalized financially relative to our colleagues who are working similar jobs.

Moreover, as U.S. persons residing abroad, we are not able to take advantage of many of the tax credits that are available to those living in the U.S. For example, in March 2018 we bought a Tesla Model 3 (the more affordable Tesla) and were under the impression that we would be able to get the $7,500 tax credit to help us offset the still significant cost. However, when we did our U.S. taxes, we learned that this tax credit was only available to those actually living in the U.S., not those living abroad. In a way I understand the rationale: our Tesla would not be directly benefitting those living in the U.S. (although it is contributing to an overall globally cleaner environment), and therefore we should get no incentive from the U.S. to buy it. However, on the same topic, we should not be paying taxes in the U.S. on income that we do not earn from there, to pay for an infrastructure and a Congress that does not directly benefit or represent us.

Coming back to the incompatibility between Swiss and U.S. income tax systems, this is not just limited to the fact that similar Swiss retirement and education tax programs are not recognized by the U.S., but also to completely different approaches in the manner of calculating income tax. For example, in Geneva the way that taxes are assessed in relationship to our townhouse is that the income tax authorities tax us on the fictional “income” we would have earned if we had been renting the house out (which we are not). The way they calculate this is very complicated and not fully known to me, but it has something to do with the type of property, when the property was built, where it is located, and the amount of income that we earn from our work (this last element helps to ensure that we will not be priced out of our home by property taxes even as property values rise). Furthermore, it is something we find out long after the fact of filing taxes. For example, for tax year 2020, we will file our Swiss tax returns in June of 2021 and we will get the calculation of this “income tax on our property” somewhere in October–November 2021, long after our U.S. tax returns are due and interest is being assessed on any unpaid amounts. Furthermore, its incompatibility with how U.S. assesses income and property taxes makes it really difficult to know how to include that in our tax returns. We tried to do it for a couple of years, but this did not seem to be accepted by the IRS, and then we had to pay additional taxes with penalties and interest. Now we do not even try to include these taxes we pay on our U.S. tax return, and so we are being double-taxed by both Swiss and U.S. jurisdictions on that income.

When it comes to trying to get information, help and guidance from the IRS so that we can navigate these difficulties more easily, this is also not set up for those of us living abroad. Most of the time when I call the IRS, I get a message that the line is too busy and they are not accepting calls at that time. Sometimes I have gotten a message saying that the estimated wait is between a certain time, such as 7 to 10 minutes, and then finally hung up after being on hold for more than 30 minutes. Needless to say, there are no toll-free numbers for U.S. persons abroad, so of course we have to pay international long-distance rates. However, even many of the IRS online services are not available to those of us living outside of the U.S. (see below for an example).

Another problem is that as “U.S. persons”, nearly ALL banks will simply not open an account for us, which has huge implications on, for example, shopping for affordable mortgages from local/cantonal banks.

Further, we are effectively banned from investing in any kind of stocks, bonds or mutual funds in our country of residence and nationality. We are getting older, and we wanted to try to invest in a mutual fund here to put aside a little extra money for our golden years. However, the only bank we found in Switzerland that would accept us as customers had a 250,000 Swiss Francs (about $270,000) minimum investment requirement—something that is definitely out of our league! Furthermore, we learned that even if we could and did invest in a mutual fund here in the country where we live (and now are also citizens of), that it would be treated by the U.S. as a “Passive Foreign Investment Company” and would be taxed at an exorbitant rate.

Discrimination against me as a “U.S. person” has also impacted me professionally. After I was hired as the COO for a very small, non-profit Swiss NGO we learned that if I were given signatory rights on our organizational bank accounts, the financial records of this Swiss organization would have to be sent to the IRS. There-
Therefore, I do not have these rights, and I can’t perform all of the functions of my role. This puts me at a disadvantage employment-wise relative to all of the qualified candidates who do not have U.S. citizenship.

Furthermore, filing and paying taxes in the U.S. is extremely complicated, and calculations/corrections made by the IRS are not transparent. We have consistently filed and tried to pay our taxes in accordance with the rules as we understand them, although the tax code is not exactly straight-forward especially for people like us living outside the U.S. Sometimes we get bills years later without any explanation as to why or how new calculations were made. For example, we recently got a bill from the IRS for nearly $8,000(!) This is a lot of money for us. I wrote the IRS and asked for an explanation of how they calculated this amount more than six years after the fact and got no response except for a threatening letter that they are going to levy taxes on our assets. I tried to go online to get a transcript of how they calculated this tax, however the online service is not available to persons who live abroad! There is a phone-in/write-in service to obtain tax transcripts, but it only goes back to the previous three years’ returns. I tried to call anyway and was not able to get through.

I am not against paying taxes, and fully recognize the necessity of them. If I were to earn any money from U.S. sources, it would make sense that I pay U.S. tax rates under the U.S. tax system, but not that I pay Swiss taxes on top of them. If every country taxed because of nationality (or even former permanent residence status) with no regard to the other nationalities and their accompanying tax systems, the impacts would be devastating: many persons here in Geneva have 3, 4 or even more nationalities, and having to satisfy the requirements of multiple different, incompat-ible national income tax systems on income earned in one country would not be sustainable, nor would it be fair. In this respect the U.S. is the only country (outside of Eritrea) that taxes on the basis of nationality/permanent residence, but this also highlights how incongruent and out of step this practice is with the rest of the world, and for its citizens/permanent residents who happen to reside in other countries. Every time Congress makes a change to the tax code, this directly impacts me and those of us living outside of the U.S. who are also subject to other tax code regulations. However, these impacts are rarely if ever discussed by members of Congress, and certainly not studied in depth as to how they will impact/interact with the other 190+ countries’ income tax regimes where U.S. persons may be living. This results in devastating unintended consequences on ordinary folks: if I were rich, or a multinational, I would have the resources to figure out how to get around the different tax systems, but I am not.

Finally, I cannot express the anger and frustration I feel when I read that Amazon and 54 other major U.S. corporations, as recently reported in *The New York Times,* paid ZERO income taxes on incredible, record-setting profits in the many billions. How is it that we, a middle-class family who hasn’t even lived or earned any income in the U.S. for more than 15 years, are effectively paying more income taxes than Amazon?

Therefore, we ask you to:

1. Change the system of citizen-based taxation of individuals to that of individual taxation on only income earned from U.S. sources, and not worldwide taxation, also known as resident-based taxation for individuals, the kind of income taxation that most of the rest of the world practices (for a relatively simple and fast interim fix to this issue by the U.S. Treasury while waiting on lengthier legislative processes, please read this article);

2. Create a special committee that looks at the impacts of U.S. taxation on its nationals residing abroad so that any changes made to the tax code are reviewed by this body to ensure that our situations are taken into consideration in such regulation and to protect against unintended consequences; and

3. To include formal representation of Americans living abroad in our representative bodies, as the approximately 9 million of us living abroad need a voice. Switzerland and France include seats for their citizens residing abroad in their Parliaments, and the U.S. can and should do the same.

We should not be penalized and discriminated against just because we were born in, had American parents or lived a significant time in the U.S., and reside in an-

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other country. Furthermore, we can be an important resource to the U.S.—we can play the role of “local ambassador” in our countries of residence, helping to bridge differences and forge understandings between the U.S. and the countries we call home, which is increasingly important in our highly interconnected, shrinking world.

As a last note, it is more than somewhat ironic that the U.S. ostensibly got its start over a tax dispute with its overseas colonial parent, with American revolutionaries crying out the slogan “no taxation without representation,” launching a war that brought about the birth of our nation, and yet it taxes folks like me who earn their income completely outside the U.S. system and have no effective representation on the U.S.-created impacts we face living abroad. That notion of justice, of democratic representation and fair taxation is fundamental to the very identity of the United States, and yet somehow it is the only developed country that burdens individuals such as myself with a tax imposition that does not take into account the situations in which we are living, and which prevents us from fully participating in the societies of which we are part.

Many have said that you, our representatives, don’t care for U.S. persons residing abroad, that we don’t matter enough in terms of votes or funding, that our situations don’t play well on media platforms in terms of messaging, that we don’t have enough pull or importance to get any attention. However, I am still hoping that you can care about something that is wrong and unfair, even if it isn’t politically expeditious. In fact, it is my American-bred idealism and pragmatic, can-do spirit that make me believe that we can work together to develop an income tax system that is fair and not unduly burdensome, and that honors those fundamental American values which we all hold dear.

I thank you for your time and attention, and hope that this submission will be fully considered by the Committee. I would be happy to provide any additional information or support to help you better understand the implications of the U.S. income tax system on folks like me who live in other countries.

Sincerely,
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Statement of Michael G. Bindner

Chairman Warren and Ranking Member Cassidy, thank you for the opportunity to submit these comments for the record to the Committee on this topic. I am guessing that wealth taxes will be on the agenda. I will start there and then offer an alternative tax reform proposal, which includes methods to invest in human capital and include state governments in reform.

The Nature of Wealth

Money is not only a medium to exchange goods. It is also a decision tool to exchange power. Power is the ability to demand resources and labor. Capitalism seeks to consolidate this power into the hands of the owners of capital. Socialism seeks to distribute this power to society, using common action to do so. State capitalism and state socialism are the same thing, with modern mixed economies consisting of private capitalism and social democracy.

Karl Marx understood the economics of production. When he wrote, finance was a game, not a science. He had no idea that the Boom-Bust Cycle exists because of the interaction of tax and finance. Modern Marxists are still obsessed with rewarding production rather than considering the entire enterprise. Enabling workers are as essential as production, from distribution to design to marketing. Worse, they are not really up to speed on how the economics of the CEO and tax policy are interrelated or how to go from democratic socialism to the real thing.

Social Democrats have no clue either. Indeed, most Democratic Socialists, like Bernie Sanders, have mostly Social Democratic tools in their kit. Free college and Medicare for All are not really socialism, they are simply better birdseed. Elizabeth Warren at least admits that she is still a capitalist. So do the Social Democrats of Scan-
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dinavia and Western Europe. Their proposals have no clue on how to get from Social Democracy to Democratic Socialism—or to the real thing.

The essential fact in any system that uses money is that money buys work from people. Since work is a function of time, as our lives, money essentially buys people. Another way to look at money and savings is through class analysis. Savings is the power to make others work without working yourself. When realized, savings purchase essentials and luxuries. Even poor people deserve some level of luxury.

In an unbalanced economy, the working class do not even receive the essentials. Scarcity in essential goods is the incentive used to compel work. Inadequate income is used to compel work on a consistent basis. The argument against guaranteed income is that if work can be compelled, hyperinflation and shortages result.

The Nature of Income

Income is the return on assets, including sold labor. This includes the return on taxation of assets. The challenge for public policy is providing for adequate income and assets for all households so that no worker can be considered someone else’s property. How badly we have failed at this is impossible to see until we look clearly at the elements of the “supply side.”

Absolute Income is adjusted gross income plus unrealized income. Wealth taxes are an attempt to go after part two, in its stored form, on an annual basis. They will never pass because, if done correctly, the wealth will be destroyed. For some, that is likely the goal. If it is done ineffectively (by self-reporting or creating loopholes) it legitimizes assets which have no inherent value.

In the macro-economy, absolute income is gross national product plus stored future income plus speculative income. Current economic discourse and statistics do not, and likely cannot, capture the difference between the last two, although looking at income class helps.

This inability to separate future spending from speculation does not mean we cannot quantify unrealized income. Doing so shows why taxing wealth and unrealized income are close to impossible. Here is a hint: it does not really exist. Once that secret is out, capitalism’s days are numbered.

Unrealized income =

the net unrealized gain on traded equity and securitized assets held for less than a year
+ the unrealized net gain on assets held for more than a year
+ additions to retained earnings for the year that are attributable to shareholders or partners if it were to be distributed
+ increased value in a year of physical assets less their distribution expense.

All of the above include increased asset values and undistributed earnings for assets held offshore.

Asset prices and retained income and asset book values can be valued and are related but are not mutually exclusive. Asset prices may or may not reflect retained earnings and physical or market value of real assets and may, in fact, be junk assets based on fraud. Bonds have the same features and are valuable based on currently expected future income—including whether tax income attributable from holding these bonds can ever be collected.

All value is market-based. These values may or may not relate to the productive power of the underlying physical and human assets. Mass resignations and innovations may turn today’s intellectual property into dust. This is why capitalism is a less than perfect driver of real innovation. Income inequality and hierarchical control are designed to protect against sudden devaluations in both private and state capitalism. Individual and cooperative socialist organizations (from communes to partnerships) always threaten intellectual property held by capitalists.

Taxing Wealth

Anything that can be valued can be taxed. Indeed, it may even be easier to tax than capital gains, which largely rely on self reporting. Either total wealth and growth in wealth can be taxed in the micro level. Unrealized income can be estimated by the entities owned as of December 31st of each year. Any overlap between stock price and retained earnings can be taken into account. Indeed, reporting this would be beneficial to investors. This is the easy part.
The hard part is generating the liquidity to pay the tax. Actually, this is not hard at all. It merely requires the entity owned to write a check. You could not tax corporate income and the investor’s share of it twice. If wealth were to be taxed, it is easier to tax the total value of the entity rather than taxing its owners. It is much less work.

Who really shoulders the burden is a more serious concern. Because of the monopsonist nature of most employment and the monopolist nature of most goods, the wealthy will not pay it.

First, stock prices will go down to reduce burden.
Second, wages will go down.
Third, consumer prices will go up.

Firms have people who run the numbers and a duty to maximize shareholder value. Indeed, internal rents will increase because the labor to make such calculations will be taken from the labor surplus generated from extraction, production, distribution and enabling work.

**Debt Ownership and Tax Reform**

Getting the wealthy and upper-middle classes on board is essential to reform. The way to do this is to make clear who owes and owns the debt. Space limits prevent a thorough discussion of this, but I have attached a summary from my forthcoming book, *Debt as Class Warfare* in an attachment. When it is complete, I will send copies to the whole Committee and will be available to discuss it in detail.

An Asset Value-Added Tax, which is described below, captures a fifth of each trade or return from capital when bought or paid. It is a much more efficient way to extract the money. These include marking the base to market at option exercise and the first sale after inheritance, gift or donation and zero rates sales to qualified Employee Stock Ownership Plans. There is a huge volume of literature on how employee-ownership expands opportunity, including a fair bit of it by me. We can discuss this as well at a later time.

Please see a second attachment detailing the Center’s Tax Reform proposals. These also include a proposal to create tax prepayment bonds to shift wealth from speculation and market debt to federal debt retirement.

The nation has already taken steps on the journey to reform in passing the American Rescue Plan Act.

The ARPA has its pluses and its minuses. On the minus side, families who had adequate income during the pandemic now have money to blow. Instead of spending it they are using it to speculate. Masses of people are about to enter the bottom half of EFT and Crypto markets, which will allow the top tiers of the scheme (whose seed money was provided by the Ryan-Brady-Trump tax cuts) to get out.

On the plus side, the increased child tax credit and its new refundability will provide long term economic security families. The second essential step is to increase the minimum wage so that no one has to work for free or have a decreased standard of living without working by living solely on the CTC.

The minimum wage should be immediately increased to match the Republican offer of $10 per hour. To return wages to 1965 levels, which rewarded productivity gains, the wage should be increased over time to $12 per hour and adjusted for inflation automatically every year, starting now. The current challenge in implementing a higher CTC is how to get the money to families immediately. Doing so through direct IRS payments cannot be a long term solution.

There are two avenues to distribute money to families. The first is to add CTC benefits to unemployment, retirement, educational (TANF and college) and disability benefits. The CTC should be high enough to replace survivor’s benefits for children.

The second is to distribute them with pay through employers. This can be done with long term tax reform, but in the interim can be accomplished by having employers start increasing wages immediately to distribute the credit to workers and their families, allowing them to subtract these payments from their quarterly corporate or income tax bills.

Over the long haul, tax reform is necessary to cement these gains. Please see our tax reform plan in the third attachment. It is designed to provide adequate income and services to families (both with increased minimum wages and child tax credits) through employer-paid taxes, funding government services through a goods and
services tax, separating out taxation of capital gains and income from income to an asset value added tax and higher tier subtraction VAT collections on wage income up to the $330,000 level and above, with additional personal income taxation for incomes over $425,000.

The top rates for higher tier subtraction VAT, personal income taxes and asset VAT would all be set to the same rate, say 26%, so that forms of income are not manipulated to avoid taxation. It would also effectively raise taxes on salaried income to 52%, with capital incomes reinvested or investments funded by salary income adding an additional 26% of taxation. Spending money will also trigger taxation.

Adding the effect of lower tier subtraction VAT collection to taxation on business owners and the top marginal rate approaches 90%. Such taxes are meant to prevent payment of extreme salaries rather than maximizing revenue. This provides more wages to the rest of the population, especially to those who are not adequately compensated at lower income levels.

Reform allows a rebalancing of fiscal responsibilities. The federal child tax credit we propose, plus increases in the minimum wage to at least $12/hour may provide enough family income in most states. Other states would add additional support through a state subtraction VAT. Comprehensive reform will truly end welfare as we know it by giving families what they need for a decent living.

Human Capital Funding and State Government Participation
The state S–VAT would fund education, with options for funding private schools either as donors or clients. Espinoza v. Montana has settled the question of whether this is constitutional. Now the question is the political will to enact such tuition support and for private schools to allow teachers to organize.

It would also fund remedial education, english as a second language (regardless of immigration status), junior college and technical education and pay for all students who have completed sophomore year in high school or, after their cohort has reached that level.

Retail sales taxes, corporate income and most personal income tax filing would be replaced with the S–VAT and a border adjustable goods and services credit-invoice tax (which we call I–VAT for short). The state-level I–VAT would fund public safety and commercial regulation. Property taxes, without the burden of funding education, would fund both building inspections and local public works, with the latter supplemented by tolls, motor fuel and/or carbon value added taxes (also receipt visible).

States would collect federal S–VAT and I–VAT, review compliance audits and investigate and prosecute criminal violations.

An asset VAT at the state level would collect taxes on rental income (as would the federal AVAT), with states collecting an additional AVAT on real property transfers with price appreciation. This levy would be collected at closing and forwarded to states. Other AVAT collections would be collected by brokers and submitted to the U.S. Securities and Exchange Commission.

Any state AVAT collected on financial transactions would be forwarded to the states by the SEC. I would not recommend state enactment of such levies should an international or OECD AVAT rate be negotiated. This type of competition leads to a race to the bottom.

Any state-level debt service and retirement would be satisfied by higher salary surtax. State constitutional amendments to implement these changes would also include permission to incur debt in a federally declared disaster. This debt would be satisfied by any federal disaster assistance and the salary surtax.

Thank you for the opportunity to address the committee. We are, of course, available for direct testimony or to answer questions by members and staff.

Attachment—Debt as Class Warfare, September 24, 2020
Visibility into how the national debt, held by both the public and the government at the household level, sheds light on why Social Security, rather than payments for interest on the public debt, are a concern of so many sponsored advocacy institutions across the political spectrum.

Direct household attribution exists through direct bond holdings, income provided by Social Security payments and secondary financial instruments backed with debt assets. Using the Federal Reserve Consumer Finance Survey and federal worker and Social Security payment and tax information, we have calculated who owes and
who owns the national debt by income quintile. Federal Reserve and Bank holdings are attributed based on household checking and savings account sizes.

Responsibility to repay the debt is attributed based on personal income tax collection. Payroll taxes create an asset for the payer, so they are not included in the calculation of who owes the debt. Calculations based on debt held when our study on the debt was published, distributed based on the latest data (2017) from the IRS Data Book show a ratio of $16.5 of debt for every dollar of income tax paid.

This table shows a summary level distribution of income, national debt and debt assets in three groupings based on share of Adjusted Gross Income received, rather than by number of households. This answers the perennial question of who is in the middle class.

The bottom 75% of taxpaying units hold few, if any, public debt assets in the form of Treasury Bonds or Securities or in accounts holding such assets. Their main national debt assets are held on their behalf by the Government. They are owed more debt than they owe through taxes.

The next highest 20% (the middle class), hold few bonds, a third of bond-backed financial assets and a quarter of government held retirement assets.

The top 5% (roughly 8.5% of households) own the vast majority of non-government retirement holdings and collect (and roll-over) most net interest payments. This stratum owns very little of retirement assets held by the government, hence their interest in controlling these costs. Their excess liability over assets is mostly attributable to internationally held debt. Roughly $4 trillion of this debt is held by institutions, with the rest held by individual bond holds, including debt held by members of this stratum in off-shore accounts.

Source: Settling (and Squaring) Accounts: Who Really Owes the National Debt? Who Owns It; available from Amazon at https://www.amazon.com/dp/B08FRQFF8S.

Attachment—Tax Reform, Center for Fiscal Equity, March 5, 2021

Individual payroll taxes. These are optional taxes for Old-Age and Survivors Insurance after age 60 for widows or 62 for retirees. We say optional because the collection of these taxes occurs if an income sensitive retirement income is deemed necessary for program acceptance. Higher incomes for most seniors would result if an employer contribution funded by the Subtraction VAT described below were credited on an equal dollar basis to all workers. If employee taxes are retained, the ceiling should be lowered to $85,000 to reduce benefits paid to wealthier individuals and a $16,000 floor should be established so that Earned Income Tax Credits are no longer needed. Subsidies for single workers should be abandoned in favor of radically higher minimum wages.

Wage Surtaxes. Individual income taxes on salaries, which exclude business taxes, above an individual standard deduction of $85,000 per year, will range from 6.5% to 26%. This tax will fund net interest on the debt (which will no longer be rolled over into new borrowing), redemption of the Social Security Trust Fund, strategic, sea and non-continental U.S. military deployments, veterans’ health benefits as the result of battlefield injuries, including mental health and addiction and eventual debt reduction. Transferring OASDI employer funding from existing payroll taxes would increase the rate but would allow it to decline over time. So would peace.

Asset Value-Added Tax (A-VAT). A replacement for capital gains taxes, dividend taxes, and the estate tax. It will apply to asset sales, dividend distributions, exercised options, rental income, inherited and gifted assets and the profits from short sales. Tax payments for option exercises and inherited assets will be reset, with prior tax payments for that asset eliminated so that the seller gets no benefit from them. In this perspective, it is the owner’s increase in value that is taxed.
As with any sale of liquid or real assets, sales to a qualified broad-based Employee Stock Ownership Plan will be tax free. These taxes will fund the same spending items as income or S–VAT surtaxes. This tax will end Tax Gap issues owed by high income individuals. A 26% rate is between the GOP 24% rate (including ACA–SM and Pease surtaxes) and the Democratic 28% rate. It’s time to quit playing football with tax rates to attract side bets.

Subtraction Value-Added Tax (S–VAT). These are employer paid Net Business Receipts Taxes. S–VAT is a vehicle for tax benefits, including

- Health insurance or direct care, including veterans’ health care for non-battlefield injuries and long term care.
- Employer paid educational costs in lieu of taxes are provided as either employee-directed contributions to the public or private unionized school of their choice or direct tuition payments for employee children or for workers (including ESL and remedial skills). Wages will be paid to students to meet opportunity costs.
- Most importantly, a refundable child tax credit at median income levels (with inflation adjustments) distributed with pay.

Subsistence level benefits force the poor into servile labor. Wages and benefits must be high enough to provide justice and human dignity. This allows the ending of state administered subsidy programs and discourages abortions, and as such enactment must be scored as a must pass in voting rankings by pro-life organizations (and feminist organizations as well). To assure child subsidies are distributed, S–VAT will not be border adjustable.

The S–VAT is also used for personal accounts in Social Security, provided that these accounts are insured through an insurance fund for all such accounts, that accounts go toward employee-ownership rather than for a subsidy for the investment industry. Both employers and employees must consent to a shift to these accounts, which will occur if corporate democracy in existing ESOPs is given a thorough test. So far it has failed. S–VAT funded retirement accounts will be equal-dollar credited for every worker. They also have the advantage of drawing on both payroll and profit, making it less regressive.

A multi-tier S–VAT could replace income surtaxes in the same range. Some will use corporations to avoid these taxes, but that corporation would then pay all invoice and subtraction VAT payments (which would distribute tax benefits). Distributions from such corporations will be considered salary, not dividends.

Invoice Value-Added Tax (I–VAT). Border adjustable taxes will appear on purchase invoices. The rate varies according to what is being financed. If Medicare for All does not contain offsets for employers who fund their own medical personnel or for personal retirement accounts, both of which would otherwise be funded by an S–VAT, then they would be funded by the I–VAT to take advantage of border adjustability. I–VAT also forces everyone, from the working poor to the beneficiaries of inherited wealth, to pay taxes and share in the cost of government. Enactment of both the A–VAT and I–VAT ends the need for capital gains and inheritance taxes (apart from any initial payout). This tax would take care of the low-income Tax Gap.

I–VAT will fund domestic discretionary spending, equal dollar employer OASI contributions, and non-nuclear, non-deployed military spending, possibly on a regional basis. Regional I–VAT would both require a constitutional amendment to change the requirement that all excises be national and to discourage unnecessary spending, especially when allocated for electoral reasons rather than program needs. The latter could also be funded by the asset VAT (decreasing the rate by from 19.5% to 13%).

As part of enactment, gross wages will be reduced to take into account the shift to S–VAT and I–VAT, however net income will be increased by the same percentage as the I–VAT. Adoption of S–VAT and I–VAT will replace pass-through and proprietary business and corporate income taxes.

Carbon Value-Added Tax (C–VAT). A Carbon tax with receipt visibility, which allows comparison shopping based on carbon content, even if it means a more expensive item with lower carbon is purchased. C–VAT would also replace fuel taxes. It will fund transportation costs, including mass transit, and research into alternative fuels (including fusion). This tax would not be border adjustable.

Summary

This plan can be summarized as a list of specific actions:
1. Increase the standard deduction to workers making salaried income of $425,001 and over, shifting business filing to a separate tax on employers and eliminating all credits and deductions—starting at 6.5%, going up to 26%, in $85,000 brackets.

2. Shift special rate taxes on capital income and gains from the income tax to an asset VAT. Expand the exclusion for sales to an ESOP to cooperatives and include sales of common and preferred stock. Mark option exercise and the first sale after inheritance, gift or donation to market.

3. End personal filing for incomes under $425,000.

4. Employers distribute the child tax credit with wages as an offset to their quarterly tax filing (ending annual filings).

5. Employers collect and pay lower tier income taxes, starting at $85,000 at 6.5%, with an increase to 13% for all salary payments over $170,000 going up 6.5% for every $85,000—up to $340,000.

6. Shift payment of HI, DI, SM (ACA) payroll taxes employee taxes to employers, remove caps on employer payroll taxes and credit them to workers on an equal dollar basis.

7. Employer paid taxes could as easily be called a subtraction VAT, abolishing corporate income taxes. These should not be zero rated at the border.

8. Expand current state/federal intergovernmental subtraction VAT to a full GST with limited exclusions (food would be taxed) and add a federal portion, which would also be collected by the states. Make these taxes zero rated at the border. Rate should be 19.5% and replace employer OASI contributions. Credit workers on an equal dollar basis.

9. Change employee OASI of 6.5% from $18,000 to $85,000 income.

LETTER SUBMITTED BY JAK DAC

U.S. Senate
Committee on Finance
To Whom This May Concern:

I am a proud citizen of the United States of America—that great citadel of freedom and justice. But, I am writing today to call attention to the extreme injustice of the U.S. extraterritorial tax regime and how it severely limits the freedom of individual U.S. citizens living outside the United States. This system is very unfair and it’s high time that the extraterritorial tax system be abolished with the goal of "Creating Opportunity Through a Fairer Tax System."

The only thing that makes me different as an American from U.S. residents is that I live outside the United States. For the record, I did not move from the United States to avoid U.S. taxation. In fact, I have discovered that by living outside the United States I am subject to (1) taxation in the country where I live and (2) a more punitive form of taxation that what is imposed on U.S. residents. My only crime seems to be that I live outside the United States—and therefore my income and assets are foreign to the United States. But, the income and assets are actually local to me.

I am writing to express my great concern about the failure of the Senate Finance Committee to consider the impact of proposed tax legislation on me and on Americans living abroad generally. We are average, ordinary, every day people. Because we are flesh and blood humans, we need to eat. Because we will get old and retire we need to save for retirement. Because we are individuals with responsibilities to our families, our communities and our countries of residence we may need to operate our own small businesses. We are definitely NOT mini multinational corporations and we are tired of being treated as though our normal day-to-day activities are somehow "offshore" and deserving of punishment. We are tax compliant in our countries of residence. We pay a lot of tax. We pay our fair share. We do this even though it is almost impossible for us to be both tax compliant in our country of residence and be compliant with U.S. tax laws. We don't understand why U.S. tax laws are being applied in an extraterritorial manner to income and assets that are not in the United States. Other countries don't tax their citizens who live in the United States. Why should the United States tax U.S. citizens living in other countries?
Our situation is bad. It is unique. Only the African dictatorship of Eritrea follows the lead of the United States by imposing worldwide taxation on its citizens who live outside the country.

I really don’t understand the indifference of the Senate Finance Committee to this situation. Interestingly, the Senate Finance Committee in 2015 recommended changes to the U.S. extraterritorial tax regimes. There have been no changes for the better, but many changes for the worse.

So far, the 2021 Senate Finance Hearings have been very, very bad. The Committee is obsessed with corporations without acknowledging that changes to corporate tax will have a huge effect on individuals. You haven’t mentioned that your obsession with the taxation of corporations will have a bigger impact on the many individuals than on the few corporations.

The hearing on April 27, 2021—about a wealth tax—took the treatment of U.S. citizens abroad to a new level. The bottom line is this:

As described Elizabeth Warren’s proposed wealth tax will result in (1) taxation of assets earned outside the A and (2) the taxation of our non-U.S. citizen spouses who we share our lives with.

And to add insult to injury, Senator Warren’s proposed wealth tax would bring assets acquired by U.S. citizens, after having moved from the United States, into the wealth tax system. Come on! My house was acquired after I moved from the United States. My local business has nothing to do with the United States. My non-U.S. citizen spouse’s assets have nothing to do with United States.

Question: Would the United States like it if China imposed taxes on all property situated in the United States that was owned by Chinese citizens?

If this comes as a surprise to you it’s because you either don’t understand or are conveniently ignoring that the U.S. has extraterritorial tax regime—a regime imposed on Americans abroad. All indications are that the Warren wealth will actually leverage the injustice of United States citizenship-based taxation to make the whole world part of its tax base.

Seriously, these predatory, obscene and unjustifiable tax practices must stop. It’s simply not fair!!

God Bless the United States of America!

LETTER SUBMITTED BY PAUL DALE

U.S. Senate
Committee on Finance

To Whom This May Concern:

I am writing to express my great concern about the failure of the Senate Finance Committee to consider the impact of proposed tax legislation on me and on Americans living abroad generally. We are average, ordinary, every day people. We pay a lot of tax. We pay our fair share. We do this even though it is almost impossible for us to be both tax compliant in our country of residence and be compliant with U.S. tax laws.

We don’t understand why U.S. tax laws are being applied in an extraterritorial manner to income and assets that are not in the United States. Other countries don’t their citizens who live in the United States? Why should the United States tax U.S. citizens living and earning in other countries?

Our situation is bad. It is unique. Only the African dictatorship of Eritrea follows the lead of the United States by imposing worldwide taxation on its citizens who live outside the country.

I really don’t understand the indifference of the Senate Finance Committee to this situation. Interestingly, the Senate Finance Committee in 2015 recommended changes to the U.S. extraterritorial tax regimes. There have been no changes for the better, but many changes for the worse.

So far, the 2021 Senate Finance Hearings have been very, very bad. The Committee is obsessed with corporations without acknowledging that changes to corporate tax will have a huge effect on individuals. You haven’t mentioned that your obsession
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As described Elizabeth Warren’s proposed wealth tax will result in (1) taxation of assets earned outside the USA and (2) the taxation of our non-U.S. citizen spouses who we share our lives with.

And to add insult to injury, Senator Warren’s proposed wealth tax would bring assets acquired by U.S. citizens, after having moved from the United States, into the wealth tax system. I am an American only by accident of birth I move back to the UK with my British parents when I was only months old.

Everything (yes EVERYTHING), I have earned has been done outside the borders of the U.S., I have never lived in the U.S., but somehow the U.S. believes my foreign income belongs to it. I have not earned one single penny in the U.S., I use no services and I have no family or connections to the U.S. apart from a birth certificate. Additionally, all my non-U.S. citizen spouse’s assets have nothing to do with United States, but means we have to keep as financially separated as possible, which is a ridiculous state to be in because of archaic and punitive laws of Citizenship based taxation.

Question: Would the United States like it if China imposed taxes on all property situated in the United States that was owned by Chinese citizens?

Please just let me expatriate without the huge cost ($2350), why is it so expensive? Why is the U.S. the most expensive country to expatriate from? Why does it cost more to renounce citizenship then to gain it? Why can there not be a clause or provision ’if you paid 0 taxes for the last 5 years’ you can expatriate for free? As at the moment my tax returns are nothing but a burden for myself and the IRS, with time and money wasted by both parties for zero tax due.

If this comes as a surprise to you it’s because you either don’t understand or are conveniently ignoring that the U.S. has extraterritorial tax regime—a regime imposed on Americans abroad. All indications are that the Warren wealth will actually leverage the injustice of United States citizenship-based taxation to make the whole world part of its tax base.

Seriously, these predatory, obscene and unjustifiable tax practices must stop. It’s simply not fair!! Please join the rest of the world and tax on Residence, it is the only fair way, as an African Dictatorship is strange bedfellow for a country that prides itself on freedom.

LETTER SUBMITTED BY SYLVIA JEANET DE BRUIN

U.S. Senate  
Committee on Finance  
U.S. Senator Elizabeth Warren (MA)  
U.S. Edward “Ed” Markey (MA)  
U.S. Representative Lori Trahan (MA 3rd District)

Dear Senators,

As an individual, I support efforts to create opportunity through a fairer tax code. I look forward to the hearing next week where these opportunities are presented. But I worry. Whenever the discussion comes up—that we must close the tax gap. Make people pay their fair share, something usually gets lost. In an effort to create opportunity for America’s middle class, we overseas citizens are almost always treated as collateral damage.

And we too, are part of America’s middle class.

We vote. We pay our U.S. taxes. We pay our taxes to the country we live in. But we are constantly treated as not even second class citizens. We are constantly and structurally deprived of opportunities that are already granted to every ordinary working class resident of the U.S.

When you talk about fairness and creating opportunity, please consider all of the opportunities that the U.S. tax code deprives me, 9 million overseas Americans, and our families of.
The Opportunity to Have a Savings Account at a Bank

Because of unintended consequences related to the Foreign Accounts Tax Compliance Act (FATCA), U.S. citizens are treated as a 'liability' by any reputable financial institution outside of the United States.

Even when providing my SSN and full unredacted copies of my tax returns proving compliance with U.S. tax obligations, it is nearly impossible to be accepted for an interest-bearing bank account where I live.

Because banks are so terrified of the possibility that a U.S. citizen becomes a customer while fully compliant on their tax obligations, but later fails to pay them, they simply deny all law abiding U.S. citizens access to financial services out of fear of a few bad eggs.

This is because the banks regard the 30% withholding penalty in cases of non-compliant account holders as a "corporate death penalty". It's simply cheaper and safer for them to ban all U.S. citizens from having an account, even if we make every effort to comply with regulations.

The Opportunity to Have Investments in the Country I Live in

I am not a sophisticated investor. The most suitable products for me to own are safe and sane investments like a mutual fund or Exchange Traded Fund (ETF), rather than trying to pick winning stocks.

Unfortunately, because the United States considers all investment funds based outside of the United States to be suspect, I am subject to punitive PFIC reporting and tax rules.

Were I to buy the "VT" Vanguard Total World ETF investment fund from the NYSE–ARCA exchange, I would pay 15% to 20% in capital gains upon selling it. I'd be fully able to deduct or carry forward losses, if they occur.

Were I to buy the "VWRL" Vanguard FTSE All-World UCITS USD ETF investment fund from the NYSE–EuroNext exchange, I'd be subjected to 37% ordinary income tax on unrealized capital gains each year, limited deductibility, and a brutal 37 hour reporting form to be filed each and every year.

These are nearly identical funds, they are tightly regulated in U.S. and EU jurisdictions, but because one fund is from outside of the U.S., I cannot safely invest my money in it.

It's a moot point though. I don't have access to investment brokerage services where I live, because I'm a U.S. citizen.

A North Korean or Cuban customer is perfectly acceptable, and they can invest in a Vanguard fund through a bank here. I as a U.S. citizen cannot. All because of U.S. regulations that uniquely affect U.S. citizens.

The Opportunity to Have Investments in the Country I Am a Citizen of

The logical conclusion after reading the previous paragraph is to say, "Just buy the U.S. fund".

This is not an option for overseas Americans in many jurisdictions.

Because the United States is the only country in the world that subjects its citizens to an extraterritorial tax regime, local financial regulations don't account for the possibility that someone is either denied access to local financial services or that those services are severely penalized by the tax code of a country they don't live in.

Within Europe, multiple barriers exist to a U.S. citizen investing in a U.S. bank account. While I don't live in Germany or Italy, which apply similar punitive rules do discourage investment in offshore locations like the United States, the European MiFID II/PRIIPS regulations prevent EU residents without a high net worth from investing in non-EU investment products.

I suppose if I was rich and could afford the $500,000 minimum assets under management and a 1.0% annual fee, I'd qualify for a specialized investment manager that could put my money in U.S. based funds.

I'm middle class though, so I have to suck it up and stick to a 0% interest checking account.

Because the U.S. tax code penalizes investments outside of the U.S., even by people outside of the U.S., and because I am required to keep my investments in the EU, I am unable to follow good financial practices and invest my money.
The Opportunity to Start My Own Small Business
There’s nothing that outright stops me from starting my own business in the country where I live, but the United States sure goes out of its way to make it difficult. If I wanted to start a business, there are so many barriers that I’d face that citizens of any other country would not:
- I’d be denied business loans, on account of being a U.S. person
- I’d have difficulty finding a business bank account, on account of being a U.S. person
- I’d have to set aside a big pile of money for my super complicated 5471 form
- I’d have to pay GILTI tax, as a “U.S. company” in the Netherlands. Any competitors here wouldn’t, because they’re not American owned.
- I’d possibly have to pay self-employment tax, which no other competitor would need to do.

No other country throws up such barriers to its own citizen starting small businesses in the countries they live in. They’re just happy to see their citizens being successful. In America, only a large multinational is able to do business abroad.

The Opportunity to Have a Retirement That is Above Subsistence Levels
In most countries, the U.S. included, it is assumed that individuals will save for their retirement.
Unfortunately, this is also not an option for me, as a U.S. citizen.
Contributing to a Traditional IRA isn’t an option—MiFID II rules mean that most U.S. financial institutions will turn me away, for fear of hurting their compliance in the EU.
Contributing to a Roth IRA isn’t an option—those aren’t recognized as valid account types by most countries, and they’ll be subject to double taxation.
Contributing to a 401k isn’t an option—I don’t have a U.S. employer.
I suppose I could contribute to a Dutch retirement account, subject to rules similar to an IRA, but stricter.

Except it’s not clear that that’d not trigger those horrible PFIC rules. I’m not rich, so I can’t afford tens of thousands of dollars in accounting costs to fill out forms that were designed to be as complicated and time consuming as possible. Even if I could, accountant fees would eat up any benefit of saving for retirement.
And besides, most financial institutions here want nothing to do with Americans.
I’ll just have to settle for whatever the social security system in my current home country would pay out. The Windfall Elimination Provision ensures that even if I did move back to the United States and work for an additional 10 years for a total of more than 35 years of U.S. years, I wouldn’t get a full social security payment.

The Opportunity to Refinance My Mortgage Safely
In many countries, it’s normal to refinance a mortgage every few years. Unfortunately, the U.S. has a concept of “phantom gains” that makes this a very complicated and expensive process.

If I took out a loan for €100,000 today, and I paid it back next year, I’m liable for ordinary income taxation on any savings that resulted from the Euro declining in value.

€100,000 is $118,000 today, but if it’s $100,000 next year because the exchange rate dropped—well, that’s clearly an $18,000 gain, even though that also means my home is worth less, my salary paid in euros is worth less, and I’m no richer despite these “phantom gains” that the U.S. tax code has invented.

If I lived in the U.S., where my mortgage was in U.S. dollars, I wouldn’t need to worry about a change in the exchange rate leading to a massive tax bill on money that I never had.

The Opportunity to Sell My Home at a Loss and Not Be Punitively Taxed
What if there was a housing crisis and I needed to sell my home at a loss? I better hope that the U.S. dollar has stayed strong relative to the Euro.

Suppose that I bought a house this year for €100,000, with an EUR–USD exchange rate of $1.18 to the Euro. If the exchange rate is $1.35 5 years from now, I would have a capital gain even if I sold the house for a loss at €90,000.
Only Americans need to pay capital gains tax when selling the house, they live in, in another country. Only Americans need to worry about their capital loss being taxed as a gain.

The Opportunity for a Mortgage Interest Deduction
If I lived in the U.S., I'd be able to deduct the interest I pay on my mortgage from my U.S. taxes.

But because I am a U.S. citizen that does not live in the U.S., the tax code does not permit me to deduct my mortgage interest from the taxes I pay to a country I don't even live in.

The Opportunity for My Child to Benefit From the Taxes I Pay
What about our child? He'd hopefully receive benefits from the 49.5% income tax that I pay here. We happily pay them to ensure a strong social safety net.

Once again though, that global taxation throws a wrench in things. Benefits here like child support benefit, disability benefits, or student study are considered un-earned income, subject to taxation by the U.S.

Because some of these are paid to children or individuals with no income, they likely will end up paying U.S. taxes because they have no foreign taxes to offset it—because those are paid at another point in time, when they are in the workforce.

China doesn't tax government benefits of its Dutch residents. Germany doesn't tax government benefits of its Dutch residenta. But America is happy to undermine the opportunities the Netherlands (and other foreign lands) have for their residents.

The Opportunity to Feel Safe When Filing My Taxes
As if it wasn't painful enough to be deprived of these opportunities, entirely because the United States insists on being the one weird developed country that taxes non-resident citizens, we haven't even touched on compliance.

It's not subject to legal protections against excessive fines—they're penalties, not fines. Penalties are never excessive.

When a U.S. resident makes an honest, non-willful mistake on their taxes, the IRS determines whether or not to request an amendment and to assess reasonable interest-based penalties.

On most matters involving international forms—the FBAR, the FATCA 8938, the PFIC 8621 forms, we see a far more punitive approach. Non-willful errors are subject to a $10,000 fine, and willful errors are the greater of $100,000 or half of the money in the concerned account. Even if the information reporting error did not lead to a material income reporting error.

Of course, lines between non-willful and willful are blurry, given that the Treasury has sometimes gone as far as considering an insufficient understanding of the tax code to be willful negligence.

Either way, it doesn't matter—the penalties for honest mistakes are remarkably high in comparison to those made by U.S. residents. So, while a resident can trust that a small mistake will not have dire financial consequences, nonresident citizens don't get that.

It's pretty clear what the U.S. Government thinks of us. One of our annual information reporting forms goes to the Treasury’s Financial Crimes Enforcement Network.

We're lumped in with criminals simply because we have accounts in the countries we live in.

We don't get the opportunity to rest easy at the end of tax season. We instead get to stay up late, hoping that we did not make one single mistake.

Conclusion
If Congress wishes to look at making a fairer tax system that creates opportunity and benefit for ordinary Americans, it should take a moment to look at the numerous ways in which the tax code discriminates against U.S. citizens that live abroad.

We are subject to a separate, but more punitive tax system than the one that U.S. residents live in.

The opportunities we are deprived of did not stem from nothing—much of this, FATCA, PFIC, GILTI, and all the weirdness around exchange rates stems from a legitimate desire to make sure that the top 0.1% of Americans pay their fair share of taxes.
But it seems that at some point along the way, Congress lost sight of the goal. The U.S. tax code and treasury regulations are stripping away any form of financial opportunity for middle-class citizens that live abroad.

The rich can afford high powered lawyers to work around this. They can freely invest in the U.S. if they live in Europe because of the size of their bank accounts. They are not bothered by the thousands of dollars of tax preparation fees necessary to work with the mess that is foreign taxes, U.S. taxes, the tax treaties, and the forms needed to reconcile all of this.

They will never suffer the pain and humiliation of paying thousands of dollars to complete compliance paperwork that ultimately proves that they rightfully owed nothing that year. If you’re going to invoke terms like “civic duty” and “citizens have obligations”—at least make those duties and obligations benefit the state. I would rather pay the IRS than an accountant.

Please understand that every time you talk about fairness, and about dealing with offshore issues, you are also talking about making life tougher for ordinary Americans that live on other shores.

The 7 to 9 million overseas Americans, an overwhelmingly average folk that closely reflects the population living in the U.S., have been crying out for necessary reform and relief for over a decade now, with no meaningful talk from Congress about improvement.

Please stop taking away the opportunities that are afforded to Americans back home and other residents of the countries we live in.

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DEMOCRATS ABROAD
PO Box 15130
Washington, DC 20003

May 7, 2021

RE: “Creating Opportunity Through a Fairer Tax System”—Comments and Recommendations in Support of Americans Abroad

Democrats Abroad is grateful to comment on matters covered in the April 27th Fiscal Responsibility and Economic Growth Subcommittee hearing and noted in the chair and co-chair statements on “Creating Opportunity Through a Fairer Tax System.” This submission reflects the experience of non-resident citizens navigating inequitable provisions in the U.S. tax system and it includes recommendations to address tax code injustices created by tax policy established without a clear understanding of its impact on ordinary, middle-class Americans living abroad.

I. SUMMARY

The State Department estimates there are 9 million Americans living outside the United States. Unfortunately, we suffer from the stubborn misperception—driving the development of tax policy and regulations—that Americans abroad are uniformly “high-rollers”, living a life of luxury in low- or no-tax countries. Research published at the behest of Congressional staff demonstrates that we live abroad primarily because a relationship, employment, education, or adventure took us abroad, and we decided to stay.¹ The vast majority of us are middle-class Americans, working, raising families, and retiring in countries with a higher overall tax-burden than the U.S. The tax policies and regulations that affect Americans abroad do not reflect this reality, but instead penalize millions of us ordinary American citizens in attempts to foil a few bad actors.

Filing taxes from abroad and navigating the convergence of the U.S. and a non-U.S. tax system is stunningly complex. Research has found most seek the services of ex-

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Democrats Abroad recognizes that the American Jobs Plan and American Families Plan—federal government spending programs essential to supporting Americans through the pandemic, rescuing the economy and investing in our future prosperity—are going to place pressure on current and future taxpayers.

Democrats Abroad supports the aim of raising additional federal government revenue from those wealthy Americans and large U.S. corporations not paying their fair share. We celebrate President Biden’s pledge not to raise taxes on those making under $400,000 per annum. We laud the actions of Congress in advancing tax policies that treat low-income Americans differently from high-income Americans, such as the income-based eligibility criteria for receiving CARES Act and American Rescue Plan Act pandemic aid. And we strongly support the Made In America Tax Plan reforms to the Tax Cuts and Jobs Act that remove incentives to offshore jobs and R&D, move profits to low-tax jurisdictions, and abuse tax havens.

However, we also need Congress to address the distressing taxation predicament of working-class Americans living abroad. We need Congress to understand our community, recognize our tax problems and enact reforms to reduce the hardships we inadvertently suffer due to laws meant to deal with bad actors, not ordinary citizens.

Americans abroad long to be placed on a taxation par with others who live and are taxed in a country other than their country of citizenship. Most tax systems require citizens to declare revenue in the country where the taxpayer generates it, i.e., residency-based taxation (RBT). Democrats Abroad and the other organizations representing Americans abroad have had detailed discussions with Congress about a proposal to enact RBT and other reforms for Americans abroad that eliminate double taxation, remove barriers to banking, saving and investing and simplify filing from abroad.

We will continue to advocate in support of an RBT model that provides relief to Americans abroad, prevents residency-driven U.S. tax avoidance and is revenue neutral to the federal government. We believe the time will come when Congress embraces RBT.

Reform Recommendations

Now when the government is building a fairer tax system to create opportunity for all Americans, we recommend these reforms for Americans abroad, which comply with the Biden Administration’s plan to place the greatest burden of taxation on those with the greatest ability to pay.

1. A tax filing exemption for Americans abroad compliant with financial account reporting requirements who owe zero U.S. tax. We believe this reform fits into the aims and proposed provisions of the American Families Plan.

2. An exemption from GILTI taxes on the profits of controlled foreign corporations owned by Americans abroad compliant with foreign financial account reporting requirements who have income under $400,000. We believe this reform fits into the proposed provisions of the Made In America Tax Plan.

3. Updates to the Report of Foreign Bank and Financial Accounts (FBAR) including:
   - the indexation of the FBAR reporting threshold for inflation;
   - creation of an FBAR filing threshold for Americans abroad that is five (5) times higher than the indexed threshold;
   - the elimination of FBAR and FATCA filing-duplication;
   - modification of the enormously out-of-proportion penalties for non-willful neglect to file FBAR reports; and
   - reinstatement of the option to paper-file the FBAR.

Further, we re-affirm our support for an exemption for Americans abroad from FATCA reporting of the financial accounts in the country where they live and pay tax. We believe these financial account reporting reforms fit into the proposed provisions of the American Jobs Plan/Made in America Tax Plan.
II. BACKGROUND

For many years Americans abroad have been speaking to U.S. lawmakers about the genuine personal and financial hardships we experience due to the taxation of our income both by our country of residence and by the U.S. The harm caused to Americans abroad by inordinately complex U.S. tax-filing, by double taxation, and by policy-borne barriers to banking, saving, and investing, is so severe that it often feels to us that the U.S. is punishing us for moving to another country.

Congress enacts tax policy, and Treasury implements it, in our view without giving adequate prior consideration for the unintended adverse impact it might have on ordinary working-class Americans who are living abroad. We do not live abroad to avoid paying taxes; we pay taxes in the countries we live in, the vast majority of which have higher tax rates than does the U.S. Americans abroad need Congress and Treasury officials to understand who we are so that they can strike a better balance in policy making between discouraging and apprehending tax cheats—which we strongly support—and caring for the welfare of ordinary Americans living abroad.

Americans abroad understand that we are collateral damage in an on-going war against tax cheats. Those seeking to hide assessable income from the IRS engage legions of clever lawyers, bankers, accountants, and formation agents to collaborate on the development of ever-more complex tax-avoidance schemes. The fight against their tireless efforts routinely results in policy that makes life harder for ordinary Americans abroad. In alignment with Congressional efforts and the Biden Administration's intent, we strongly support efforts to crack down on tax cheats; however, the next tax reform debate must take into consideration the perspective of Americans abroad, a gravely misunderstood and under-acknowledged community.

WHO ARE AMERICANS ABROAD AND WHAT ARE OUR TAX PROBLEMS?

a. We Are Not “Fat Cats”

Democrats Abroad wants desperately to vanquish the persistent, apocryphal stereotype that the 9 million American civilians living abroad are wealthy “fat cats” avoiding U.S. taxes. The vast majority of us are ordinary working-class Americans, about whom our research has found:

- 61% had household income less than $100,000.
- 72% were married, 71% of whom to non-U.S. spouses.
- 63% owned their own home.
- 32% had moved abroad for marriage or a relationship.
- 25% had left the U.S. for work/employment.
- 64% had made their home abroad and had no plan to return to the U.S.
- Most live in countries with a higher overall tax-burden than the U.S.

b. Tax Problems for Individuals

While the Foreign Earned Income Exclusion and Foreign Tax Credit provide some protection from double taxation, there are many types of income that fall outside those provisions and are double taxed. These include income associated with retirees and with vulnerable citizens living on foreign government social welfare. Some U.S. tax treaties protect savings in statutory retirement accounts from double taxation, but, as we have informed this Committee previously, most treaties do not.

Punitive tax-treatment of non-U.S. investment (Passive Foreign Investment Companies or PFICs) and saving vehicles, combined with provisions in securities, national security, and banking laws, make saving for retirement or the family's future very expensive and inefficient, if not impossible. They create obstacles to saving and investing both in the U.S. and abroad, which is an intolerable hardship for families.

Even the family home puts the non-resident taxpayer at risk. Americans abroad are entitled to no deduction for interest on a home mortgage, nor to favorable capital gains and other tax treatment on sale. In fact, they are at risk of a capital gains tax liability should fluctuations in exchange rates create an artificial gain at the time of property sale or even re-finance.

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5 “Tax Filing From Abroad.”
Filing from abroad is inordinately complex, forcing most Americans abroad to seek the services of expensive tax-return preparers who understand the tax systems of both the U.S. and the country where they reside. On average, Americans abroad pay nearly triple what U.S.-based filers pay for tax preparation. Therefore, most are paying heavily to maintain U.S. tax compliance even though they owe no tax to the U.S. government.

The burden of tax filing from abroad is compounded by foreign financial account reporting requirements. Since the Foreign Account Tax Compliance Act (FATCA) fully implemented double-disclosure foreign account and financial asset reporting—meaning that both the individual and their bank must report—30% of Americans abroad have reported impaired access to even ordinary financial products and services where they live. This “lockout” of Americans abroad by foreign banks and financial institutions has been enormously disruptive for those affected, as noted in sworn testimony to the April 26, 2017 House Subcommittee on Government Operations hearing, “Reviewing the Unintended Consequences of FATCA.”

Failure to comply with FBAR reporting requirements for foreign bank and other foreign financial accounts carries heavy penalties that are far out of proportion to the taxpayer lapse, especially when, for example, it is due to ignorance borne of IRS neglect, language barriers, or lack of ability to use or to access electronic devices which are mandatory for FBAR filing.

Non-U.S. domestic partners of Americans abroad often remove their U.S. spouse from financial accounts to avoid U.S. financial account reporting requirements, making the American vulnerable to financial abuse, manipulation, or neglect.

Americans abroad also suffer from serious deficiencies in IRS service and support. For many years the IRS has provided little to no advice about tax-filing obligations to non-resident citizens. Ignorance, misinformation, and confusion abound, even among consulate and embassy staff. In recent years the IRS has withdrawn staff from international postings and replaced them with telephone and online support that vastly underestimates how inordinately difficult it is to file taxes from abroad. FreeFile programs are not suited to non-resident filers and free support from volunteer tax return preparers available to aged and indigent taxpayers in the U.S. is not accessible to those living abroad.

The unfortunate experiences of Americans abroad in accessing the pandemic aid provide further evidence of the need for greater attention by the IRS to our needs. Research published in October 2020 on Americans abroad and the CARES Act indicates that only two in three Americans abroad who were eligible for a CARES Act stimulus payment received one. Further, 70% of those who received the aid received a check, which took on average 12 weeks to arrive and be converted into cash. IRS data suggesting 90% of CARES Act stimulus payments were distributed within two weeks clearly made no accommodation for the time it took for the cash to actually reach the hands of Americans abroad (and turned a blind eye to the fees incurred for cashing a U.S. government check abroad.)

The IRS cannot deposit funds, e.g., stimulus payments or tax refunds, into a non-resident American's foreign bank account. Direct deposit is available for bank accounts located only in the U.S. Requests by Americans abroad groups to change this policy have so far yielded no response, but given the Social Security Administration, Veterans Administration and Railroad Retirement Board have worked out how to make payments into the non-U.S. bank accounts of beneficiaries living abroad, we are hopeful the IRS will soon work out a way.

c. Tax Problems for Employees and Small Business Owners

U.S. taxation puts job-seeking Americans abroad pursuing tax-equalization at a competitive disadvantage in the job market as it makes them 40% more expensive for companies to hire than those of other nationalities.

Financial account reporting requirements make Americans abroad very unattractive as business partners to those averse to sending their business’s financial information to the U.S. government.

The Repatriation and GILTI taxes in the 2017 Tax Cuts and Jobs Act are causing an existential crisis for the small to medium-sized businesses.

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"Tax Filing From Abroad."


"Americans Abroad and CARES Act Aid," Bit.ly/CARESActandAmericansAbroad.
owned by Americans abroad. The reforms that ushered in these new taxes have been enormously beneficial for American companies with profits in overseas subsidiaries. But conversely, for Americans abroad, retirement savings held in their business are being drained to pay Repatriation tax and their current and future earnings are double taxed by GILTI; those Americans are being forced to either restructure their businesses at considerable cost or to close them entirely.

d. Transformational Policy Is Coming; Don’t Leave Americans Abroad Out

The programs in the American Jobs Plan/Made In America Tax Plan and the American Families Plan comprise a generation-defining investment in American commercial and social infrastructure and a commitment to grow the middle-class and expand the benefits of economic growth to all Americans.

Americans living abroad manage U.S. businesses and other enterprises, promote U.S. interests and serve as unofficial ambassadors of American culture and values. They contribute to the U.S. economy, industry, foreign relations, incoming investment and cultural exchange, all of which Congress has made little attempt to understand. Americans abroad are yet another component of U.S. infrastructure that the government has neglected and in which the government has underinvested. The reforms outlined herein will produce new personal and financial opportunities for the community of Americans abroad and will ensure they are not left out of this transformational policy-making.

Implementing residency-based taxation, a FATCA filing exemption for the accounts of Americans abroad in the countries where they live and already pay tax, and reforms to improve the FBAR would address all these problems. However, we also understand that (1) the pandemic has put the government under enormous revenue pressure to invest in physical and social infrastructure to put the American economy back on its feet, and (2) we have more work to do to persuade Congress that residency-based taxation can be introduced without expanding tax avoidance by High Net Worth Americans. We have therefore established three reform recommendations for incorporation into the American Jobs Plan/Made In America Tax Plan and the American Families Plan that will provide desperately needed relief to Americans abroad.

III. THE CASE FOR A FILING EXEMPTION FOR AMERICANS ABROAD WHO OWE NO U.S. TAX

Americans abroad bear onerous tax compliance responsibilities, facing taxation firstly by their country of residence and then by the U.S. Those who do have a U.S. tax liability are paying twice on the same dollar of income.

Filing from abroad is inordinately complex and IRS support is insufficient to enable Americans abroad to easily comply. IRS resources outside the U.S. have been withdrawn. IRS telephone support is not accessible from many countries and, when it is, the number is not toll-free, wait times are lengthy and reports suggest operators lack the knowledge to address questions particular to non-resident filers.

The IRS’s Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) programs offer free basic tax return preparation to qualified individuals in the U.S. only.10 The IRS Locator tool that connects qualified individuals with program volunteers in their local area uses U.S. zip codes. There is no online version of the program for Americans abroad. IRS 2021 communications recruiting tax preparation participants for the program does not solicit applications from those skilled and prepared to help eligible Americans abroad.

The IRS FreeFile fillable forms for electronic filing have multiple barriers to access by Americans abroad.11 Creating an IRS account to file electronically requires a U.S. telephone number. Many e:forms require the filer to provide a U.S. address. Entering a foreign address—even U.S. military addresses abroad—may cause the system to reject the return entirely. Two of the forms most commonly used by Americans abroad—Form 2555 for declaring bona fide offshore residency and the Foreign Earned Income Exclusion and Form 1116 for claiming a Foreign Tax Credit—cannot be filed electronically because required attachments cannot be included. The FreeFile fillable forms system does not include the Foreign Employee Compensation Form nor Form 2350, Application for Extension of Time to File U.S. Income Tax Return.

The IRS YouTube channel provides video support to U.S. taxpayers and advisers that help them file; but there are no videos specifically addressing the myriad problems and challenges faced by Americans abroad.12

For all these reasons, nearly 60% of Americans filing from abroad pay tax return preparers to complete their U.S. reports and returns.13 More than 60% pay more than $500 for tax return preparation services,14 in some cases much more. This compares to the U.S. average cost for tax preparation of $175–$275.15

The irony is that non-resident filers are often paying these exorbitant fees to professionals to prepare tax returns that indicate that there is no U.S. tax to pay. Sixty percent of Americans abroad have income under $100,000.16 Overseas residency makes them eligible for the Foreign Earned Income Exclusion ($107,600 in 2020) and most have Foreign Tax Credits for tax already paid.

PROPOSAL: We propose eliminating the tax filing requirement for Americans abroad who owe no tax.

- The IRS Substantial Presence Test17 exists for taxpayers to certify offshore residency.
- Tax calculation worksheets can assist ordinary earners to demonstrate that they have a $0 U.S. tax liability.
- Declarations can be established for non-resident taxpayers to certify their eligibility for the $0 tax liability filing exemption.
- The IRS has already established categories of Americans who do not have to file, having defined filing status, age and annually-updated income eligibility criteria.
- De Minimis provisions can exclude High Net Worth taxpayers from eligibility for the $0 tax liability filing exemption.
- FBAR filings and FATCA filings keep IRS eyes on taxpayers even if they don’t have to file.

The American Families Plan holds the promise of delivering an historic shift towards a more equitable America. Americans abroad ask not to be left out. As we have demonstrated, the Internal Revenue Code is in many ways highly punitive to ordinary American families living middle-class lives abroad and is, therefore, unjust. A tax filing exemption for those working-class Americans who do not owe any U.S. tax would provide consequential relief to American families abroad with no impact on government revenue-raising.

IV. THE CASE FOR A GILTI TAX EXEMPTION FOR AMERICANS ABROAD WITH INCOME UNDER $400,000

Research on Americans abroad published in 2017 and 2019 indicates somewhere between 2% and 20% of Americans abroad own and operate small to medium sized businesses registered in the countries where they live.18 Americans abroad owning and operating businesses are an exceedingly diverse group; they are architects, yoga instructors, retailers, recruiters, beekeepers, IT professionals, film and television producers, music distributors, advertising agents, financial service providers and more. Comments from some of them about the 2017 Tax Cuts and Jobs Act (TCJA) are included in a briefing document we published for Congress in 2018 entitled “Another Accidental Tax Penalty for Americans Abroad: This Time Hitting Small to Medium Sized Business Owners.”19

The Repatriation Tax and the GILTI Tax introduced in the TCJA were carefully negotiated by corporate America over many years; however, they came as a great shock to small business owners living abroad. Although the Repatriation Tax and GILTI Tax provided enormous tax relief to U.S. multinationals, enabling them to repatriate profits of their offshore subsidiaries at deeply discounted tax rates and with offsets and deductions that ensure that little to no tax is due, the impact on individuals who own companies registered abroad has been devastating.

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12 https://www.youtube.com/channel/UCcWZOFh3l-1LC7UcM7dCtQg.
13 Tax Filing From Abroad.
14 Tax Filing From Abroad.
16 Tax Filing From Abroad.
18 “Tax Filing From Abroad“ and “Can We Please Stop Paying Twice?”
19 Another Accidental Tax Penalty for Americans Abroad: This Time Hitting Small to Medium Sized Business Owners,” bit.ly/AnotherAccidentalTax.
Owners of small to medium sized businesses without access to employer-provided retirement savings plans often retain profits in their businesses to save for retirement. The Repatriation Tax, imposed retroactively on retained profits going back as far as 1986, is devouring their retirement savings. Those without funds to meet the tax have had to liquidate assets, which may have attracted capital gains or other local tax, further increasing their financial pain.

The GILTI Taxes on all future earnings—earnings already taxed in the country where the business is registered and operates—must be declared on the owner’s personal tax filing, taxed at the taxpayer’s marginal rate rather than the 10.5% rate (50% of 21% corporate tax rate) available to corporations, afforded none of the foreign tax credits available to corporations and calculated using a highly complex formula that references corporate factors wholly irrelevant to small businesses. The absence of provisions relevant to the small to medium sized businesses owned by Americans abroad suggest that the GILTI tax was not conceived with the small to medium sized businesses of ordinary Americans abroad in mind.

New GILTI rules finalized by Treasury in the middle of 2020 gave individuals a means of accessing the discounted corporate tax rate (Sec. 962 election) and the 50% tax rate discount (Sec. 250 deduction) available to corporations. Claiming the Sec. 962 election and Sec. 250 deduction, however, is inordinately complex and very expensive. Further, it does not completely resolve the double taxation issues, as the profits of their companies will be taxed yet again when the profits are paid out to the business owner as dividends. So, although regulatory relief was provided, it is incomplete and it is not commercially accessible to ordinary working class Americans abroad who rely on their businesses to provide for themselves and their families. Many of them have already been forced to close their businesses after years of investment and effort, or to undergo costly corporate restructuring. In either case the outcome is highly punitive.

American business owners abroad have truly suffered under the burden of the double taxation wrought by Repatriation and GILTI. And now the pandemic has in many cases increased economic duress. The Made In America Tax Plan proposals increasing the GILTI tax to perhaps twice the current rate. The prospect of the GILTI tax increase is causing anger and levels of distress for everyday working class American families that Congress should find intolerable and unacceptable.

PROPOSAL: We propose a GILTI tax exemption for the profits of small businesses owned by Americans abroad with income under $400,000 per annum.

- The IRS Substantial Presence Test exists for taxpayers to demonstrate offshore residency.
- Tax calculation worksheets assist ordinary earners to demonstrate that they have income under $400,000.
- As Made in America Tax Plan proposals include increasing the GILTI tax rate, this exemption is consistent with President Biden’s pledge not to increase taxes on any American with income under $400,000 per annum.
- De Minimis provisions can exclude High Net Worth taxpayers from eligibility for the GILTI Tax exemption.
- Eligibility criteria applicable to the taxpayer’s business can include limits on annual turnover, employees or other.
- Declarations can be established for Americans abroad who own small to medium size businesses abroad to certify their eligibility for the GILTI Tax exemption.
- FBAR filings and FATCA filings keep IRS eyes on taxpayers.

The American Jobs Plan/Made In America Tax Plan lays out the steps towards a fairer tax code that rewards work and not wealth, and makes sure that corporations and the highest income individuals pay their fair share. An exemption for middle class Americans from the GILTI tax, a tax that was never meant to impact them, fulfils these ambitions and is consistent with President Biden’s promise to protect those making income under $400,000 per annum from tax increases.

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V. THE CASE FOR REFORMS TO THE REPORT OF FOREIGN BANK AND FINANCIAL ACCOUNTS (FBAR) AND FATCA

Court cases involving an FBAR violations are not rare. The foreign financial account reporting requirement is clearly instrumental in the apprehension of tax evaders using offshore financial accounts to hide assessable income. The perpetrators, however, are invariably citizens living inside of the U.S. rather than living abroad.21

Rules guiding the implementation of the FBAR have not been adjusted since the law was passed in 1970. Reasonable updates can both improve the report’s focus on bad actors and simplify compliance for Americans abroad.

PROPOSAL: We propose the following reforms to the FBAR.

1. Index the $10,000 reporting threshold for inflation.
2. Create a separate reporting threshold for Americans living abroad perhaps 5 times higher.
3. Address the duplication of reporting on FBAR and FATCA, as recommended by the IRS National Taxpayer Advocate.
4. Modify the out-of-proportion penalties for non-willful failure to disclose accounts.
5. Restore the option to submit FBAR paper filings.
6. Provide for FBAR reporting in Spanish and other languages.

Further, we re-affirm our long-standing support for the Overseas Americans Financial Access Act which would exempt from FATCA reporting the foreign financial accounts of Americans abroad in the countries where they live and face taxation because tax cheats do not hide assessable income in the countries where they live. Further, the Corporate Transparency Act adds a powerful new tool for discouraging and apprehending tax cheats. As the law mandating disclosure of beneficial interests in anonymous shell companies is implemented, reports will illuminate the activities of the tax cheats and other bad actors that foreign financial account disclosure did not.

Consistent with President Biden's vision in the American Families Plan, these reforms help ensure that all Americans have access to essential banking services and the financial infrastructure necessary to create opportunity. They can be modified to exempt certain individuals from eligibility and ensure they enhance existing tax enforcement mechanisms. They will focus policy on bad actors and provide relief to those who have long suffered unintended adverse consequences, such as bank lock outs. Finally, these FBAR and FATCA reform recommendations are entirely consistent with the goals of getting everyone to pay their fair share.

Thank you for the opportunity to comment and provide recommendations. Not since the Carter Administration has there been a hearing in the U.S. Congress on Americans living abroad and the range of serious personal and financial problems U.S. taxation causes for them, their families, their businesses and the U.S. and non-U.S. entities they do business with. We re-state our belief that it is past time that the issues of Americans abroad be heard, documented in the public record, and addressed by the government.

Thank you for your interest in these matters. Please contact Carmelan Polce of our Taxation Task Force (+61 404 767 088 or carmelan@democratsabroad.org) or the undersigned with any questions about the information and recommendations provided herein.

Sincerely,

Julia Bryan
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CC: The Honorable Nancy Pelosi
The Honorable Charles Schumer
Speaker of the House
Majority Leader
U.S. House of Representatives
U.S. Senate
Office of the Speaker, United States
S–224, United States Capitol

LETTER SUBMITTED BY SUSAN DE PAUL

To whom it may concern,

I am a proud citizen of the United States of America, but I am writing today to call attention to the injustice of the U.S. extraterritorial tax regime and how it severely limits the freedom of individual U.S. citizens living outside the United States. This system is highly unfair, and it’s time that the extraterritorial tax system be abolished with the goal of “Creating Opportunity Through a Fairer Tax System” as proposed by the organization Stop Extraterritorial American Taxation (SEAT).

The only thing that makes me different from U.S. residents is that I live outside the United States. For the record, I did not move from the United States to avoid U.S. taxation. In fact, I have discovered that by living outside the United States I am subject to (1) taxation in the country where I live and (2) a more punitive form of taxation by the U.S. than what is imposed on U.S. residents. My only crime seems to be that I live outside the United States—and, therefore, my income and assets are foreign to the United States. However, the income and assets are actually local to me.

I am writing to express my deep concern about the failure of the Senate Finance Committee to consider the impact of proposed tax legislation on me and on Americans living abroad generally. We are average, ordinary, everyday people. Because we are flesh and blood humans, we need to eat. Because we will get old and plan to eventually retire, we need to save for retirement. Because we are individuals with responsibilities to our families, our communities, and our countries of residence, we may need to operate our own small businesses. We are definitely NOT mini-multinational corporations, and we are tired of being treated as though our normal day-to-day activities are somehow “offshore” and deserving of punishment. We are tax-compliant in our countries of residence. We pay a lot of tax. We pay our fair share. We do this even though it is almost impossible for us to be both tax-compliant in
our country of residence and compliant with U.S. tax laws. We do not understand why U.S. tax laws are being applied in an extraterritorial manner to income and assets that are neither generated nor disposed of in the United States. Other countries do not tax their citizens who live in the United States. Why should the United States tax U.S. citizens living in other countries?

Our situation is bad. It is also nearly unique. Only the African dictatorship of Eritrea follows the lead of the United States by imposing worldwide taxation on its citizens who live outside the country.

I do not understand the indifference of the Senate Finance Committee to this situation. Interestingly, the Senate Finance Committee in 2015 recommended changes to the U.S. extraterritorial tax regimes. Unfortunately, there have been no changes for the better but many changes for the worse.

So far, the 2021 Senate Finance Hearings have been very, very bad for U.S. citizens living abroad and the Committee shows absolutely no understanding of the issues facing us. The Committee is obsessed with corporations without acknowledging that changes to corporate tax will have a huge effect on individuals.

The taxation of corporations will have a bigger impact on many individuals with small businesses than on a relatively small number of corporations.

The hearing on April 27, 2021—about a wealth tax—took the treatment of U.S. citizens abroad to a new level. The bottom line is this: as described Elizabeth Warren’s proposed wealth tax will result in (1) taxation of assets earned outside the U.S.A. and (2) the taxation of our non-U.S. citizen spouses whom we share our lives with.

To add insult to injury, Senator Warren’s proposed wealth tax would tax assets acquired abroad by U.S. citizens. Houses purchased abroad with foreign earnings have nothing to do with the United States, nor do small businesses that were founded abroad. My non-U.S. citizen spouse’s assets also have nothing to do with United States.

Here is an interesting question: Would the United States like it if China imposed taxes on all property situated in the United States that was owned by Chinese citizens?

Admittedly, the current threshold for the wealth tax is $50 million and, therefore, far beyond the middle class. However, there is no provision for it to be indexed to inflation. As U.S. citizens who live abroad well know, the Report of Foreign Bank and Financial Accounts (FBAR) minimum reporting threshold of $10k remains unchanged since 1970 even though $10,000 in 1970 is worth $68,267 today. Similarly, the level of the Foreign Earned Income Exclusion (FEIE) was set at $75k in 1981 but was not indexed to inflation for several decades. Although $75k in 1981 is equivalent to $226k in 2021 dollars, the current FEIE level is only $107k. Past policies aimed at “wealthy” expatriates have a way of trickling down into the middle class, and I do not want to see future generations of ordinary Americans (such as my foreign-born children) burdened in this way.

As for consideration of the foreign spouse’s assets, even those with modest incomes would presumably need their spouses to prove that they are not in the $50 million wealth range if this law passes, but why should a person without U.S. citizenship and without even a green card be obliged to report their assets to what is (to them) an entirely foreign government? Non-U.S.-resident, non-citizen spouses without green cards have none of the benefits of U.S. citizenship (neither in terms of employment rights nor inheritance). They do not use the infrastructure of the U.S., and needlessly to say, they cannot vote. The money they have earned has been earned abroad. Taxing such people is a massive overreach by the U.S. into other countries’ jurisdictions.

If this comes as a surprise to you it’s because you either do not understand or are conveniently ignoring that the U.S. has extraterritorial tax regime—a regime imposed on Americans abroad. All indications are that the Warren wealth tax will actually leverage the injustice of United States citizenship-based taxation to make the whole world part of its tax base.

I support efforts to make sure that U.S. residents do not evade taxation by stashing their wealth in shell companies and secret accounts, but there is a significant difference between hiding taxable income that was earned within the U.S. and being taxed twice on money legally earned abroad by U.S. citizens who also live abroad. I would like to see evidence that the Senate understands this important distinction.
LETTER SUBMITTED BY CHRISTINE DYMKOWSKI

I am writing again in the probably forlorn hope that someone in Washington will finally pay attention to the extreme injustice of the U.S. extraterritorial tax regime and how it severely limits the freedom of individual U.S. citizens living outside the United States. This extremely unfair system needs to be abolished, if you really intend to “Create[e] Opportunity Through a Fairer Tax System”.

I did not move from the United States to avoid U.S. taxation, but because I fell in love with someone British. I have lived and worked in the UK my entire adult life, and because I live outside the United States, I am subject to (1) taxation in the UK and (2) a more punitive form of U.S. taxation than is imposed on U.S. residents. This is because my income and assets are foreign to the United States, although they are actually local to me.

I am greatly disappointed by the continued failure of the Senate Finance Committee to consider the impact of proposed tax legislation on individual Americans living abroad. We are ordinary people who need to earn a living and save for retirement. We are NOT mini multinational corporations hiding U.S. assets “offshore”. Because of the U.S.’s punitive tax treatment of Americans living abroad, we find it almost impossible to be tax compliant both in our country of residence and with U.S. tax laws. I do not understand why U.S. tax laws are being applied in an extraterritorial manner to income and assets that have nothing to do with the United States. Other countries don’t tax their citizens who live in the United States, so why should the United States tax U.S. citizens living in other countries?

Our situation is uniquely bad. Only dictator-led Eritrea follows the lead of the United States in imposing worldwide taxation on its citizens who live outside the country, but for them it’s only 2% of income, rather than the confiscatory rate that the U.S. imposes on, for example, mutual funds local to me. It’s ironic that the U.S. State Department regularly condemned Eritrea for its extraterritorial tax until, I presume, it realized the U.S. is guilty of worse.

I cannot understand the indifference of the Senate Finance Committee to this unjust situation, especially when, as long ago as 2015, the SFC itself recommended changes to the U.S. extraterritorial tax regime. There have been no changes for the better, but many changes for the worse.

So far, the 2021 Senate Finance Hearings have been totally inadequate. The Committee is obsessed with corporations and ignores the ways in which changes to corporate tax will have a huge effect on individuals. The hearing on April 27, 2021—about Elizabeth Warren’s proposed wealth tax—took the treatment of U.S. citizens abroad to a new level, proposing (1) the taxation of assets earned outside the USA and (2) the taxation of our non-U.S. citizen spouses.

Try to imagine this situation from the opposite point of view. Would the U.S. be happy if Europeans living in the U.S., working for U.S. companies, and earning U.S. dollars had to pay tax not only to the U.S. but to the countries of which they are citizens? I doubt it.

Please stop ignoring the fact that the U.S. extraterritorial tax regime makes life difficult, if not impossible, for Americans living abroad. Show that you understand the difference between state side Americans trying to hide assets and avoid paying tax and Americans living abroad who have no financial and economic ties to the U.S.

LETTER SUBMITTED BY ASHLEY LYNN ELLIS

Dear Senate Finance Committee,

I have written previous, very long letters to your committee and to my Senators and they seem to just be ignored. So in this brief message, I am asking you to please stop tax discrimination against U.S. citizens abroad. We probably are the most discriminated group in U.S. tax code, yet we are NEVER considered. We are ALWAYS IGNORED. Please make revisions to current rules (FATCA, GILTI, FBAR reporting, etc) to consider middle class Americans abroad.

In our local countries, we NEED to be able to EASILY have interest savings accounts, pensions, life insurance savings plans, own businesses, etc. We need to be able to compete locally. Allow us to live like regular people should. Stop imposing high fines and pretentious laws on those of us who are low or middle class people. I live in a developing country and cannot have a life insurance savings account because the reporting to the IRS costs more than any benefit. That is extremely un-
just. I have zero retirement options. Also, the IRS website does not allow any online services for expats (IP Pin number, for example). We do not have equal access to hardly anything, yet are slammed with the highest penalties.

I get migraines and lose sleep over this. I never am moving back to the U.S. I worry daily about my children's future. I already tell them they can renounce U.S. citizenship if they want to be successful in their home country, and it breaks my heart I have to tell my kids these things. I wish they could be both American and Mexican. It is ridiculous. Please make reforms to protect middle class Americans abroad, or just switch the Residency Based Taxation like the rest of the developed world. Let us live our lives where we choose. We are subject to local tax laws and it makes no sense that the U.S. does this. FATCA is the biggest nightmare. Stop discriminating against us. Stop ignoring us. Stop forcing us to renounce citizenship. Help us.

I hope you read this and do not leave us behind.

Thank you,

Your average American abroad

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LETTER SUBMITTED BY MARK ENGEN

To Whom This May Concern:

I am a proud citizen of the United States of America, living overseas—I am “boots on the ground,” helping to escort U.S. products and services into the global markets. Currently, the U.S. tax system taxes me because I am in a citizen. Worse yet, it requires tax forms of me no matter where I live. The tax forms are more complex and restrictive than any citizen living in USA. The taxforming system means that the taxation policies and regulations make it nearly impossible to own a business and impossible to have a mutual fund. It also makes it more difficult for me to have a bank account. FATCA/FBAR also destroys my financial privacy. FATCA/FBAR means that it is impossible to fulfil any nondisclosure agreements with my employer, and would make it impossible for me to have any financial leadership position with bank signature authority.

Extra-territorial tax reporting, taxing, and financial account tracking are unfair, immoral, and unconstitutional.

All countries tax their RESIDENTS and not their CITIZENS.

You must:

– End FATCA. It is unconstitutional and makes U.S. expatriate patriots into suspected criminals. The penalties are horrendous and redundant.

– End FBAR. It is unconstitutional and makes U.S. expatriate patriots into suspected criminals. The penalties are horrendous and redundant.

– Throughout the U.S. tax system, replace “U.S. citizen” with “U.S. resident.”

– End all tax-reporting forms for citizens not residing in USA.

This proposal is tax neutral. It is a myth that USA can gain tax revenue from overseas residents. Please see this article showing that USA cannot gain revenue and the cost of processing forms is creating deficit spending.


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LETTER SUBMITTED BY ANDREA FERNANDEZ

U.S. Senate
Committee on Finance
Subcommittee on Fiscal Responsibility and Economic Growth

To the members of the Subcommittee on Fiscal Responsibility and Economic Growth:

I am writing to you as an ordinary U.S. citizen who happens to live abroad and would like to share my perspective on “a fairer tax system”.

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I have lived in London for the last 13 years. I can assure you I am not a tax dodger trying to escape the U.S. tax system. I got transferred here for 6 months with a consultancy I worked for and fell in love with the city. Eventually I changed jobs, got married, bought a house and had a child. I don’t know that I will stay in the UK forever, as my mom is elderly, but I like having the flexibility.

Today I am a Director at a non-profit organization focused on supporting cities around the world to address the climate crisis—hardly the picture of a wealthy expat living a life of luxury. Please keep in mind that there are millions of ordinary Americans overseas who are salaried workers, who aren’t living off of investment income. I dutifully pay my high taxes to the British government and under the dual taxation treaty, fortunately that usually eliminates my U.S. tax burden. And yet like so many others, I have to shell out £700 to prepare tax forms to prove to the U.S. that I don’t owe it taxes from my UK income. The complexity of U.S. tax preparation makes it very difficult for me to do this on my own. Meanwhile IRS officers are wasting their time reviewing forms for people who don’t actually owe tax.

The U.S. is one of only two countries in the world that uses citizen-based taxation, the other being Eritrea. I firmly believe one should pay taxes in the country that is protecting you, providing you infrastructure, education, healthcare, fire and police services and of late, vaccines. And that, my dear Senate Committee on Finance, is not the U.S. The burden of being a U.S. citizen abroad is tremendous—many banks don’t want to provide us services and investment opportunities (including company pension plans) are really constrained, given the need to think about both U.S. and UK tax treatment and reporting requirements.

I will share another grave injustice. I spent 6 weeks working from the city of Medellin, Colombia in the summer of 2019. I discovered there is a whole world of digital nomads, U.S. citizens who have jobs that allow them to work remotely. These digital nomads essentially live year-round in Colombia but take breaks in the middle of the year to ensure their Colombian tourist visas can get renewed. They live and work in Colombia, using infrastructure the country provides. And yet they pay ZERO tax to the Colombian government, and continue to pay taxes the U.S. It is morally repugnant that there are Americans living abroad in poor countries in the shadows of the economy without paying anything to the country they live in. And yet they see nothing wrong this because they are hiding behind the U.S. requirements of citizen-based taxation. Is that fair?

It is absolutely true that there are crazy wealthy Americans who live abroad and try to evade taxes. But as the Panama Papers show, people who have that level of wealth have very sophisticated mechanisms to hide their investments in offshore companies and spend just enough time in homes they own around the world to not trigger residential taxation. By all means go after these types who are making their money in the U.S. and evading the IRS. But please don’t forget the needs of ordinary salaried Americans who need justice and equity as well. The UK doesn’t tax Brits living and working in the U.S.—why is it fair the other way around?

My understanding is Senator Warren’s proposed wealth tax could result in (1) taxation of assets earned outside the USA, including assets acquired after having moved from the U.S. and (2) the taxation of our non-U.S. citizen spouses who we share our lives with. Now my British husband’s assets from his job in the education sector may generate a tax burden to the U.S.? This is absolute MADNESS. Imagine the UK wanting to tax assets of the 700,000 Brits who live and work in the U.S.—this is Taxation without Foundation. Or what if the Chinese government sought to tax the assets of property owned by its citizens in the U.S.? There would be outrage by people on this very Committee.

According to the Tax Justice Network’s Financial Secrecy Index, Switzerland is the number one country on the world in term of their secrecy and the scale of their offshore financial activities. Do you know who number two is? The United States of America. Your focus of extraterritorial taxation seems very misdirected when the U.S. is the world’s number two tax haven.

What is a fairer tax system? It’s one that is equitable, that treats working people fairly, that gets its fair share from the super-rich, that ensures corporations earning revenues in the U.S. pay their fair share, that taxes its residents who are benefiting from its infrastructure and services, and that does not burden ordinary Americans abroad. It is time to end citizen-based taxation for individuals and shift to residence-based taxation.

I ask you to please consider the significant impact and perverse outcomes of the reforms you are contemplating on ordinary citizens abroad and think more broadly about what a fairer tax system means for Americans living abroad. Thank you for your consideration.

Sincerely,
Andrea Fernandez

LETTER SUBMITTED BY AARON FISHBONE

May 11, 2021

U.S. Senate
Committee on Finance
Subcommittee on Fiscal Responsibility and Economic Growth

Dear Committee, I moved abroad to be with my wife who is from another country and now we have 2 dual national children. We both work and pay a relatively high tax rate to the government of Slovakia, where we live. I’m not complaining—we pay our share and get good quality and highly affordable medical care, (and many, many other public goods and services) as a result. Notably and importantly, this includes things like paid family leave to raise and care for our children. In Slovakia our wages are adequate, but we live on a budget even here and they are not adequate to pay for additional tax preparation in the USA for the income earned in Slovakia, or for a tax professional who knows both Slovak and American tax law and their convergence, nor for taxes in the US for income we don’t earn there. I now qualify for and file under the foreign earned income exclusion, but in my first two years here it was a mess and I was double taxed as a sole proprietor while I was trying to find my way and get settled, which took a significant portion out of my savings and was very frustrating and dispiriting.

I pay into the tax system here (again, at a high rate as required here) and am eligible for benefits like paid family leave. I should be able to take full advantage of this pro-family, pro-child measure which I have financially contributed to without fear that I might be taxed additionally in the USA for doing so. The money that would be taxed (for no good reason) is money I would want to live on, or, should I have any extra, invest in my children’s 527 plan.

I support the need for the U.S. Government to invest heavily to help us recover from the pandemic, to recover economically, and to invest heavily in the jobs of the future and building cleaner energy infrastructure, and will need to look at tax increases for some tax brackets to pay for this. Nonetheless, I urge the committee to recognize that I and many other Americans overseas are not wealthy, and are trying to live our lives and be with our families, and should not face an onerous, additional tax burden or double taxation for doing so.

Thank you.

Aaron Fishbone

LETTER SUBMITTED BY LELAND GORDON

May 9, 2021

U.S. Senate
Subcommittee on Fiscal Responsibility and Growth

Dear Sir/Madame:

I am an American/Canadian citizen permanently living in Canada. I am required to still file U.S. taxes along with Canadian taxes. I have lived in Winnipeg since 2008. I was a good U.S. resident when I lived in Miamisburg, Ohio and paid U.S. taxes.

The IRS filing process when living abroad is complicated. It is also expensive; typically, $400 a year, as it requires a specialized accountant. The forms are not the same as a typical U.S. tax return. It also wastes IRS resources, as most filers end up not owing U.S. tax.
The U.S. is the only major country in the world that makes its citizens file taxes when living abroad. Every year I get stressed due to the burden of the U.S. filing. I am required to file U.S. taxes for the rest of my life. It is just not fair. This policy is having a significant effect on thousands of citizens permanently living abroad who still absentee vote.

I am requesting the foreign tax filing requirement for U.S. citizens be removed and instead be made residence based. This is an issue that could likely garner bipartisan support.

Sincerely and respectfully,
Leland Gordon

LETTER SUBMITTED BY JEFFREY GUNSCH

U.S. Senate
Committee on Finance
To Whom This May Concern:

I am no longer a proud citizen of the United States of America. I am an angry American citizen living outside the United States. The reasons for why I am angry will be outlined in this letter. I live in Taiwan where I am a tax resident and where I am subject to full taxation already. I am writing today to call attention to the extreme injustice of the U.S. extraterritorial tax regime and how it severely limits the freedom of individual U.S. citizens living outside the United States. This system is very unfair and it’s high time that the extraterritorial tax system be abolished with the goal of “Creating Opportunity Through a Fairer Tax System.”

The only thing that makes me different as an American from U.S. residents is that I live outside the United States. For the record, I did not move from the United States to avoid U.S. taxation! Contrary to public view and even some in government! In fact, I have been sickened that I am subject to (1) taxation in the country where I live and (2) a more punitive form of taxation that what is imposed on U.S. residents. As well as embassy fees for services which my taxes should pay already anyway! My only crime seems to be that I live outside the United States—and therefore my income and assets are foreign to the United States. But, the income and assets are actually local to me.

I am writing to express the Senate Finance Committee continually fails to consider and understand the impact of the proposed tax legislation on me and on Americans living abroad generally both past and present and that we are tired of it. We are average, ordinary, every day people. Do you not want us to be able to retire anywhere and have to go on welfare? We have responsibilities to our families, our communities and our countries of residence and we may need to operate our own small businesses. We are definitely NOT mini multinational corporations and we are tired of being treated as such through our normal day-to-day activities are somehow seen as “offshore” and deserving of punishment. Seriously? Because we have a job, not in the U.S., we are tax cheats? Because we pay taxes to another country’s government, we are tax evaders? When will this rhetoric in the U.S. government stop? We are tax compliant in our countries of residence! We pay a lot of tax! We pay WAY MORE than our fair share. We do this even though it is almost impossible for us to be both tax compliant in our country of residence and be compliant with U.S. tax laws. We don’t understand why U.S. tax laws are being applied in an extraterritorial manner to income and assets that are not in the United States! Other countries don’t tax their citizens who live in the United States? Why should the United States tax U.S. citizens living in other countries?? Please explain? Is it because you think we use some services in the U.S.? Guess what? We do not! If we need service, we also have to pay for that at our embassy! By the way, being we pay U.S. taxes, where are our vaccines? The U.S. government should supply them for ALL U.S. citizens living overseas until you stop taxing us!

Our situation is bad. It is unique. Only the African dictatorship of Eritrea follows the lead of the United States by imposing worldwide taxation on its citizens who live outside the country. But even their system is more fair than what the U.S. inflicts on U.S. Citizens!

I really don’t understand the indifference of the Senate Finance Committee to this situation. Interestingly, the Senate Finance Committee in 2015, recommended
changes to the U.S. extraterritorial tax regimes. There have been no changes for the better, but many changes for the worse.

So far the 2021 Senate Finance Hearings have been very, very bad. The Committee is obsessed with corporations without acknowledging that changes to corporate tax will have a huge effect on individuals. You haven’t mentioned that your obsession with the taxation of corporations, will have a bigger impact on the many, individuals than on the few corporations.

The hearing on April 27, 2021—about a wealth tax—took the treatment of U.S. citizens abroad to a new level. The bottom line is this:

As described Elizabeth Warren’s proposed wealth tax will result in (1) taxation of assets earned outside the USA and (2) the taxation of our non-U.S. citizen spouses who we share our lives with. And to add insult to injury, Senator Warren’s proposed wealth tax would bring assets acquired by U.S. citizens, after having moved from the United States, into the wealth tax system. Come on! My house was acquired after I moved from the United States! Not BEFORE, the U.S. has no right to tax my house in a foreign country paid for by foreign currency, from a foreign job! Which to me is all local!! Local currency! Local job! Local Property! My local business has nothing to do with the United States! Period! My non-U.S. citizen spouse’s assets have nothing to do with United States. Stop asking for them, stop spying on her, stop asking questions! It is none of your business quite frankly! She is not and will never be a U.S. Citizen! Period!

Question: Would the United States like it if China imposed taxes on all property situated in the United States that was owned by Chinese citizens?

If this comes as a surprise to you it’s because you either don’t understand or are conveniently ignoring the U.S. has extraterritorial tax regime—a regime imposed on Americans abroad. All indications are that the Warren wealth will actually leverage the injustice of United States citizenship-based taxation to make the whole world part of its tax base.

It makes me wonder if anyone in the U.S. Government has actually lived and worked and banked post-FATCA outside the U.S. without the comfy situation of being a U.S. Government employee? Because it seems like you totally do not understand and do not want to understand the situation you are forcing us to accept or comply with! Seriously, these predatory, obscene and unjustifiable tax practices must stop. It’s simply not fair and unconstitutional!

In last week’s Senate Finance Committee hearing, one of the witnesses claimed that the U.S. system of extraterritorial taxation “works quite well.” He also stated:

You pay a substantial exit tax under current law by revoking citizenship.

Not many people do it. Some do. If they don’t value the protections and services provided to citizens of the United States then fine. But the protections and services provided to extreme wealth are huge and most ultra-wealthy benefit tremendously from being United States citizens and having those protections and services, and it’s fair to have them pay a reasonable amount of tax on that which they currently are not.

I do not agree with this at all!!!! First it does not work well, this witness fails to understand our situation as stated again and again throughout this letter. Secondly, many citizens are renouncing, but it is not being reported! Or it is being reported because they want to avoid taxes which could not be further from the truth! We overseas Americans are sick and tired of the rhetoric from the U.S. Government, partisan and targeting those who do not live in the U.S. and to appease the voter base! We do not pay a reasonable amount, we pay an extraordinary amount which is unfair! I pay more than 35% of my income in taxes to two different governments on just 30k a year! This is ludicrous!

Secondly this witness claims that we benefit tremendously from being a U.S. citizen, really? Please explain how? I am double taxed, I have no representation in Congress, I am forced to fill out FBAR forms to report foreign account balances which take me a lot of time due to the complexity in forms, local laws, etc., I get no benefits from that taxation, and I am having my bank accounts closed in both the U.S. and where I live overseas, I have been threatened by my banks that I need to comply with U.S. law on foreign soil, that seems like a sanction to me, and I am constantly worried about not being able to retire. So please explain to me what my magic little blue passport entitles me to?
The time has come for the United States to abandon its extraterritorial tax regime and join the rest of the world in adopting a system of residence-based taxation. And get rid of FATCA and just leave us alone!

LETTER SUBMITTED BY NICHOLAS MATTHEW LEE

U.S. Senate
Committee on Finance
Cc: U.S. Representative Madeline Dean (PA 4th District)
U.S. Senator Bob Casey, Jr. (PA)
U.S. Senator Pat Toomey (PA)

Dear Senators,

As an individual, I support efforts to create opportunity through a fairer tax code. I look forward to the hearing next week where these opportunities are presented.

But I worry. Whenever the discussion comes up—that we must close the tax gap. Make people pay their fair share, something usually gets lost. In an effort to create opportunity for America’s middle class, us overseas citizens are almost always treated as collateral damage.

And we too, are part of America’s middle class. We vote. We pay our U.S. taxes. We pay our taxes to the country we live in. But we are constantly treated as not even second class citizens. We are constantly and structurally deprived of opportunities that are already granted to every ordinary working class resident of the U.S.

When you talk about fairness and creating opportunity, please consider all of the opportunities that the U.S. tax code deprives me, 9 million overseas Americans, and our families of:

The Opportunity to Have a Savings Account at a Bank
Because of unintended consequences related to the Foreign Accounts Tax Compliance Act (FATCA), U.S. citizens are treated as a liability by any reputable financial institution outside of the United States.

Even when providing my SSN and full unredacted copies of my tax returns proving compliance with U.S. tax obligations, it is nearly impossible to be accepted for an interest-bearing bank account where I live.

Because banks are so terrified of the possibility that a U.S. citizen becomes a customer while fully compliant on their tax obligations, they simply deny all law abiding U.S. citizens access to financial services out of fear of a few bad eggs.

This is because the banks regard the 30% withholding penalty in cases of non-compliant account holders as a “corporate death penalty”. It’s simply cheaper and safer for them to ban all U.S. citizens from having an account, even if we make every effort to comply with regulations.

The Opportunity to Have Investments in the Country I Live in
I am not a sophisticated investor. The most suitable products for me to own are safe and sane investments like a mutual fund or Exchange Traded Fund (ETF), rather than trying to pick winning stocks.

Unfortunately, because the United States considers all investment funds based outside of the United States to be suspect, I am subject to punitive PFIC reporting and tax rules.

Were I to buy the “VT” Vanguard Total World ETF investment fund from the NYSE–ARCA exchange, I would pay 15% to 20% in capital gains upon selling it. I’d be fully able to deduct or carry forward losses, if they occur.

Were I to buy the “VWRL” Vanguard FTSE All-World UCITS USD ETF investment fund from the NYSE-EuroNext exchange, I’d be subjected to 37% ordinary income tax on unrealized capital gains each year, limited deductibility, and a brutal 37 hour reporting form to be filed each and every year.

These are nearly identical funds, they are tightly regulated in U.S. and EU jurisdictions, but because one fund is from outside of the U.S., I cannot safely invest my money in it.
It's a moot point though. I don't have access to investment brokerage services where I live, because I'm a U.S. citizen.

A North Korean or Cuban customer is perfectly acceptable, and they can invest in a Vanguard fund through a bank here. I as a U.S. citizen cannot. All because of U.S. regulations that uniquely affect U.S. citizens.

**The Opportunity to Have Investments in the Country I am a Citizen of**

The logical conclusion after reading the previous paragraph is to say, "just buy the U.S. fund."

This is not an option for overseas Americans in many jurisdictions.

Because the United States is the only country in the world that subjects its citizens to an extraterritorial tax regime, local financial regulations don’t account for the possibility that someone is either denied access to local financial services or that those services are severely penalized by the tax code of a country they don’t live in.

Within Europe, multiple barriers exist to a U.S. citizen investing in a U.S. bank account. While I don’t live in Germany or Italy, which apply similar punitive rules do discourage investment in offshore locations like the United States, the European MiFID II/PRIIPs regulations prevent EU residents without a high net worth from investing in non-EU investment products.

I suppose if I was rich and could afford the $500,000 minimum assets under management and a 1.0% annual fee, I’d qualify for a specialized investment manager that could put my money in U.S. based funds.

I’m middle class though, so I have to suck it up and stick to a 0% interest checking account.

Because the U.S. tax code penalizes investments outside of the U.S., even by people outside of the U.S., and because I am required to keep my investments in the EU, I am unable to follow good financial practices and invest my money.

**The Opportunity to Start My Own Small Business**

There’s nothing that outright stops me from starting my own business in the country where I live, but the United States sure goes out of its way to make it difficult.

If I wanted to start a business, there are so many barriers that I’d face that citizens of any other country would not:

- I’d be denied business loans, on account of being a U.S. person.
- I’d have difficulty finding a business bank account, on account of being a U.S. person.
- I’d have to set aside a big pile of money for my super complicated 5471 form.
- I’d have to pay GILTI tax, as a “U.S. company” in the Netherlands. Any competitors here wouldn’t, because they’re not American owned.
- I’d possibly have to pay self-employment tax, which no other competitor would need to do.

No other country throws up such barriers to its own citizen starting small businesses in the countries they live in. They’re just happy to see their citizens being successful. In America, only a large multinational is able to do business abroad.

**The Opportunity to Have a Retirement That is Above Subsistence Levels**

In most countries, the U.S. included, it is assumed that individuals will save for their retirement.

Unfortunately, this is also not an option for me, as a U.S. citizen.

Contributing to a Traditional IRA isn’t an option—MiFID II rules mean that most U.S. financial institutions will turn me away, for fear of hurting their compliance in the EU.

Contributing to a Roth IRA isn’t an option—those aren’t recognized as valid account types by most countries, and they’ll be subject to double taxation.

Contributing to a 401k isn’t an option—I don’t have a U.S. employer.

I suppose I could contribute to a Dutch retirement account, subject to rules similar to an IRA, but stricter.

Except it’s not clear that that’d not trigger those horrible PFIC rules. I’m not rich, so I can’t afford tens of thousands of dollars in accounting costs to fill out forms
that were designed to be as complicated and time consuming as possible. Even if I could, accountant fees would eat up any benefit of saving for retirement.

And besides, most financial institutions here want nothing to do with Americans. I’ll just have to settle for whatever the social security system in my current home country would pay out. The Windfall Elimination Provision ensures that even if I did move back to the United States and start working for 35 years, I wouldn’t get a full social security payment.

The Opportunity to Refinance My Mortgage Safely

In many countries, it’s normal to refinance a mortgage every few years. Unfortunately, the U.S. has a concept of “phantom gains” that makes this a very complicated and expensive process.

If I took out a loan for €100,000 today, and I paid it back next year, I’m liable for ordinary income taxation on any savings that resulted from the Euro declining in value.

€100,000 is $118,000 today, but if it’s $100,000 next year because the exchange rate dropped—well, that’s clearly an $18,000 gain, even though that also means my home is worth less, my salary paid in euros is worth less, and I’m no richer despite these “phantom gains” that the U.S. tax code has invented.

If I lived in the U.S., where my mortgage was in U.S. dollars, I wouldn’t need to worry about a change in the exchange rate leading to a massive tax bill on money that I never had.

The Opportunity to Sell My Home at a Loss and Not Be Punitively Taxed

What if there was a housing crisis and I needed to sell my home at a loss? I better hope that the U.S. dollar has stayed strong relative to the Euro.

Suppose that I bought a house this year for €100,000, with an EUR–D exchange rate of $1.18 to the Euro. If the exchange rate is $1.35 5 years from now, I would have a capital gain even if I sold the house for a loss at €90,000.

Only Americans need to pay capital gains tax when selling the house, they live in, in another country. Only Americans need to worry about their capital loss being taxed as a gain.

The Opportunity for a Mortgage Interest Deduction

If I lived in the U.S., I’d be able to deduct the interest I pay on my mortgage from my U.S. taxes.

But because I am a U.S. citizen that does not live in the U.S., the tax code does not permit me to deduct my mortgage interest from the taxes I pay to a country I don’t even live in.

The Opportunity to Marry Freely, Without Fear

At some point, I would like to marry my partner. Unfortunately, doing so would take away so many opportunities from her.

She’d be unable to have a savings account here, because banks fear spouses of U.S. citizens.

She’d be unable to have investments where we live, because brokerages fear people married to a U.S. citizen.

She’d be unable to have investments in the U.S. because she has never lived in the U.S., nor does she have an SSN. Even if she had one, EU rules would prevent that too.

She’d be unable to have a small business, because community property rules would mean that I am a partial owner of her business, and then her & her business partners would have to deal with Controlled Foreign Company issues and GILTI taxes.

She’d be unable to retire, because in the Netherlands, retirement accounts are joint property, and that would then mean we have PFIC problems that would bankrupt us.

So whenever a family member asks, why aren’t you getting married yet, you have to sadly answer “Because I love her, and I can’t do that to her.”

Because only America taxes its overseas citizens in this way.
The Opportunity for My Children to Benefit From the Taxes I Pay
What if we had children? They'd hopefully receive benefits from the 49.5% income tax that I pay here. We happily pay them to ensure a strong social safety net.

Once again though, that global taxation throws a wrench in things. Benefits here like child support benefit, disability benefits, or student study are considered unearned income, subject to taxation by the U.S.

Because some of these are paid to children or individuals with no income, they likely will end up paying U.S. taxes because they have no foreign taxes to offset it—because those are paid at another point in time, when they are in the workforce.

China doesn't tax government benefits of its Dutch residents. Germany doesn't tax government benefits of its Dutch residents. But America is happy to undermine the opportunities the Netherlands (and other foreign lands) have for their residents.

The Opportunity to Feel Safe When Filing My Taxes
As if it wasn't painful enough to be deprived of these opportunities, entirely because the United States insists on being the one weird developed country that taxes nonresident citizens, we haven't even touched on compliance.

It's not subject to legal protections against excessive fines—they're penalties, not fines. Penalties are never excessive.

When a U.S. resident makes an honest, non-willful mistake on their taxes, the IRS determines whether or not to request an amendment and too assess reasonable interest-based penalties.

On most matters involving international forms—the FBAR, the FATCA 8938, the PFIC 8621 forms, we see a far more punitive approach. Non-willful errors are subject to a $10,000 fine, and willful errors are the greater of $100,000 or half of the money in the concerned account. Even if the information reporting error did not lead to a material income reporting error.

Of course, lines between non-willful and willful are blurry, given that the Treasury has sometimes gone as far as considering an insufficient understanding of the tax code to be willful negligence.

Either way, it doesn't matter—the penalties for honest mistakes are remarkably high in comparison to those made by U.S. residents. So, while a resident can trust that a small mistake will not have dire financial consequences, nonresident citizens don't get that.

It's pretty clear what the U.S. Government thinks of us. One of our annual information reporting forms goes to the Treasury's Financial Crimes Enforcement Network.

We're lumped in with criminals simply because we have accounts in the countries we live in.

We don't get the opportunity to rest easy at the end of tax season. We instead get to stay up late, hoping that we did not make one single mistake.

Conclusion
If Congress wishes to look at making a fairer tax system that creates opportunity and benefit for ordinary Americans, it should take a moment to look at the numerous ways in which the tax code discriminates against U.S. citizens that live abroad.

We are subject to a separate, but more punitive tax system than the one that U.S. residents live in.

The opportunities we are deprived of did not stem from nothing—much of this, FATCA, PFIC, GILTI, and all the weirdness around exchange rates stems from a legitimate desire to make sure that the top 0.1% of Americans pay their fair share of taxes.

But it seems that at some point along the way, Congress lost sight of the goal. The U.S. tax code and treasury regulations are stripping away any form of financial opportunity for middle-class citizens that live abroad.

The rich can afford high powered lawyers to work around this. They can freely invest in the U.S. if they live in Europe because of the size of their bank accounts. They are not bothered by the thousands of dollars of tax preparation fees necessary to work with the mess that is foreign taxes, U.S. taxes, the tax treaties, and the forms needed to reconcile all of this.
They will never suffer the pain and humiliation of paying thousands of dollars to complete compliance paperwork that ultimately proves that they rightfully owed nothing that year. If you’re going to invoke terms like “civic duty” and “citizens have obligations”—at least make those duties and obligations benefit the state. I would rather pay the IRS than an accountant.

Please understand that every time you talk about fairness, and about dealing with offshore issues, you are also talking about making life tougher for ordinary Americans that live on other shores.

The 7 to 9 million overseas Americans, an overwhelmingly average folk that closely reflects the population living in the U.S., have been crying out for necessary reform and relief for over a decade now, with no meaningful talk from Congress about improvement.

Please stop taking away the opportunities that are afforded to Americans back home and other residents of the countries we live in.

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**LETTER SUBMITTED BY PAMELA MILLER**

May 11, 2021

U.S. Senate
Committee on Finance
Subcommittee on Fiscal Responsibility and Economic Growth
Dirksen Senate Office Bldg.
Washington, DC 20510–6200

To the Senate Committee on Finance:

Thank you for the opportunity to submit this statement for the record of your recent hearing in the Subcommittee on Fiscal Responsibility and Economic Growth.

Almost 25 years ago, I married a Belgian citizen and moved from Tennessee to Belgium to start our life together in his home country. During the early years of our marriage, we worked, bought a house together, and had two children (BE-U.S. dual citizens). Career opportunities, education opportunities, and home ownership are a few of the reasons we decided to stay in Belgium and raise our family here.

I implore the Subcommittee to listen to the voices of U.S. citizens living abroad when considering any further changes to U.S. tax system. Below are a few of the major impacts FATCA and Citizen based taxation have on my life abroad.

**ISSUES**

- Before FATCA, my banking options were those I could expect in the U.S.—checking/savings/retirement/investment/college savings for the children. After FATCA, my bank, out of fear of the penalties imposed for mistakes in compliance on the reporting requirements, has closed all my accounts save my checking account. I am no longer able to save for my retirement nor attempt to improve my financial standing via investments. I was a financially independent woman but have now become financially dependent upon my husband for our future retirement.

- In a few years, our children will be old enough to join the workforce, marry if they desire, and consider home ownership. **Should our sons decide to continue living abroad, home ownership and retirement savings, savings of any kind, will not be available to them unless they renounce their U.S. citizenship.** Our sons identify as Americans and hope to one day live in the U.S., but they also expect part of their adulthood will be spent living overseas. The potential decision to renounce their U.S. citizenship will not be taken lightly, but already serves as a source of stress and concern for us.

- Annual filing of taxes and FBAR is a financial and psychological burden. Due to the complexities of filing from abroad, I use the services of a specialized tax accountant in spite of the fact that my income has never, in 25 years, exceeded the Foreign Earned Income Exclusion. However, I invest time and money every year to prove that and must comb through bank records to be able to accurately file the FBAR report.

While I understand the original intent of FATCA, I believe the full impact of the legislation on average American citizens living overseas was not fully investigated and the stories of the subsequent reality of financial life of Americans abroad have
not been heard. Repeal of FATCA, or instituting Residence Based taxation like all other countries in the world (save Eritrea), would afford citizens such as myself some relief from our current financial situation. This combined with changes to or the elimination of FBAR reporting would allow us to once again have the financial freedoms our fellow citizens in the U.S. enjoy.

CONCLUSION

I am a proud U.S. citizen and have raised my sons to be the same. Our family lives what would be considered in the U.S. a middle-class life. It pains me to be treated like a tax cheat by my own country for the simple reason that I married and live abroad. Now is your opportunity to rectify the U.S. International tax situation for non-resident Americans and give some relief to your fellow citizens who have been struggling under the burden of FATCA and CBT for more than 10 years.

Sincerely,

Pamela Miller
Voting in Tennessee (9th Congressional District)

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The Honorable Elizabeth Warren
Chair
Subcommittee on Fiscal Responsibility and Economic Growth
219 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Bill Cassidy
Ranking Member
Subcommittee on Fiscal Responsibility and Economic Growth
520 Hart Senate Office Building
Washington, DC 20510

Dear Chair Warren, Ranking Member Cassidy, and Members of the Subcommittee:

On behalf of National Taxpayers Union (NTU), the nation's oldest taxpayer advocacy organization, I wish to submit this statement for your hearing “Creating Opportunity Through a Fairer Tax System.” NTU has advocated for a simpler, fairer, and more growth-oriented tax code for all 51-plus years of our existence, so we welcome your broad focus on reforming and improving the U.S. tax system. However, we are concerned that some of the proposals that may be discussed today—such as a national wealth tax, a minimum tax on corporations’ “book profits,” and a swift and significant increase to the budget of the Internal Revenue Service (IRS) without accompanying reforms—could make the tax code more complex, less fair, and, in turn, stunt economic growth at a fragile point in the country’s recovery from the COVID–19 pandemic.

A National Wealth Tax Would Be Extremely Difficult to Administer, Could Adversely Bias Investment Decisions, and Raises Legal and Constitutional Concerns

My colleagues at NTU and NTU Foundation (NTUF) have written extensively on national wealth tax proposals, both in the abstract and in response to Chair Warren's specific wealth tax proposal. We have raised a number of concerns that your latest proposal falls short of addressing.

The first and perhaps foremost concern is the significant challenges the IRS would face in administering a wealth tax. Experts from across the ideological spectrum have raised legitimate questions over how the IRS would value intangible assets, how the agency would handle valuation appeals, and how those responsible for collecting the wealth tax would tackle tax planning and avoidance measures that reduce a taxpayer's base.

As Lawrence Summers, former Treasury Secretary under President Obama, co-wrote with law and finance professor Natasha Serin in a 2019 Washington Post op-ed:
We suspect that to a great extent [the discrepancy between our estimate for wealth tax revenue and the estimate from economists Emmanuel Saez and Gabriel Zucman] reflects the myriad ways wealthy people avoid paying estate taxes that in some form will be applicable in any actually legislated wealth tax. These include questionable appraisals; valuation discounts for illiquidity and lack of control; establishment of trusts that enable division of assets among family members with substantial founder control; planning devices that give some income to charity while keeping the remainder for the donor and her beneficiaries; tax-advantaged lending schemes; and other complex devices known only to sophisticated investors. Except for reducing a naïve calculation by 15 percent, Saez and Zucman do not seem to take account of these devices.1

Unfortunately, the “Ultra-Millionaire Tax Act of 2021,” as currently written, defers all the work of developing a valuation methodology to the Department of Treasury, and instructs them to finish their work in a mere 12 months. This is an inordinate task to put on regulators in a short amount of time, and lawmakers should instead heed the lessons of multiple European countries that struggle to administer a wealth tax. As one report from National Public Radio (NPR) explained:

In 1990, twelve countries in Europe had a wealth tax. Today, there are only three: Norway, Spain, and Switzerland. According to reports by the OECD and others, there were some clear themes with the policy: it was expensive to administer, it was hard on people with lots of assets but little cash, it distorted saving and investment decisions, it pushed the rich and their money out of the taxing countries—and, perhaps worst of all, it didn’t raise much revenue.2

Indeed, experts at the Organisation for Economic Co-operation and Development (OECD) have found that wealth taxes “[reduce] the amount of capital available, which may in turn affect entrepreneurship and business creation as access to capital is an important determinant of an individual’s propensity to start a business.”3

NTUF’s Andrew Wilford raised additional concerns over the potential impact a wealth tax could have on charitable contributions to private foundations and on market competitiveness (should smaller, start-up companies with reduced access to capital need to sell their businesses more often to larger competitors).4

Wilford also noted the numerous legal or constitutional concerns with the proposed wealth tax as designed in the “Ultra-Millionaire Tax Act”:

The first major legal barrier, not unique to Warren’s specific proposal but pertinent nonetheless, is the Constitutional requirement that “direct taxes” be apportioned equally among the states based on population. Back in 1895, the Supreme Court ruled in Pollock v. Farmers Loan and Trust Company that income taxes violated this Constitutional requirement that direct taxes be equally apportioned. Now, taxpayers are on the hook for income taxes today because the Sixteenth Amendment overrode this decision via the appropriate constitutional process, but it did so specifically for income taxes.

Wealth taxes would still be subject to this constitutional requirement.

. . . Warren’s framework does raise another unique problem, however. The right to exit a country has been recognized as a fundamental human right since the time of the Magna Carta, and was confirmed by the U.N. Universal Declaration of Human Rights in 1948. In the United States, the Su

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preme Court ruled in Kent v. Dulles (1958) that the Fifth Amendment protects the right to exit. For all of the above reasons and more, lawmakers should swiftly and completely abandon wealth tax proposals, which would likely fall well short of even the stated goal of developing a fairer U.S. tax system.


In a viral exchange you had with Dr. Kimberly Clausing at a recent Senate Finance Committee hearing, Chair Warren referred to legitimate provisions of the tax code such as expensing for research and development (R&D) costs, carryforwards for net operating losses (NOLs), and deductions for employee stock compensation as “loopholes and tax shelters.” With respect, we could not disagree more strongly with this assessment.

As Members of the Subcommittee well know, the tax code includes many cost recovery provisions for U.S. businesses, including a variety of tax deductions and credits for business activities that lawmakers have determined are worth incentivizing in the code. In the case of Amazon, the company discussed in this viral exchange, experts have shared in the pages of The Wall Street Journal and at NTUF that Amazon’s delta between taxable profits and so-called “book profits” can be explained by a number of legitimate provisions of the code mentioned above, including R&D incentives and NOLs.

This brings us to your proposal, Chair Warren, to establish a minimum 15 percent tax on companies’ “book income.” As you know, President Biden has adopted this proposal for his “Made in America Tax Plan.”

We have numerous concerns with this proposed tax increase, as we outlined shortly after President Biden introduced the plan:

To use an oversimplified example, a company that experiences a $100 million net operating loss in one year but a $10 million net operating profit over each of the next 10 years may ultimately pay nothing in corporate income tax under current law. Under Biden’s plan, though, not only would that company have $0 in net profit over 11 years but they would pay an additional $15 million in minimum “book income” taxes over that period, reducing their net profits over the 11-year period to below zero.

That oversimplified example only considers a business taking NOL carryforwards. Additional businesses could be punished under a minimum tax on “book income” simply for investing in R&D, or for providing their employees with a competitive level of compensation. Companies with high revenue but low profit margins would see profits further reduced under such a proposal, forcing difficult tradeoffs at those companies that could, in turn, negatively impact job, wage, and economic growth. The Tax Foundation estimated that an earlier version of President Biden’s minimum tax proposal “would reduce long-run economic output by about 0.21 percent in combination with Biden’s other tax proposals” (such as an increase in the corporate tax rate from 21 percent to 28 percent).
For all of the above reasons and more, lawmakers should abandon plans to establish a minimum corporate tax on “book profits.” Doing so could harm America’s leading job creators at a fragile point in the country’s economic recovery from a swift but severe recession.

**A Bloated IRS Budget Will Not Produce a Fairer Tax System Without Accompanying Reforms**

As NTU Foundation’s Andrew Wilford noted in his analysis of the “Ultra-Millionaire Tax Act”:

> Warren’s solution to this problem is to throw money at the IRS and hope they can figure it out. Warren would spend $100 billion over 10 years to “rebuild and strengthen” the IRS—more than eight times the agency’s entire FY 2021 operating budget. Of this amount, 70 percent would be devoted simply to enforcing the wealth tax. Beyond that, there’s little in the way of practical solutions to administrative difficulties Warren’s wealth tax would face.12

Indeed, throwing money at the Internal Revenue Service (IRS) without accompanying reforms could have the opposite effect intended by lawmakers here, making the tax code less fair and less efficient. NTU and NTU Foundation have closely tracked IRS reform efforts for decades, and significant additional work is necessary before lawmakers hand the IRS a proverbial wad of cash that significantly outstrips current funding.

NTU worked closely with the late Rep. John Lewis (D–GA) on IRS reform, who often noted the disproportionate impact tax compliance and enforcement had on small businesses and on communities of color.13 In 2017, NTU President Pete Sepp issued several broad recommendations to then-Secretary of Treasury Steven Mnuchin on how to improve the IRS, including focusing on key areas of complexity and measuring tax compliance burdens more accurately.14 While the IRS has no doubt made progress since then, in part due to the passage of the bipartisan Taxpayer First Act and in part due to the tax simplicity gains made under the Tax Cuts and Jobs Act (TCJA), much work remains to be done on all the recommendations NTU issued 4 years ago.

NTU and NTU Foundation have also expressed regular concern over “shifting positions and ambiguous regulations” from the IRS when it comes to enforcement. For instance, in the one area of conservation easement deductions:

> Despite cross-partisan congressional support for conservation easement deductions, the IRS has engaged in draconian enforcement actions, new rules issued without public input and applying retroactively, and zealous valuation denials against many taxpayers who claim them.15

Needless to say, developing, implementing, and administering a wealth tax regime (or even a minimum corporate tax) would likely be orders of magnitude more difficult than the current conservation easement debacle at the IRS, and significantly increasing the agency’s budget to do so without necessary reform proposals should be a non-starter for lawmakers. While lawmakers and tax policy experts have legitimate concerns about the tax gap that may be addressed by IRS reform and a more efficient allocation of resources, a big budget hike for the IRS is not the solution some lawmakers think it is.

**Alternatives to Building a Fairer Tax System**

To the extent that lawmakers can reduce or eliminate tax provisions that make the code less efficient and/or provide a disproportionate amount of benefits to wealthy households without corresponding economic benefits, NTU believes that several re-
form options could accomplish the stated goals of this hearing without adversely impacting investment decisions or harming economic growth. Possible reform options include, but are not limited to:

- **Repealing the state and local tax (SALT) deduction**, which currently confers nearly 90 percent of benefits to households making six figures or more per year.\(^\text{16}\) This deduction results in more than $20 billion per year in forgone revenue, and incentivizes states and municipalities to raise taxes on their residents and businesses.

- **Limiting the new, generous Child Tax Credit (CTC) and Child and Dependent Care Tax Credit (CDCTC) to households making less than six figures per year.** As NTU has written before, “[i]f the goal of CTC expansion is to reduce child poverty, it is not necessary to direct an extraordinarily generous benefit to six-figure households.”\(^\text{17}\) Congressional Research Service (CRS) estimates from before the American Rescue Plan’s CTC expansion indicate that 40.1 percent of the CTC benefit in 2020 went to households making six figures or more per year, likely totaling tens of billions of dollars in foregone revenue.\(^\text{18}\) The CDCTC is even more regressive, with 73.5 percent of the benefit in 2020 going to households making six figures or more per year.\(^\text{19}\)

- **Limiting the current-law electric vehicle (EV) credit, or future expansions and extensions of the EV credit, to households making less than six figures per year:** CRS estimates that “[i]n 2018, more than half of the plug-in vehicle credits were claimed on tax returns with adjusted gross income (AGI) of $200,000 or more.”\(^\text{20}\) This is a regressive credit that should be pared back, notwithstanding a push from the Biden administration and some lawmakers to make the EV credit more generous.

- **Repealing or rolling back tax credits that serve as subsidies for narrow, parochial, or temporal interests:** As former NTU Foundation Vice President Nicole Kaeding put it in 2019, some of the provisions regularly considered as so-called tax extenders “are not ideal.” Kaeding went on: “Many of the extenders involve subsidies for energy projects, such as credits for biofuel, biodiesel, and electric vehicles. These industries should not be penalized by the U.S. tax code, but they shouldn’t get a leg up either.”\(^\text{21}\) To sum up: not all extenders are created equal, nor are all credits, deductions, and expensing provisions in the tax code made equal.

**Conclusion**

We appreciate your attention to and consideration of NTU’s views and positions on a proposed wealth tax, a corporate minimum tax, IRS reform and enforcement, and a number of additional issues addressed in this submission. To the extent you and your colleagues agree with our ideas of how to (and how to not) make the tax code simpler, fairer, and more oriented to economic growth, we would be pleased to answer any questions you may have and to work with you further.

Sincerely,

Andrew Lautz, Director of Federal Policy

CC: The Honorable Ron Wyden, Chair, Senate Committee on Finance
   The Honorable Mike Crapo, Ranking Member, Senate Committee on Finance
   The Honorable Richard Burr, Member, Subcommittee on Fiscal Responsibility and Economic Growth


\(^\text{18}\) Ibid, page 788.

\(^\text{19}\) Ibid, page 174.

\(^\text{20}\) Ibid, page 835.

LETTER SUBMITTED BY KARL STEINKE

Submission on behalf of Stop Extraterritorial American Taxation (SEAT)

U.S. Senate
Committee on Finance

To Whom This May Concern:

I am a citizen of the United States. I have been living outside of the United States since 1995. I am writing today to call attention to the extreme injustice of the U.S. extraterritorial tax regime and how it severely limits the freedom of individual U.S. citizens living outside the United States. This system is very unfair and it’s high time that the extraterritorial tax system be abolished with the goal of “Creating Opportunity Through a Fairer Tax System.”

The only thing that makes me different as an American from U.S. residents is that I live outside the United States. For the record, I did not move from the United States to avoid U.S. taxation. In fact, I have discovered that by living outside the United States I am subject to (1) taxation in the country where I live and (2) a more punitive form of taxation that what is imposed on U.S. residents. My only crime seems to be that I live outside the United States—and therefore my income and assets are foreign to the United States. But, the income and assets are actually local to me.

I am writing to express my great concern about the failure of the Senate Finance Committee to consider the impact of proposed tax legislation on me and on Americans living abroad generally. We are average, ordinary, every day people. Because we are flesh and blood humans, we need to eat. Because we will get old and retire we need to save for retirement. Because we are individuals with responsibilities to our families, our communities and our countries of residence we may need to operate our own small businesses. We are definitely NOT mini multinational corporations and we are tired of being treated as though our normal day-to-day activities are somehow “offshore” and deserving of punishment. We are tax compliant in our countries of residence. I am tax compliant in the U.S. as well.

We pay a lot of tax. We pay our fair share. We do this even though it is almost impossible for us to be both tax compliant in our country of residence and be compliant with U.S. tax laws. We don’t understand why U.S. tax laws are being applied in an extraterritorial manner to income and assets that are not in the United States. Other countries don’t their citizens who live in the United States? Why should the United States tax U.S. citizens living in other countries.

Our situation is bad. It is unique. Only the African dictatorship of Eritrea—follows the lead of the United States—by imposing worldwide taxation on its citizens who live outside the country.

I really don’t understand the indifference of the Senate Finance Committee to this situation. Interestingly, the Senate Finance Committee in 2015, recommended changes to the U.S. extraterritorial tax regimes. There have been no changes for the better, but many changes for the worse.

So far the 2021 Senate Finance Hearings have been very, very bad. The Committee is obsessed with corporations without acknowledging that changes to corporate tax will have a huge effect on individuals. You haven’t mentioned that your obsession with the taxation of corporations, will have a bigger impact on the many individuals than on the few corporations.

The hearing on April 27, 2021—about a wealth tax—took the treatment of U.S. citizens abroad to a new level. The bottom line is this:

As described Elizabeth Warren’s proposed wealth tax will result in (1) taxation of assets earned outside the USA and (2) the taxation of our non-U.S. citizen spouses who we share our lives with.

And to add insult to injury, Senator Warren’s proposed wealth tax would bring assets acquired by U.S. citizens, after having moved from the United States, into the wealth tax system. Come on! My house was acquired after I moved from the United States. My local business has nothing to do with the United States. My non-U.S. citizen spouse’s assets have nothing to do with United States.

Question: Would the United States like it if China imposed taxes on all property situated in the United States that was owned by Chinese citizens?
If this comes as a surprise to you it’s because you either don’t understand or are conveniently ignoring the U.S. has extraterritorial tax regime—a regime imposed on Americans abroad. All indications are that the Warren wealth will actually leverage the injustice of United States citizenship-based taxation to make the whole world part of its tax base.

Seriously, these predatory, obscene and unjustifiable tax practices must stop. It’s simply not fair!

Thank you,
Karl Steinke

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7 May 2021

Please accept this as our submission with respect to the subject of the April 27, 2021 Senate Finance Committee Hearing: “Creating Opportunity Through a Fairer Tax System.”

Previous hearings have focused on large corporations and high net worth individuals. The hearing on April 27, 2021 focused on a wealth tax. No hearing has recognized the impact of the proposals on U.S. citizens living outside the United States who are tax residents of countries outside the United States. It is important for Congress to understand that any change in the U.S. tax system that does not remove the current citizenship-based extraterritorial tax regime will exacerbate the problems facing U.S. emigrants and the small businesses they run in their countries of residence. In this hearing, the problems created by extraterritorial taxation were not only ignored, but one witness held up the citizenship-based extraterritorial tax regime as the reason why a wealth tax would work for the U.S. when it has failed in so many other countries.

In our submission, we remind the committee of the problems created by the extraterritorial tax system and discuss the implications of using citizenship-based taxation as an enforcement tool for a wealth tax on ordinary Americans living outside of the U.S.

Part A: Context
The Internal Revenue Code establishes three distinct U.S. tax regimes:

1. **Non-resident Alien Tax Regime**: Taxation on U.S. source income only
2. **Tax Regime For U.S. Residents**: Taxation of U.S. residents on worldwide income (regardless of citizenship).
3. **Extraterritorial Tax Regime**: Taxation of the worldwide income, mostly non-U.S. source income of individuals who are U.S. citizens, who do not live in the United States and are tax residents of other countries. This is a separate and more punitive tax regime than that imposed on U.S. citizens living outside the United States. To put it simply: The extraterritorial tax regime is based on citizenship regardless of economic or physical connection to the United States. Some—including the Committee witness Professor Gamage—refer to the extraterritorial tax regime as “citizenship-based taxation.”

The extraterritorial tax regime applies to the non-U.S. source income of U.S. citizens (and Green Card holders) who live outside the United States and are tax residents of other countries. For example a U.S. citizen Yoga teacher living in France who is paid in France is subject to U.S. taxation on that French income. The extraterritorial tax regime is a more punitive and more penalty-laden regime than the tax regime imposed on U.S. residents. This is the direct result of the income and assets of Americans abroad being (although local to the individual), foreign to the United States.

Indeed, the Senate Finance Committee recognized the problem of the extraterritorial tax regime, at least as early as 2015. That is when the Senate Finance

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Committee Bipartisan Tax Working Group on International Tax concluded their report with the following paragraphs:

According to working group submissions, there are currently 7.6 million American citizens living outside of the United States. Of the 347 submissions made to the international working group, nearly three-quarters dealt with the international taxation of individuals, mainly focusing on citizenship-based taxation, the Foreign Account Tax Compliance Act (FATCA), and the Report of Foreign Bank and Financial Accounts (FBAR).

While the co-chairs were not able to produce a comprehensive plan to overhaul the taxation of individual Americans living overseas within the time-constraints placed on the working group, the co-chairs urge the Chairman and Ranking Member to carefully consider the concerns articulated in the submissions moving forward.

In other words, in 2015 the Senate Finance Committee recommended that the negative effects of the extraterritorial tax regime be specifically considered.

Six years have passed and there is still no movement on overhauling the taxation of individual U.S. citizens living overseas, in spite of the clear directive from the International Tax Working Group. In fact, the situation for U.S. citizens abroad has gotten far worse. This is due in large part to the enhancements to the Subpart F regime in TCJA. We informed the Senate Finance Committee in that regard in our submission dated April 22, 2021, available here.

The Senate Finance Committee Must Consider Its Laws from The Perspective of Both:

A. The tax regime imposed on U.S. residents; and
B. The extraterritorial tax regime imposed on U.S. citizens living outside the United States.

SEAT is unaware of a single instance in which the Senate Finance Committee has considered how proposed legislation affects U.S. citizens abroad—who are subject to the U.S. extraterritorial tax regime.

SEAT respectfully submits that because the United States is operating an extraterritorial tax regime which applies uniquely to U.S. citizens abroad, the Senate Finance Committee has an obligation to follow the 2015 directive of the Senate Finance Committee and consider the impact of tax changes on U.S. citizens abroad, who are by definition subject to the extraterritorial tax regime.

The Scope of the 2021 Senate Finance Committee Hearings—No Consideration of Individuals

Since March 2021 the Senate Finance Committee has been considering changes to the workings of the U.S. tax system. For the most part the hearings have discussed tax changes to U.S. corporations. Neither the Committee itself, nor a single witness has mentioned or considered the profound implications of the proposed changes to corporate taxation, on the millions of individual U.S. citizens living in the United States or living abroad. Yet, as we have described in previous submissions, the proposed changes to corporate tax will impact far more individual U.S. citizens abroad than U.S. multinationals. This follows from the fact that when a U.S. citizen runs a small business using the business structures common in their non-U.S. country of residence they are often treated as a U.S. Shareholder of a Foreign Corporation, and are therefore subject to the same Subpart F rules that apply to multinational corporations headquartered in the U.S.

Part B: Implications of a Wealth Tax for U.S. Citizens Living Abroad

The title to this hearing bears little relation to what the hearing was actually about. The hearing was for the purpose of introducing Senator Warren’s proposed wealth tax. Hence, our remarks in this submission, will be restricted to the question of a
Wealth Tax and its implications for the millions of individual U.S. citizens living abroad, who are subject to the extraterritorial (citizenship) tax regime.

About the Wealth Tax in General—Senator Warren in her own words: excerpts from a recent CNBC interview . . .

WARREN. Based on fact, the wealthiest in this country are paying less in taxes than everyone else. Asking them to step up and pay a little more and you're telling me that they would forfeit their American citizenship, or they had to do that and I'm just calling her bluff on that. I'm sorry that's not going to happen.

WARREN. Look, they want to use American workers. They want to use American highways. They want to use American police forces. They want to use American infrastructure, but they just don't want to help pay to support it. And that's the trick, a wealth tax needs to be national because you can still get advantages, if you move from state to state. But the idea behind wealth tax is you have to pay it if you're an American citizen. It doesn't matter whether you live in Texas or California or even you move to Europe or South America. If you want to keep your American citizenship, you pay the wealth tax and it doesn't matter where you put your assets. You can try to hide them in the Cayman Islands, you can try to put them up in Switzerland, but it doesn't matter, you still pay the two-cent wealth tax. And here's the nice thing about that, you know, a lot of the wealth is quite visible and easy to see, it's right there in the stock market. A two-cent wealth tax changes this country fundamentally because it means we say as a nation, we are going to invest in the next generation. We're going to invest in creating opportunity not just for a handful at the top, we're going to create opportunity for all of our kids.

That's how we build a strong future in this country.

Senator Warren's own words confirm that the effectiveness of her proposed wealth tax is dependent on the application of the U.S. extraterritorial (citizenship-based) tax regime which is imposed on U.S. citizens abroad.

SEAT would like to raise three issues about this proposed wealth tax: first the measurement of the dollar threshold over which the tax applies, second, how the tax base is computed, and third, the potential impact of the proposed enforcement methods.

Wealth Tax Threshold

On or about March 1, 2021, Senator Warren introduced her proposed “Ultra-Millionaire Tax Act of 2021”. The threshold for the tax is $50 million USD. There is nothing in the proposed act that suggests this threshold is indexed to inflation. Even if the threshold is NOT lowered (which it will most certainly be), the inevitability of inflation will ensure that more and more people are ensnared by it. In the same way that the late Senator Kennedy referred to the 877A Exit Tax as the billionaire’s tax (when it applied to everyday people), over time, the wealth tax will become the millionaires’ tax that will be applied to (by the standards of today) thousandaires.

Furthermore, the threshold is measured in U.S. Dollars. This is fair enough for individuals whose wealth and income are tied to the U.S. economy. However, for U.S. citizens whose economic life is exercised entirely outside of the U.S., the requirement that all U.S. tax computations be made as if they ran their lives and businesses in U.S. Dollars creates currency risk for individuals whose financial life actually runs in a single currency.

What is included in the tax base?

Senator Warren’s wealth tax would apply to the non-U.S. assets (among other things) of U.S. citizens living in other countries. U.S. citizens include: 1. American Expatriates (living abroad temporarily) 2. American Emigrants (living permanently outside the United States) 3. Accidental Americans (possibly never having lived in the United States). This would include assets that are part of the economies of other
sovereign nations and that were accumulated after the individual emigrated from the U.S.; that is, the tax base includes assets that have no economic connection to the United States.

Furthermore, it is drafted in a way that the assets of the non-U.S. citizen spouse may be part of the calculation!

Therefore: To impose the wealth tax on U.S. citizens abroad is to impose the wealth tax on (1) tax residents of other countries and (2) on assets in other countries which may not necessarily be owned by U.S. Citizens.

As explained by U.S. tax lawyer Virginia La Torre Jeker,9 the proposed wealth tax applies to anybody in the world. Nonresidents (however they may be defined) would be assessed a wealth tax based only on their U.S. assets. A podcast with Virginia La Torre Jeker about the impact of the wealth tax on U.S. citizens living abroad is available at this link.10

Using the Extraterritorial Tax Regime as an Enforcement Tool for a Wealth Tax

Professor David Gamage confirms that the extraterritorial tax regime, which the 2015 Senate Finance Committee recommended should be reconsidered, is the tool used to enforce the proposed wealth tax!

What follows is a transcript of part of Professor Gamage's testimony at the April 27, 2021 hearing:

1:15:10—Second exchange between Senator Cassidy and David Gamage

CASSIDY. Do you favor a worldwide wealth tax because that doesn’t seem practical to me but that seems like people can move and they do. And capital can move and it does. One example for example: I understand that China has an incredible capital flight and if there’s any country that’s done its best to surveille everything about every one of its citizens it’s China and yet they have significant capital flight. So, would you recommend a global wealth tax?

GAMAGE. The United States tax system—the current income tax is citizenship-based and taxes all worldwide income for citizens and always has. This is a key difference between the U.S. tax system and the French tax system. You can’t escape the U.S. taxation without revoking your citizenship and paying a substantial exit tax. That’s current law and it works quite well.

CASSIDY. And so the idea that somebody would give up their citizenship—I think one of the partners that made a lot of money from selling—some big Silicon Valley going public, renounced his citizenship and moved to Singapore, if I remember correctly. I’m gathering from you you feel as if that problem would be minimal.

GAMAGE. It historically has been minimal and you pay a big exit tax. . . .

CASSIDY. Historically we haven’t had a wealth tax so I’m not sure we can use past history to predict future actions to kind of paraphrase the financial commercial.

GAMAGE. Again, you pay a substantial exit tax under current law by revoking citizenship. Not many people do it. Some do. If they don’t value the protections and services provided to citizens of the United States then fine. But the protections and services provided to extreme wealth are huge and most ultra-wealthy benefit tremendously from being United States citizens and having those protections and services, and it’s fair to have them pay a reasonable amount of tax on that which they currently are not.

It’s not clear what part(s) of the current extraterritorial tax system Professor Gamage thinks work “quite well”, but from the perspective of Americans actually living outside of the U.S., the system is inherently dysfunctional. Numerous surveys11 have been conducted which provide ample evidence that the U.S. tax laws

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9 https://us-tax.org/2021/03/11/what-does-senator-warrens-proposed-wealth-tax-mean-for-you/
Recently-released survey report dispels myth of the wealthy American abroad and demonstrates why middle-class Americans abroad are forced to renounce US citizenship.


This profoundly ignorant comment from Senator Baucus, alongside many others expressed by other members of the United States Congress dating back to the Civil War right up to today,13 expose longstanding and deep-seated prejudices against Americans who live outside the United States. Is it any wonder that these prejudices have been translated into extraterritorial taxation and banking policies that are highly damaging to Americans and green card holders living outside the United States? It appears that Senator Warren’s wealth tax is premised on many of the same profoundly ignorant assumptions about U.S. citizens living outside the United States.

Part D: The Solution: Ending the U.S. Extraterritorial AKA Citizenship-Based Tax Regime

The best solution to this problem is for the United States to come into alignment with every other developed nation on the planet and move to a residence-based taxation system for individuals. Taxing non-resident citizens is “Mission Impossible,” as it is impossible to fairly administer an extraterritorial tax system and afford non-resident U.S. citizens the rights guaranteed by the Taxpayer Bill of Rights (IRC § 7803(a)(3)), by multiple human rights instruments and by the U.S. Constitution.14

It is well past the time that the Senate Finance Committee act upon the call of the 2015 Senate Finance Committee Bipartisan Tax Working Group on International Tax, and finally accord to Americans living outside the United States the full attention, concern, and respect to which they are entitled as U.S. citizens. It is also well past time to put an end to the taxation and banking policies that penalize them so severely.

Thank you for your attention to these matters.

Respectfully submitted by:
Dr. Laura Snyder (President)
Dr. Karen Alpert
Suzanne Herman
David Johnstone
Keith Redmond
John Richardson

About SEAT—Education to Facilitate Change

Stop Extraterritorial American Taxation (SEAT) is an independent, nonpartisan organization with no affiliation with the tax compliance industry. The mission of SEAT is to provide an educational platform for individuals, policymakers, governments, academics, and professionals about the terrible effects of U.S. extraterritorial taxation. The imposition of U.S. taxation on the residents of other countries damages the lives of the affected individuals and siphons capital from the economies of other nations while eroding their sovereignty.

While SEAT is created under the laws of France (Law of 1901), it is an international organization. http://www.seatnow.org.

LETTER SUBMITTED BY JUAN VALDEZ

U.S. Senate
Committee on Finance

I am a proud American citizen who lives outside the United States. To be clear: I am an individual. I am not a corporation. I am not a multinational. I did not move from the United States to avoid paying U.S. taxes. But, by moving from the United States, I am automatically subject to the U.S. Extraterritorial tax regime—a regime that imposes more punitive taxation and reporting on Americans living abroad—than is imposed on American residents. This is because the Internal Revenue Code treats all things foreign to the United States punitively.

I moved from the United States because wanting to experience new cultures. In fact, I am a full tax resident the country where I live. But, because I actually live and work in New Zealand I am required to pay taxes and assume responsibility for my financial and retirement planning here, where I live. My income, financial and retirement assets are foreign to the United States, but are local to me. Because my income and financial assets, although local to me, are foreign to the United States I am subject to the U.S. Extraterritorial tax regime. As such, I am subject to constant stress and fear of penalties should I make mistakes in complying with the Internal Revenue Code. Furthermore, I find it very difficult to find competent professional help. The help I can find is very expensive (often costing more than $1500 a year).

I know that you will find it difficult to relate to this. However, because and only because, I live outside the United States, my difficulties include the following:

- Difficulty in maintaining bank/financial accounts where I live
- FATCA has provided incentives for banks in my country to refuse to deal with U.S. citizens
- Punitive Taxation on non-U.S. mutual funds
- Being able to participate in non-U.S. pensions and still get the benefits of tax deferral available to my neighbors
- Taxation on the sale of my principal residence which is not taxed in the country where I live
- Difficulty in carrying on a business. It is normal for people in my country to carry on business through small business corporations—which are taxed punitively by the IRS (GILTI)
- Having the retirement savings in my corporation effectively confiscated by the 965 Transition Tax
- Being subject to income based on phantom capital gains. (Because I required to live my life tethered to the U.S. dollar, fluctuations in the exchange rate can result in unexpected fake income)

To be clear, I am and will always be a proud American. But I find it very difficult to maintain compliance with both the U.S. Internal Revenue Code and the tax code of my country of residence. Because of this dual tax obligation, I am finding it very difficult to save and invest for retirement. What one country gives, the other country takes. The necessity of complying with both tax regimes means that I get the worst of each tax regime. As a result, I feel that I am being forced to consider whether it is possible to retain my U.S. citizenship. No proud American should be forced to choose between his cherished U.S. citizenship and the need to engage in responsible financial/retirement planning.

It is terribly unfair, that because I live outside the United States, that I am forced to choose between my responsibilities to plan for retirement and my responsibilities under the Internal Revenue Code. Why should I be subject to additional require-
ments that resident Americans are not? I am not living in the United States and using services in the United States. I have even been denied a COVID–19 vaccine from the U.S. Government (because I don’t live in the United States) while being required to pay taxes to the United States!

The U.S. Extraterritorial tax system is terribly unfair.

A great American writer, the late Pat Conroy, began his book “The Prince of Tides” with the words:

“My wound is geography. It is also my anchorage, my port of call.”

Although, my U.S. citizenship is my anchorage and my port of call. The unfair U.S. extraterritorial tax regime—triggered by my geography”—is most definitely my wound.

Please fix this extreme injustice!

LETTER SUBMITTED BY DOMINIK VAN OPDENBOSCH

I would like to comment on the hearing on “Creating Opportunity Through a Fairer Tax System”. Within his testimony, Mr. David Gamage stated that citizenship-based taxation “works quite well”. I strongly object to this statement.

Please understand that all legislative actions with regards to taxes for residents inside the U.S. have also impacts on residents outside the U.S. and often enough the impacts are not considered and reflected enough in the legislative process.

As an example: I wanted to volunteer here for a local non-profit charity organization as treasurer. I could not do that because of FBAR and FACTA requirements this would mean that the bank account details of the non-profit had to be sent to the U.S. As a citizen of the EU, I am also obliged to follow GDPR rules and make sure that no personal data and financial data are collected and shared. Finally, I decided not to volunteer. The same holds for promotions inside a company, where at some point you might get filing authority over a bank account. FACTA also results in bank accounts being closed as European banks fear the draconian penalties of not complying.

More generally, the U.S. extraterritorial tax regime makes it difficult for us to save, invest, participate in pension plans, and generally behave in a financially responsible way. This is because all of these essential activities are taking place in my country of residence and not in the United States. My retirement investments are foreign to the United States but local to me. The tax systems are usually mutually incompatible.

There is no assistance from the IRS on how to translate specifics of foreign taxes into the U.S. tax code. That usually requires hiring costly ex-pat tax advisors even for very simple tax filings. If there is a global tax system, I would expect some assistance in my native language and with a local office, I can visit or call to help me with details.

And please don’t believe that foreign tax rules and/or the Foreign Earned Income Exclusion solve these problems. They don’t! Take PFIC as an example: I followed my local (from a U.S. perspective foreign) investment advisor and bought some ETFs from the money I earned solely overseas, I later found that they are subject to double taxation. As a tax resident of both the United States and my country of residence, I get the worst of both tax systems. If you want to open a business here you pay local taxes and GILTI taxes. This puts you into a considerable disadvantage compared to non-U.S. citizens.

This is extremely unjust. For many years, Americans abroad feel like second-class citizens and have been attempting to get both Treasury and Congress to address these issues.

It is not about rich people trying to evade taxes. It is about the average American that happens to live outside the U.S. We can not afford expensive lawyers that optimize our financial situations. We are stuck with two tax systems. Don’t think that the U.S. tax system for ex-pats is the same as for U.S. residents. It is much more complex and underestimated by lawmakers. I would encourage you to invite actual ex-pats into the senate hearings to have first-hand witnesses of the complexity and Kafkaesque situation. It is time to change to residency-based taxation.
I hope you find this statement valuable. I believe it helps to understand and address the issues of million of American workers around the world.

LETTER SUBMITTED BY GENELLE WINDSOR

U.S. citizens who live outside of the U.S. are residents of other countries and pay taxes in those countries. This is called RBT (residency-based taxation). The United States has CBT (citizen-based taxation). Besides Eritrea, the United States is the only country in the world to have CBT. The United States should eliminate CBT and convert to RBT to be fairer to the U.S. citizens who do not live in the United States.

The current hearing in the Senate Finance committee is researching how taxes can be fairer. In past discussions, the bills before the Senate to change the taxation of U.S. citizens living outside of the United States had to be “revenue neutral”. This means, that if the law is changed, the United States does not want to lose any tax revenue. The previous proposed solution was to tax U.S. sourced income such as interest in U.S. banks, U.S. social security and capital gains in the U.S. at a flat 30%.

With the current law (CBT), a U.S. citizen living outside of the United States first pays tax in the country where she lives, then declares worldwide income on the U.S. tax return and can pay taxes in the U.S. as well, depending on the income amount. If a choice between CBT and RBT is available to U.S. citizens living outside of the U.S., a U.S. citizen can opt for RBT for all of the income earned or accrued outside of the United States. Then any income in the United States would be taxed at 30%. So, if a U.S. citizen living outside of the United States is dependent on U.S. social security, adopting RBT would significantly reduce those social security benefits by the 30% tax. Few people living outside of the United States could afford to opt for RBT in this case. These people would have to continue with the CBT option or face financial hardships. As you can see with this example, the U.S. citizens living outside of the United States with the least income (social security) would bear the brunt of “revenue neutrality”. These U.S. citizens would have to remain with the unfair CBT rule and continue paying very expensive tax accounts to do their U.S. taxes. The tax accountants can charge between $1,100.00 and $3,000.00 to do a tax return for one year. This is still less than a tax of 30% on the social security income.

If the option of RBT or CBT is available when filling out a U.S. tax return, the less well off people will still be paying more taxes while the people with more money will pay less.

Most countries who practice RBT tax residents only (not citizens). For example, if a person has revenue in two countries, he pays taxes in the country where he resides, not in the country where the revenue is generated. If a person earns income in the United Kingdom and France, all of that income is taxed in the United Kingdom if the person lives in the United Kingdom and in France if the person lives in France. Taxes are paid for services. If you pay taxes in a country where you do not reside, you do not get the services because the services are residency based. Medicare is an example of this. U.S. citizens must reside in the United States to receive Medicare benefits.

Tax treaties have been written with the United States with many countries. This tells you that at least the United States realizes that U.S. citizens should not be taxed twice on the same income. If the U.S. citizen uses the tax treaty, he may end up paying no tax. So, regarding revenue neutrality, tax treaties have to be written, tax returns have to be processed, and IRS staff have to be trained on how to deal with tax returns from U.S. citizens who do not live in the United States. This is an extra cost to process tax returns where the tax payer may not owe anything. If RBT were adopted, the IRS would save this money. Please take this into consideration when you are calculating revenue neutrality. RBT could actually be revenue neutral.

CBT is an unjust system and causes great anguish to the U.S. citizens living abroad who are trying to be tax compliant. Abolishing an unjust system should not be dependent on revenue.
LETTER SUBMITTED BY LIBIN ZHANG

The following was published in 171 Tax Notes Federal 87 (April 5, 2021).

A Wealth Tax on Ultra-Millionaire Charitable Trusts and Marriages

In a recent article,1 Marie Sapirie discussed some key aspects of the Ultra-Millionaire Tax Act of 2021 (S. 510), a bill proposed by Senate Finance Committee member and former Presidential candidate Elizabeth Warren, D-Mass. If enacted, the law would generally impose an annual 2 percent wealth tax on the net value of a taxpayer’s total assets above $50 million and below $1 billion, and an annual 3 percent or 6 percent tax on the net value of a taxpayer’s assets in excess of $1 billion.

Two additional observations are worth noting.

First, a “taxpayer” subject to the wealth tax is an individual, a married couple, or a trust other than a trust described in section 401(a) and section 501(a). A trust that is exempt only under section 501(a) can still be subject to the wealth tax. In other words, tax-exempt pension trusts are exempt from the wealth tax, but charitable trusts are subject to the wealth tax if they have more than $50 million of assets.

It is unclear why charitable lead trusts, charitable remainder trusts, and other tax-exempt trusts with charitable purposes are targeted as ultra-millionaires that should pay the tax. The annual wealth tax would have a significant adverse effect on the non-profit organizations that are beneficiaries of charitable trusts or are themselves organized as trusts in legal form. Proponents of the bill may not fully appreciate the different types of trusts under the tax code.

Second, the same thresholds of $50 million and $1 billion of assets apply to a single individual or a married couple (whether filing jointly or separately). Two single individuals effectively lose half of their combined exemptions if they are married.

For example, let’s assume there are two individuals with the hypothetical names of “A-Rod” and “J-Lo,” who work in the sports and entertainment industries, respectively. A-Rod has $700 million of assets under the government’s valuation method, consisting of half real estate and other investments and half intangible assets such as his ability to generate endorsement income that is valued using the discounted cash flow method. Similarly, J-Lo used to have little but now has $700 million of assets under the wealth tax regime, based on a valuation of her Louboutins and other designer outfits, rocks, and rights to royalty income from movies, English and Spanish language music albums, and reality TV shows.2

If A-Rod and J-Lo were married, they would have $1.4 billion of combined assets. The assets below the $50 million floor would be exempt. The next $950 million of assets would be subject to a 2 percent wealth tax of $19 million per year. The remaining $400 million of assets would be subject to a wealth tax of up to 6 percent, or $24 million per year. The married couple’s annual wealth tax liability would be $43 million each year.

In contrast, if A-Rod and J-Lo were not married and did a multi-year engagement instead, each person would have $50 million of exempt assets and $650 million of assets subject to a 2 percent wealth tax of $13 million each year. The two single individuals would collectively pay $26 million each year and therefore save $17 million or 40 percent of their annually wealth tax bill, achieved by wisely postponing marriage.

There are similar marriage penalties in the $10,000 SALT deduction limitation and the home mortgage interest deduction limitation that are the same for a single

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2 For examples of how the Internal Revenue Service may value celebrity likeness and music rights, see Ben Sisario, “I.R.S. Says Prince’s Estate Worth Twice What Administrators Reported,” The New York Times, January 4, 2021; Jeff Gottlieb, “Michael Jackson Estate Embroiled in Tax Fight with IRS,” Los Angeles Times, February 7, 2014 (“Most of the dispute is over the value of Jackson’s image, along with his interest in a trust that includes the rights to some of his songs and most of the Beatles catalog, including ‘Yesterday,’ ‘Sgt. Pepper’s Lonely Hearts Club Band’ and ‘Get Back.’ The estate valued Jackson’s likeness at just $2,105. The IRS put it at $434,264 million.”)
individual or a married couple, but the social engineering in the wealth tax bill against marriage involves more substantial dollars. Although some may claim that love does not cost a thing and that marriage may have nontax benefits, the annual wealth tax can cost up to 6 percent of one's tangible and intangible assets each year. Celebrities and other high income individuals waiting for a wealth tax may be less likely to marry a fellow wealthy person from the block.

Sincerely,
Libin Zhang
March 27, 2021

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