



## Written Testimony for Hearing, “Examining How the Tax Code Affects High-Income Individuals and Tax Planning Strategies”

Chye-Ching Huang  
Executive Director of the Tax Law Center at NYU Law  
The United States Senate Committee on Finance  
November 9, 2023

Chairman Wyden, Ranking Member Crapo, and distinguished members of the Committee, thank you for the opportunity to testify.<sup>1</sup> I am the Executive Director of the Tax Law Center at NYU Law, a public interest initiative that seeks to improve the integrity of the tax system. The Center is staffed by tax lawyers with expertise in tax administration, private practice, and the tax legislative process, and our work draws on extensive networks of public interest minded tax practitioners and experts.

### SUMMARY

The highest-income households get the bulk of their income from their wealth. The nation spends hundreds of billions of dollars each year to maintain tax preferences that allow income from wealth to face less tax than equivalent income from work.

Tax subsidies for income from wealth add to deficits by narrowing and weakening the federal tax base. Tax breaks like these are sometimes called “tax expenditures,” or “spending through the tax code” because their impact on the budget and the economy is like a spending program designed to subsidize a specific activity.

Tax subsidies for income from wealth are a poor investment. They increase deficits, widen inequality, and spur complex tax avoidance and evasion that locks up capital and talent that could be used for more productive work and innovations. This is a misallocation of both public and private resources. Tax evasion by the very wealthy can often involve the proceeds of other criminal acts such as sanctions evasion and corruption, which undermines the rule of law.

Federal resources can instead be directed towards investments that better meet the nation’s most pressing challenges. That could include investing in workers and families; supporting an innovative and dynamic economy; meeting global challenges; and putting the federal budget on a stronger long-term federal trajectory as the baby boomers retire.

---

<sup>1</sup> This testimony draws heavily on my prior work, including: [Strengthening the Tax Base](#), Testimony Before the United States Senate Committee on the Budget (September 27, 2023); [Funding Our Nation’s Priorities: Reforming the Tax Code’s Advantageous Treatment of the Wealthy](#), Testimony Before the House Subcommittee on Select Revenue Matters (May 12, 2021).

## THE NATION SPENDS HUNDREDS OF BILLIONS EACH YEAR ON TAX BREAKS ON INCOME FROM WEALTH.

Salary earners pay a top federal tax rate of 40.8 percent on their incomes, in the year they earn it, which is usually withheld in every paycheck. The highest-income filers, however get the bulk of their income not from salaries, but from wealth.<sup>2</sup> Wealth includes financial assets such as stocks and bonds, real estate, personal property such as art, and ownership stakes in non-corporate businesses.<sup>3</sup> About a third of all US wealth is held by the wealthiest 1 percent of households.<sup>4</sup> That wealth generates income, including capital gains from when the assets grow in value, dividends, and business income from ownership of “pass-through” businesses that does not face the corporate tax rate, but is, in theory, taxed at owners’ individual tax rates.

The federal tax system gives income from wealth a series of preferences that allow the very wealthy to effectively choose when—or whether—to pay tax, and at what rate. Large amounts of income from wealth can disappear from the federal tax base and escape being taxed across decades, lifetimes, and even generations. Federal tax breaks on incomes from wealth include:

**Lower rates.** The federal tax code allows income from wealth to face a wide range of rates at a discount to what would be faced on salaries of the same amount—depending on how that income is reported.<sup>5</sup> Long-term capital gains and dividends face a top rate of 23.8 percent, far lower than the top rate of 40.8 percent that would be paid on the same amount of salary. Such preferential rates cost the federal government about \$177 billion annually.<sup>6</sup> The 2017 tax law’s section 199A “pass-through deduction” gives high-income filers a new 11.2 percentage point discount on their top rate on salaries and wages, representing a total tax expenditure of \$42 billion in 2019, with over half of that expenditure accruing to the top 1 percent of filers.<sup>7</sup>

**Deferred tax.** Capital gains, however, are usually invisible to the tax system until they are “realized,” usually when the asset has grown in value is sold. If a wealthy person holds stock that grows in value from \$100 million to \$1 billion, they will not face tax on the \$900 million gain until they sell the stock. That allows the very wealthiest filers to choose when to face capital gains income tax—even though they can enjoy the benefit of the gain. The fact that this income is “real” in any practical sense is perhaps most obvious when filers borrow against the gain at low rates—and then, just as with any other type of income, can choose to either consume or invest the proceeds.<sup>8</sup> At the same time as deferring taxes on gains, wealthy filers will often rush

---

<sup>2</sup> Congressional Budget Office (CBO), [The Distribution of Household Income, 2019](#) (November 15, 2022). These data do not include unrealized capital gains.

<sup>3</sup> CBO, [Trends in the Distribution of Family Wealth, 1989 to 2019](#) 1 (September 27, 2022).

<sup>4</sup> Joint Committee on Taxation (JCT), JCX-51-23, [Present Law on the Income Taxation of High Income and High Wealth Taxpayers](#) 17 (November 7, 2023); *see also id.* at 2.

<sup>5</sup> *See* Lily L. Batchelder & David Kamin, [Taxing the Rich: Issues and Options](#) (February 1, 2020).

<sup>6</sup> The JCT projects that the reduced rate of tax on dividends and long-term capital gains will cost \$1.14 trillion from 2022 to 2026, or an average of \$227.9 billion each year. JCT, JCX-22-22, [Estimates of Federal Tax Expenditures for Fiscal Years 2022-2026](#), at 35 (December 22, 2022). The surtax on net investment income, estimated at—\$254.2 billion between 2022 to 2026, or an average of \$50.8 billion each year—partially offsets the lower rates. *Id.* at 6 n.16, 38.

<sup>7</sup> *See* JCT, *supra* note 4, at 10; *see also* Chuck Marr, Brendan Duke & Chye-Ching Huang, [New Tax Law Is Fundamentally Flawed and Will Require Basic Restructuring](#), Center on Budget and Policy Priorities (CBPP) (August 14, 2018).

<sup>8</sup> *See, e.g.*, Rachel Louise Ensign & Richard Rubin, [Buy, Borrow, Die: How Rich Americans Live Off Their Paper Wealth](#), Wall Street Journal (July 13, 2021).

to harvest losses. This is the main driver behind estimates that the 400 highest-income households in the country paid effective federal income tax rates in the range of 8 to 10 percent.<sup>9</sup> Precise estimates are difficult to make: the nature of this preference means that the income does not show up on federal income tax returns.

***Evaporating income***<sup>10</sup> (*stepped-up basis*). If a wealthy person holds assets that have gained in value until they die, then that untaxed gain disappears from the income tax system entirely. Neither they nor their heirs will ever pay income tax on the gain. This provision is referred to as “stepped up basis,” or the “angel of death loophole.”<sup>11</sup> It is a federal tax subsidy for wealthy families making intergenerational transfers because bequests are exempt from capital gains taxes that would normally apply to the sale or transfer of appreciated assets.<sup>12</sup> JCT estimates that this exemption costs some \$60 billion annually.<sup>13</sup> Over half of the value of the wealthiest estates is made up of unrealized gain that has never faced tax.<sup>14</sup> A weakened estate tax means that much of that income will never face any type of federal tax.

## A DIZZYING ARRAY OF TAX BREAKS, LOOPHOLES, AND GAMING

Lower rates, tax deferral, and the stepped-up basis are the most obvious tax preferences for the wealthy. In turn, those tax breaks support a dizzying array of additional methods that wealthy filers can use to push yet more income out of the tax base.

Lawmakers have deliberately enacted further preferences that build on or expand the rate, deferral, and step-up provisions. And tax advisors have also created loopholes and complex avoidance schemes. Using such methods, wealthy filers can not only seek the lowest possible tax rate on income from their assets, but they can also try to push their *labor* income into the code’s preferences for “capital” income, to avoid top income and payroll rates.

Examples include:<sup>15</sup>

- **Carried Interest:** Managers of private investment funds (including hedge funds, venture capital funds, and private equity funds) can be paid in both “management fees” taxed at

---

<sup>9</sup> Danny Yagan, [What Is the Average Federal Individual Income Tax Rate on the Wealthiest Americans?](#), 39 Oxford Review of Economic Policy 438-50 (Autumn 2023). For an earlier version of this paper based on data through 2018, see Greg Leiserson & Danny Yagan, [What is the Average Federal Individual Income Tax Rate on the Wealthiest Americans?](#), White House (2021).

<sup>10</sup> See Jason S. Oh, [Increasing Progressivity by Reforming the Taxation of Capital Income](#), Testimony Before the Subcommittee on Select Revenue Measures 2-3 (May 12, 2021).

<sup>11</sup> Michael Kinsley, [The 'Angel-of-Death' Loophole](#), Washington Post (June 25, 1987).

<sup>12</sup> See Adam Looney, [Funding Our Nation's Priorities: Reforming the Tax Code's Advantageous Treatment of the Wealthy](#), Testimony Before the Subcommittee on Select Revenue Measures (May 12, 2021).

<sup>13</sup> JCT, *supra* note 6, at 37.

<sup>14</sup> Chye-Ching Huang & Chloe Cho, [Ten Facts You Should Know About the Federal Estate Tax](#), CBPP (October 30, 2017).

<sup>15</sup> In the past, loss-making jobba farms (before 1986 tax reform equalized top rates on work and capital income), see Department of the Treasury (Treasury), [The Problem of Corporate Tax Shelters](#) 42 (July 1999), and “basket options” (after gaps emerged again), see [Wyden Urges Treasury Action Against Basket Options](#), Tax Notes (June 16, 2015) were other popular techniques, and more recently capital treatment for SPAC founders was one feature of the SPAC craze. See Lee A. Sheppard, [SPAC Founders' Shares Are Compensation](#), Tax Notes (February 22, 2021).

ordinary income rates and “carried interest” taxed at low capital gains rates. Managers typically choose to receive as much of their income as possible as carried interest.<sup>16</sup>

- **Turning life insurance, investment funds, health savings accounts, and retirement accounts into tax shelters.** Some investments, if made directly by a wealthy household, would generate capital gains and dividends that would be taxed at preferential rates. But planners have found ways to exploit loopholes and deliberate preferences in the code to take that income from wealth entirely out of the tax system by running it through various vehicles recognized by the tax code.

For example, a loophole enables deferral and even complete avoidance of tax on capital gains made **through Exchange Traded Funds (ETFs)**, including extreme forms of tax avoidance such as “heartbeat trades,” in which investment banks partner with ETFs to cycle large stock portfolios into funds and then quickly out of them using in-kind redemptions.<sup>17</sup> **Private Placement Life Insurance (PPLI)**, a form of life insurance offered privately and only to the wealthiest individuals, enables investment in a wide range of assets and structures (including hedge funds), with tax-deferred growth and tax-free transfer to heirs.<sup>18</sup> **Health Savings Accounts (HSAs)**, instead of improving health care, has become a favored vehicle for tax sheltering, in part due to the ability for pre-tax contributions to be invested and to accrue earnings free of tax.<sup>19</sup> Retirement accounts, particularly **Roth IRAs**, have increasingly become a vehicle into which the wealthy “stuff” undervalued assets like founders’ stock and never pay tax on their incredible returns.<sup>20</sup>

- **Tax avoidance using pass-through businesses, including relabeling income from labor.**<sup>21</sup> An array of holes in the taxation of pass-throughs allow high-income filers to pick lower rates on their “business” income.<sup>22</sup> The “Gingrich-Edwards” loophole is an example. Active owners of S Corporations, a type of pass-through, can underreport the share of their income from those pass-throughs that is salary for their labor services, overstate the share that is “business profits,” and in doing so avoid both the 3.8 percent Medicare payroll taxes on high salaries and the parallel 3.8 percent tax on net investment income. The 2017 “Tax Cuts and Jobs Act” (TCJA) section 199A pass-through deduction supercharges the incentive for filers

---

<sup>16</sup> The 2017 tax law made small modifications but left the tax break largely intact. See Tax Policy Center (TPC), [What is Carried Interest, and How is It Taxed?](#) (May 2020).

<sup>17</sup> Sam Potter, Katherine Greifeld & Elaine Chen, [ETF Industry Risks Losing Key Tax Edge as Democrat Whets Knife](#), Bloomberg (September 14, 2021).

<sup>18</sup> See Press Release, U.S. Senate Committee on Finance, [Wyden Launches Investigation Into Private Placement Life Insurance Schemes](#) (August 15, 2022). See also Lauren Loricchio, Sarah Paez, Kiarra M. Strocko & Chandra Wallace, [Offshore Life Insurance: Wrapped in Controversy Amid Senate Probe](#), Tax Notes (August 31, 2023).

<sup>19</sup> For discussion of existing tax sheltering using HSAs and House proposals that would exacerbate these problems, see Gideon Lukens, [Expanding Health Savings Accounts Would Boost Tax Shelters, Not Access to Care](#), CBPP (June 22, 2023).

<sup>20</sup> See Justin Elliott, Patricia Callahan & James Bandler, [Lord of the Roths: How Tech Mogul Peter Thiel Turned a Retirement Account for the Middle Class Into a \\$5 Billion Tax-Free Piggy Bank](#), ProPublica (June 24, 2021).

<sup>21</sup> See Huang, *Strengthening the Tax Base*, *supra* note 1, at 1-2, 6, 11-12, 14-15.

<sup>22</sup> See Treasury, [Gaps between the Net Investment Income Tax Base and the Employment Tax Base](#) (April 14, 2016).

to reclassify their income from services as “business” income. Its “guardrails” to prevent this are illogical and porous.<sup>23</sup>

Research suggests that about three quarters of “business profits” the very wealthy receive through their pass-throughs may in fact be compensation for their labor.<sup>24</sup>

The taxation of **partnerships**—a form of pass-through controlling more than \$40 trillion in assets and vastly outnumbering public firms<sup>25</sup>—is another problem area that currently combines complexity, inconsistency in the system, and optionality.<sup>26</sup>

One role of the **estate tax** is to provide a backstop ensuring that some of the income that escapes the income tax base on its way to heirs is subject to at least some federal tax. More than half of the value of estates with over \$100 million in assets are made up of unrealized capital gains that have never been taxed.<sup>27</sup> But the estate tax has been so weakened that only the largest 1 out of every 1000 estates in the country faces the tax, and those that do pay an effective rate of 16.5 percent because so much of the value of an estate is exempt.<sup>28</sup>

Only the already wealthy can enjoy outright tax breaks on wealth; they try to expand the coverage of these tax breaks and maneuver through audits and disputes with the IRS to protect those advantages. They have the resources to hire expert tax lawyers and accountants who set up this tax planning and to enlarge and defend their tax breaks through the courts. Such tools are not available to low- and moderate-income workers, who are taxed at ordinary rates, pay taxes as they earn their wages and salary, and overwhelmingly have no professional representation when they are audited.<sup>29</sup>

## COMPLEXITY AND OPACITY CONCEAL TAX EVASION

The focus of this hearing is the ways in which high-income filers lawfully reduce their taxes, but it is important to know that tax breaks in the law have costs that include unlawful tax evasion.

The top 1 percent (by income) of filers are responsible for some 28 percent of the tax gap of taxes owed but not paid each year that flows from individual income underreporting—amounting

---

<sup>23</sup> See Samantha Jacoby, [Repealing Flawed “Pass-Through” Deduction Should Be Part of Recovery Legislation](#), CBPP (June 1, 2021).

<sup>24</sup> Matthew Smith, Danny Yagan, Owen Zidar & Eric Zwick, [Capitalists in the Twenty-First Century](#), 134 Quarterly Journal of Economics 1675, 1675-76 (2019).

<sup>25</sup> For the size of total assets of all partnerships, see IRS, [SOI Tax Stats – Partnership Data by Size of Total Assets \(All Partnerships\)](#) (2020). There were over 4 million partnerships in 2020, IRS, [SOI Tax Stats – Partnership Statistics by Entity Type](#), Table 9a, compared with about 4,000 to 7,000 public companies. See also, IRS, [SOI Tax Stats - Corporation Data by Type of Return](#).

<sup>26</sup> See Chye-Ching Huang, [Building Back Better: Raising Revenue to Invest in Shared Prosperity](#), Testimony Before the Joint Economic Committee 10 (October 6, 2021); see also Press Release, U.S. Senate Committee on Finance, [Wyden Unveils Proposal To Close Loopholes Allowing Wealthy Investors, Mega-Corporations To Use Partnerships To Avoid Paying Tax](#) (September 10, 2021); Michael Cooper et al., [Business in the United States: Who Owns It, and How Much Tax Do They Pay?](#), 30 Tax Policy and the Economy 91 (2016).

<sup>27</sup> See CBPP, [The Federal Estate Tax](#) (November 7, 2018).

<sup>28</sup> *Id.* See also Tax Law Center, [Broadening the US Federal Tax Base](#) (September 27, 2023).

<sup>29</sup> See Nina E. Olson, [Hearing Before the House Committee on Oversight and Government Reform](#) (April 17, 2018).

to some \$80 billion annually, according to Internal Revenue Service (IRS) estimates.<sup>30</sup> Other estimates suggest those figures are even higher.<sup>31</sup> Some of this tax gap is caused by high-income filers attempting to lawfully avoid taxes but overstepping into unlawful evasion. Some of it flows from the most egregious forms of tax evasion associated with the proceeds of other crimes including sanctions, evasion, and corruption.

Both scenarios can be difficult for the IRS to detect and untangle. Wealthy households can have finances far more complex than most typical salary earners. Some of that complexity arises from the slew of tax breaks on income from wealth and the complicated structures developed to take advantage of them.<sup>32</sup> Webs of entities used by high-income filers that own wealth and make income can also make it difficult for the IRS to match income to owners who should pay tax on it. And, unlike income from earnings reported on W-2s (which enjoy 99% compliance rates), the IRS often holds little or no “third-party” independent information on income from wealth that they can use to verify the source or amount of reported (or unreported) income.<sup>33</sup>

The returns of wage and salary filers are far easier and cheaper to audit than the complex returns of high-income filers. Before the recent Inflation Reduction Act (IRA) passed, the IRS lost about 40 percent of its auditors, including those experienced enough to review the most complex returns of large businesses and high net worth individuals.<sup>34</sup> Audit rates for the top 1 percent of filers fell by more than 70 percent, becoming a shrinking share of all audits.<sup>35</sup>

---

<sup>30</sup> Andrew Johns & Joel Slemrod, *The Distribution of Income Tax Noncompliance*, 63 Nat'l Tax J. *The Distribution of Income Tax Noncompliance*, 63 Nat'l Tax J. 397, 406 (2010); Jason DeBacker et al., *Tax Noncompliance and Measures of Income Inequality*, Tax Notes Federal 7-8 (February 16, 2020). The individual income tax underreporting gap is estimated to have increased from about \$348 billion annually between 2014 to 2016 to about \$396 billion in 2021. IRS, [Tax Gap Projections for Tax Years 2020 & 2021](#) 12 (October 12, 2023). See Huang, *Funding Our Nation's Priorities*, *supra* note 1.

<sup>31</sup> See John Guyton et al., *Tax Evasion at the Top of the Income Distribution* 35 (National Bureau of Economic Research, Working Paper No. 28542, 2021). Estimates of the total tax gap and the share attributable to the highest income filers vary and are difficult to make given limited sightlines of the IRS into some major categories of non-compliance (including offshore income, digital assets, and income held through complex layers of entities). See Daniel Reck et al., Washington Center for Equitable Growth, *Tax Evasion at the Top of the U.S. Income Distribution and How to Fight It* (March 22, 2021); *Tax Gap Projections for Tax Years 2020 & 2021*, *supra* note 30, at 18-21.

<sup>32</sup> Tax system complexity is thought to be a driver of the tax gap generally. See CRS, [Federal Tax Gap: Size, Contributing Factors, and the Debate Over Reducing It](#) 2 (October 30, 2022) (“Tax code complexity also creates opportunities for taxpayers who can afford to hire tax professionals to reduce their tax liability through questionable interpretations of the code.”).

<sup>33</sup> IRS, [Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2011–2013](#) 20 (September 2019).

<sup>34</sup> See Chuck Marr et al., [Rebuilding the IRS Would Reduce the Tax Gap, Help Replenish Depleted Revenue Base](#) (December 16, 2022).

<sup>35</sup> Calculations use data from: IRS, [IRS Data Book Table 17a: Examination Coverage and Recommended Additional Tax After Examination, by Type and Size of Return, Tax Years 2010–2018](#) (last updated October 22, 2020). The top 1 percent includes all filers with adjusted gross income of \$500,000 and above. Table 17a includes in-process and completed audits, so figures may change as new audits are opened for recent tax years. The figure cited above is for Tax Year 2015, the most recent year outside the normal statute of limitations for tax returns filed on time.

## COSTLY TAX SUBSIDIES FOR INCOME FROM WEALTH ARE A POOR WAY TO INVEST IN THE NATION’S FUTURE

Targeted tax breaks for specific types of income like those for wealth are sometimes called “tax expenditures,”<sup>36</sup> or “spending through the tax code,” because their economic and budgetary impact is like a spending program designed to subsidize a particular activity.<sup>37</sup> These preferences carve income out of the federal tax base.<sup>38</sup> Just like other types of federal spending, tax expenditures are not inherently sound or unsound policy.<sup>39</sup> But the largest tax breaks on income from wealth have large costs, including the following:

***Economic costs of tax avoidance and evasion.*** The tax avoidance, sheltering, and gaming that these tax subsidies attract pulls capital and talent away from more productive activities.<sup>40</sup>

- **Locking capital into relatively unproductive investments.** The ability to defer taxes on capital gains until they are realized—or wipe them out if held until death—is a major tax incentive for wealthy filers to hold onto old investments that have increased in value. Without this “lock in” effect from taxes, they might instead sell their appreciated assets and use the returns to make other, more productive investments that would deliver a higher pre-tax return for them and for the real economy.
- **Redirecting resources and talent into tax avoidance.** Talent and innovation go into industries devoted to creating and implementing tax avoidance schemes—which are themselves economically inefficient—rather than where that talent could be more productive.<sup>41</sup>
- **Competitively disadvantaging innovation and work.** Relatedly, innovators and entrepreneurs who wish to focus on productive activity in the real economy can find themselves at a disadvantage relative to those who use tax avoidance and evasion to compete.

***Increased inequality.*** About 90 percent of the benefit of lower rates for capital gains and dividends accrues to the top 20 percent of filers, with more than half going to the top 1 out of every thousand filers, and stepped-up basis is similarly concentrated. These tax benefits for existing wealth increase racial wealthiest disparities that have been produced by historical and current barriers to wealth building.<sup>42</sup>

***Failure to deliver promised benefits.*** Those seeking to maintain tax breaks for income from wealth often argue—contrary to evidence—that they deliver broad-based economic benefits. In

---

<sup>36</sup> TPC, [Briefing Book \(Tax Expenditures\): What Are Tax Expenditures and How Are They Structured?](#) (May 2020).

<sup>37</sup> See Congressional Budget and Impoundment Control Act of 1974, Pub. L. No. 93-344 §3(a)(3), 88 Stat. 297, 299 (1974).

<sup>38</sup> See Treasury, [Tax Expenditures](#) (last visited September 24, 2023).

<sup>39</sup> For example, the Child Tax Credit is a tax expenditure that is a powerful tool for lifting families out of poverty. See CBPP, [Policy Basics: The Child Tax Credit](#) (December 7, 2022).

<sup>40</sup> This effect can be described as a reduction in “allocative efficiency.” Empirical literature suggests that allocative efficiency effects can be more substantial than supply-side impacts in the context of individual income tax reform, see William Gale & Andrew A. Samwick, [Effects of Income Tax Changes on Economic Growth](#), Brookings Institution (February 1, 2016).

<sup>41</sup> Len Burman, [Capital Gains Tax Rates and Economic Growth \(or not\)](#), Forbes (March 15, 2012).

<sup>42</sup> See Lily Batchelder & Greg Leiserson, [Disparities in the Benefits of Tax Expenditures by Race and Ethnicity](#), Treasury (January 20, 2023).

fact, there is little evidence that such tax breaks increase private savings rates—while the amounts they add to national deficits and their other economic costs are large and clear.<sup>43</sup>

***Fiscal costs - and opportunity costs.*** The combination of lower rates for long-term capital gains and dividend income and stepped-up basis adds over \$200 billion to deficits annually.<sup>44</sup> Taxes owed but not paid by the top 1 percent (by income) of filers is an additional \$77 to 143 billion of the annual individual income underreporting gap.<sup>45</sup>

Devoting hundreds of billions in federal resources annually to support lower (and unpaid) taxes on income from wealth represents a missed opportunity to make investments that could deliver better returns for the nation.

## **REALLOCATING TAX BREAKS ON WEALTH TO BETTER INVESTMENTS**

Major provisions of the tax law enacted by President Trump are set to expire at the end of 2025. Some lawmakers are proposing to halt this in full without offsetting the cost.<sup>46</sup> That would increase inequality, further lower revenues, and add to deficits, and would represent a tripling-down on a policy mistake already made twice before. Without the two rounds of tax cuts first enacted under President Bush and President Trump, both of which gave a disproportionate share of their benefit to the already wealthy, revenues would be three percent higher as a share of GDP today and the ratio of debt to GDP would be declining indefinitely.<sup>47</sup>

Instead, in 2025 lawmakers can take the opportunity to raise revenues to meet our nation's fiscal and economic challenges, including by redirecting federal resources away tax breaks for wealth towards better investments.<sup>48</sup>

Federal revenues are currently about 18.4 percent of GDP, and CBO projects this to fall through 2025, and to rise only modestly thereafter. But a large part of that projected rise in revenues will take place only if the parts of the 2017 tax law that are scheduled to expire do in fact sunset. The U.S. raises less revenue at all levels of government, relative to the size of its economy, than most other developed countries.<sup>49</sup>

---

<sup>43</sup> For reviews of the empirical literature addressing these issues, see Congressional Research Service, [Capital Gains Taxes: An Overview of the Issues](#) (May 24, 2022); Gale & Samwick, *supra* note 40; Chuck Marr & Chye-Ching Huang, [Raising Today's Low Capital Gains Tax Rates Could Promote Economic Efficiency and Fairness, While Helping Reduce Deficits](#), CBPP (September 9, 2012).

<sup>44</sup> JCT, *supra* note 6 at 35.

<sup>45</sup> Estimates suggest that roughly 28 percent to 36 percent of the individual income underreporting gap is attributable to the highest-income one percent of filers. Johns & Slemrod, *supra* note 30; DeBacker et al., *supra* note 30; Guyton et al., *supra* note 31. The individual income tax underreporting gap is estimated to have increased from about \$348 billion annually between 2014 to 2016 to about \$396 billion in 2021. [Internal Revenue Service, Tax Gap Projections for Tax Years 2020 & 2021](#), *supra* note 30.

<sup>46</sup> See, e.g., TCJA Permanency Act, H.R. 976, 118th Cong. (2023).

<sup>47</sup> Bobby Kogan, [Tax Cuts Are Primarily Responsible for the Increasing Debt Ratio](#), Center for American Progress (March 27, 2023).

<sup>48</sup> Brian Deese & David Kamin, [Principles for the 2025 Tax Debate](#), Tax Notes (October 16, 2023); Bobby Kogan, [The Rich Get Richer, Deficits Get Bigger: How Tax Cuts for the Wealthy and Corporations Drive National Debt](#), Testimony Before the Senate Budget Committee n.xxvi (May 17, 2023).

<sup>49</sup> TPC, [How Do US Taxes Compare Internationally?](#) (May 2020).



The projected long-run growth in federal spending stems primarily from the retirement of the baby boomers and the related rise in health care and retirement security costs.<sup>50</sup> Higher revenues can help address these costs while preventing cuts to programs and investments that would both increase hardship and weaken the economy.<sup>51</sup> Raising revenues can also support the investments needed to raise health and living standards for low- and moderate-income families; secure an innovative, dynamic, and inclusive economy; and address global challenges.

**Revenue options.** There are many sound options for raising revenue. For instance, in “[Broadening the US Federal Tax Base](#),” the Tax Law Center has compiled several dozen options to strengthen the tax base, which we have designed or analyzed. The options span individual, transfer, corporate, and other federal taxes. This work draws on the deep tax practice, tax administration, and research expertise of our staff, and our networks of public interest minded tax researchers and market actors.<sup>52</sup>

To bring more income from wealth into the tax base in 2025, lawmakers can:

**(1) Allow tax breaks for income from wealth to expire.** Various provisions of the TCJA expanded tax breaks for income from wealth, increased complexity, encouraged tax avoidance, and delivered no discernible economic benefit.<sup>53</sup> They should be allowed to expire, and include the following:

- **The section 199A “pass through” deduction.** If kept in place, it will cost \$700 billion over 2026-2035.<sup>54</sup> More than half of its value goes to the top 1 percent (by income) of filers, and a full quarter goes to the highest-income one out of every thousand tax filers.<sup>55</sup> Tax advisors have called section 199A a “gaping hole” in the code.<sup>56</sup> It is, “the very worst kind of tax policy, picking winners and losers haphazardly in a complex tax provision, and then generating significant incentives for people to rearrange their businesses to try to get on the right side of the line.”<sup>57</sup> Research suggests that the deduction failed to boost economic activity in the two years following its enactment.<sup>58</sup>

---

<sup>50</sup> CBO, [The 2023 Long-Term Budget Outlook](#) 6 (June 2023).

<sup>51</sup> See Paul Van de Water, [Medicare Is Not “Bankrupt.”](#) CBPP (February 13, 2023).

<sup>52</sup> Many other compilations of potential base broadening options include Treasury’s “Green Books,” tax reform proposals, and CBO’s “Budget Options.” Ours focuses on options that the Tax Law Center has developed or analyzed recently in consultation with other experts, and includes links to relevant Tax Law Center publications such as our Priority Guidance Plan submissions and analyses of proposed legislation.

<sup>53</sup> The Tax Law Center and others have written about how the TCJA should be addressed more broadly. See Deese & Kamin, *supra* note 48; Huang, *Funding Our Nation’s Priorities*, *supra* note 1; Chuck Marr, [2025 Tax Debate Begins, Offers Opportunity for Course Correction](#), CBPP (March 7, 2023).

<sup>54</sup> Chuck Marr & Samantha Jacoby, [The Pass-Through Deduction is Tilted Heavily to the Wealthy, Is Costly, and Should Expire as Scheduled](#), CBPP (June 8, 2023).

<sup>55</sup> TPC, [Tax Benefit of the Deduction for Qualified Business Income, Baseline: Current Law, Distribution of Federal Tax Changes by Expanded Cash Income Percentile, 2022](#) (December 29, 2022).

<sup>56</sup> Emily Horton, [Tax Planner: Drive Wealthy Clients Through “Gaping Hole” in Tax Code](#), CBPP (May 31, 2018).

<sup>57</sup> Jacoby, *supra* note 23 (quoting David Kamin). Similarly, former JCT Chief of Staff Edward Kleinbard called it “Congress’ worst idea ever.” *Id.*

<sup>58</sup> Lucas Goodman et al., [How Do Business Owners Respond to a Tax Cut? Examining the 199A Deduction for Pass-Through Firms](#) 1-4 (National Bureau of Economic Research, Working Paper No. 28680, 2022).

- **The doubled exclusion from estate and gift taxes.** The 2017 tax law doubled the amount that a wealthy couple can pass tax-free to their heirs from \$11 million to \$22 million. Extending this would cost \$125 billion between 2026 and 2033.<sup>59</sup> The doubled exclusion potentially *more than* doubles the amount of money wealthy individuals can pass on tax-free. This is because the exemption can be used to make lifetime gifts of assets, and those assets may appreciate over the donee's lifetime. Such gifts can facilitate some of the most complex tax avoidance techniques that push large fortunes out of the transfer tax base.<sup>60</sup>

**(2) Ensure the IRS has adequate resources and tools so that more wealthy filers pay what they owe under the law.** To rebuild and transform taxpayer services and ensure that high-income filers and large corporations pay more of the taxes they already owe, the IRA provided the IRS an additional \$80 billion to be spent through the end of 2031. CBO estimated that this funding would raise a *net* \$180.4 billion between 2022 and 2031 by simply collecting more tax revenue that is already owed under the law.<sup>61</sup> Along with improvements to taxpayer services, the IRS has embarked on several initiatives to improve high-income compliance, including creating a new unit specifically to address large and complex pass-through entities and tripling the size of its global high-wealth group.<sup>62</sup> But by cutting some \$21.39 billion from this IRA funding, the debt limit deal, if implemented, will *add* to deficits by a net of some \$19 billion over the next ten years in increased tax non-compliance,<sup>63</sup> and move forward a cliff in IRS funding to FY2030.<sup>64</sup> Lawmakers can address this cliff in 2025 and before then not worsen the damage from the debt ceiling deal. Doing so will raise net revenue by continuing increased tax compliance among wealthy filer and large businesses.<sup>65</sup>

Additionally, lawmakers can ensure that the IRS and other regulators are able to better understand the opaque structures and transactions that some wealthy filers use to conduct tax evasion, money laundering, sanctions evasion, and other crimes. Options include the following:

- **Improving the bipartisan Corporate Transparency Act (CTA) to identify tax evasion and other criminal activity using pass-throughs.** The Panama Papers highlighted the use

<sup>59</sup> CBO, [Budgetary Outcomes Under Alternative Assumptions About Spending and Revenue](#) Table 1 (May 2023).

<sup>60</sup> See, e.g., Jesse Drucker & Maureen Farrell, [A Lavish Tax Dodge for the Ultrawealthy Is Easily Multiplied](#), New York Times (December 28, 2021); Barbara Bryniarski, [Helping a Client Benefit from an Intentionally Defective Grantor Trust](#), Tax Adviser (November 11, 2021).

<sup>61</sup> Phillip L. Swagel, [Congressional Budget Office, Additional Information About Increased Enforcement by the Internal Revenue Service](#) 1 (August 25, 2022).

<sup>62</sup> See IRS, IR-2023-166, [IRS Announces Sweeping Effort to Restore Fairness to Tax System with Inflation Reduction Act Funding; New Compliance Efforts Focused on Increasing Scrutiny on High-Income, Partnerships, Corporations and Promoters Abusing Tax Rules on the Books](#), (September 8, 2023); IRS, IR-2023-176, [IRS to Establish Special Pass-Through Organization to Help with High-Income Compliance Efforts; New Workgroup to Blend Current Employees and New Hires to Focus on Complex Partnerships, Other Key Areas](#) (September 20, 2023); Wesley Elmore, [IRS Tripling Size of Its Global High-Wealth Group](#), Tax Notes (October 30, 2023).

<sup>63</sup> Thalia Spinrad & Chye-Ching Huang, [Impact of House and Senate IRS Funding Proposals](#), Tax Law Center (July 18, 2023).

<sup>64</sup> Chye-Ching Huang, Thalia Spinrad, & Kathleen Bryant, [Debt Ceiling Deal's Cuts to IRS Funding Bring the IRS Funding Cliff Closer: Appropriators Should Not Compound Harm](#), Tax Law Center (June 28, 2023). Moreover, House bills have proposed to rescind all of the remaining IRA funds and thus would, if enacted, move the funding cliff up to FY2024. *Id.*

<sup>65</sup> Thalia Spinrad & Chye-Ching Huang, *supra* note 63.

of shell companies to hide wealth from tax and law enforcement agencies. Members of this Committee helped lead a sound bipartisan step to address this issue with the CTA, which establishes a registry of the ultimate owners of certain entities that is available to the IRS and other regulators. The registry covers many corporations and LLCs but does not currently include most general partnerships, trust arrangements, or other entities with no state filing requirement. The most egregious tax evasion linked with corruption, sanctions evasion and other criminal activities is likely to flow towards the pass-throughs and other entities left in the shadows, unless lawmakers act. The Tax Law Center has proposed paths forward.<sup>66</sup>

- **Extending broker reporting to high-value art and antiquities.** The opaque art and antiquities market facilitates tax and sanctions evasion and money laundering.<sup>67</sup> Currently, brokers must provide information reporting to the IRS on the gross proceeds of and gain or loss on dispositions of certain assets, including stocks, securities, and digital assets, but this requirement does not apply to art and antiquities.<sup>68</sup> The Tax Law Center proposes extending broker reporting to art and antiquities to address their role in enabling tax evasion.
- **Improving information reporting on digital assets.** Digital assets pose “a significant detection problem by facilitating illegal activity broadly including tax evasion.”<sup>69</sup> In 2019, the Financial Action Task Force (FATF) extended its anti-money laundering and counter-terrorist financing measures to digital assets.<sup>70</sup> But the US is not fully compliant.<sup>71</sup> Congressional action, such as the bipartisan Digital Asset Anti-Money Laundering Act, could help bring the US into compliance and address the significant money laundering and tax evasions risks posed by digital assets by ensuring additional information reporting.<sup>72</sup>

Finally, lawmakers should be ready to respond when taxpayers exploit loopholes in the tax code or undermine provisions that aim to curtail tax avoidance, including by securing interpretations of the code in the courts that undermine legislative intent and tax compliance.<sup>73</sup>

---

<sup>66</sup> Sophia Yan, [How Strengthening the Corporate Transparency Act Can Help the IRS Follow the Money](#), Just Security (April 12, 2022); Sophia Yan, [Budget Represents a Missed Opportunity to Promote Corporate Transparency Act Reforms](#), Tax Law Center (April 19, 2023); Tax Law Center, [Comment Letter on Beneficial Ownership Information Reporting Requirements](#) (February 7, 2022).

<sup>67</sup> See, e.g., Graham Bowley, [As Money Launderers Buy Dalís, U.S. Looks at Lifting the Veil on Art Sales](#), New York Times (June 19, 2021); Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, [The Art Industry and U.S. Policies that Undermine Sanctions](#) 35-37 (July 27, 2020).

<sup>68</sup> The Secretary of Treasury has not exercised her authority under Section 6045(a) to require brokers to report the gross proceeds of transactions involving art and antiquities.

<sup>69</sup> Treasury, [The American Families Plan Tax Compliance Agenda](#) 20 (May 2021) (citing Omri Marian, *Are Cryptocurrencies Super Tax Havens?*, 112 Mich. L. Rev. First Impressions 38 (2013)); see also Treasury, [General Explanations of the Administration's Revenue Proposals for Fiscal Year 2024](#) 200 (March 2023); David Lawder, [U.S. IRS chief asks Congress for authority to collect cryptocurrency transfer data](#), Reuters (June 8, 2021).

<sup>70</sup> FATF, [Targeted Update on Implementation of the FATF Standards on Virtual Assets and Virtual Asset Service Providers](#) 2 (2023).

<sup>71</sup> FATF, [United States](#) (last accessed November 7, 2023).

<sup>72</sup> Digital Asset Anti-Money Laundering Act of 2023, S. 2669, 118th Cong. (2023).

<sup>73</sup> Taxpayer challenges in the courts have put various bipartisan regimes under pressure, including the reportable transactions regime and the conservation easement deduction. See, e.g., *Mann Construction v. United States*, No. 1:20-cv-11307 (6th Cir. March 3, 2022); *CIC Services LLC v. IRS*, No. 3:17-cv-00110 (E.D. Tenn. March 21, 2021).

**(3) Ensure income from extraordinarily large fortunes faces at least some tax and reduce preferences for income from wealth over work.** Lawmakers can address the fundamental issue that much capital gain and dividend income does not face tax or face it at adequate rates. There are many sound options for doing so. Former JCT Chief of Staff Harry L. Gutman noted that in past decades, “both Democratic and Republican Treasury Departments have identified ‘step-up’ as a problem and proposed essentially identical solutions.”<sup>74</sup> President Biden’s Billionaires Minimum Income Tax would raise \$437 billion over 2024-2033,<sup>75</sup> and Chairman Wyden’s Billionaire’s Income Tax would raise an estimated \$577 billion over ten years.<sup>76</sup>

Lawmakers can also close down or cut back on some of the myriad of other tax breaks and loopholes for income from wealth, such as by closing the “**Gingrich-Edwards**” and related loopholes,<sup>77</sup> ensuring that **partnership taxation** is more rational, clear, and tied to economic reality (including closing the **ETF loophole**);<sup>78</sup> addressing **PPLI**,<sup>79</sup> closing the **carried interest loophole**;<sup>80</sup> and plugging numerous holes in the **transfer tax regime**.<sup>81</sup>

---

IRS, IR-2022-125, [IRS wraps up 2022 "Dirty Dozen" scams list; agency urges taxpayers to watch out for tax avoidance strategies](#) (June 10, 2022). Challenges to the economic substance doctrine are also pending.

<sup>74</sup> Harry L. Gutman, [Funding Our Nation's Priorities: Reforming the Tax Code's Advantageous Treatment of the Wealthy](#), Testimony before the Select Revenue Measures Subcommittee 3 (May 12, 2021).

<sup>75</sup> Treasury, [General Explanations of the Administration's Fiscal Year 2024 Revenue Proposals](#) 82, 214.

<sup>76</sup> JCT estimate for 2022-2031. See Press Release, U.S. Senate Committee on Finance, [Wyden Statement on Billionaires Income Tax Score](#) (November 5, 2021). Other proposals include: ending step-up basis, see Treasury, [General Explanations of the Administration's Fiscal Year 2023 Revenue Proposals](#) 30, 34; “carryover basis,” see Office of Senator Mitt Romney, [Romney, Bennet Offer Path to Bipartisan Compromise on Refundable Credits, Business Tax Fixes](#) (December 15, 2019); targeting consumption out of unrealized gains; and inheritance taxation, see Lily L. Batchelder, [Leveling the Playing Field Between Inherited Income and Income from Work through an Inheritance Tax](#), in *Tackling the Tax Code: Efficient and Equitable Ways to Raise Revenue 48-88* (Jay Shambaugh & Ryan Nunn eds., 2020).

<sup>77</sup> See Huang, *Strengthening the Tax Base*, *supra* note 1, at 14.

<sup>78</sup> *Id.* at 14-17.

<sup>79</sup> See Press Release, U.S. Senate Committee on Finance, [Wyden Launches Investigation Into Private Placement Life Insurance Schemes](#) (August 15, 2022).

<sup>80</sup> See Tax Law Center, [Broadening the US Federal Tax Base](#) (September 27, 2023).

<sup>81</sup> For several options related to closing holes in the transfer tax regime, see *id.*