Ensuring Fair Taxation of the Ultrawealthy to Strengthen Our Nation

Testimony before United States Senate Committee on Finance

Hearing on “The 2025 Tax Policy Debate and Tax Avoidance Strategies”

Thursday, September 12, 2024

10:00am ET

215 Dirksen Senate Office Building

Indivar Dutta-Gupta

Doris Duke Distinguished Visiting Fellow, McCourt School of Public Policy at Georgetown University

Tax Fellow, Roosevelt Institute

Acknowledgements: I thank Liz Pancotti, Zachary Liscow, Bobby Kogan, Bob Lord, Chye-Ching Huang, Josh Bivens, Galen Hendricks, Steve Wamhoff, Grace Henley, Bredan Duke, and Oskar Dye-Furstenberg for sharing their thoughts and resources. All ideas and errors are mine.

Thank you, Senator Wyden, Senator Crapo, and members of the Senate Finance Committee. I am a Doris Duke Distinguished Visiting Fellow at the McCourt School of Public Policy at Georgetown University and a Tax Fellow at the Roosevelt Institute. I am honored to testify before this committee as it considers medium-to-long-term tax reform for 2025. My testimony will draw from my experiences analyzing and developing policies to reduce extreme economic, racial, and gender inequality in ways that strengthen our nation by advancing fairness and prosperity together. This experience includes policies that have been enacted, such as bipartisan improvements to the Child Tax Credit and Earned Income Tax Credit over the past 15 years, as well as those under consideration now to re-balance the economy to strengthen the working and middle class, such as pricing greenhouse gas emissions, higher corporate taxes and taxing more economic income. My testimony is intended to provide helpful context and provides ideas for moving forward on a bipartisan basis to ensure that the tax system supports a democracy and an economy that works as well as possible for the American people.

I. Overview

This testimony highlights the need for policymakers to utilize the tax system, including by ensuring that the ultrawealthy pay fair taxes, to reduce economic inequality in ways that can be expected to raise living standards across the board. My read of the growing body of research on economic inequality in our country today—exemplified in part by the enormous and undertaxed wealth of a miniscule fraction of the 337 million people in our country[1]— is that economic inequality today is extreme and harms the working and middle class.

II. Economic Inequality today is Extreme and Harmful

Though some income and wealth inequality is desirable and inevitable in a liberal democracy, our nation's current levels of economic inequality are extreme and harmful, holding back our nation's productive potential and undermining wellbeing. This is true for income inequality as well as wealth inequality.

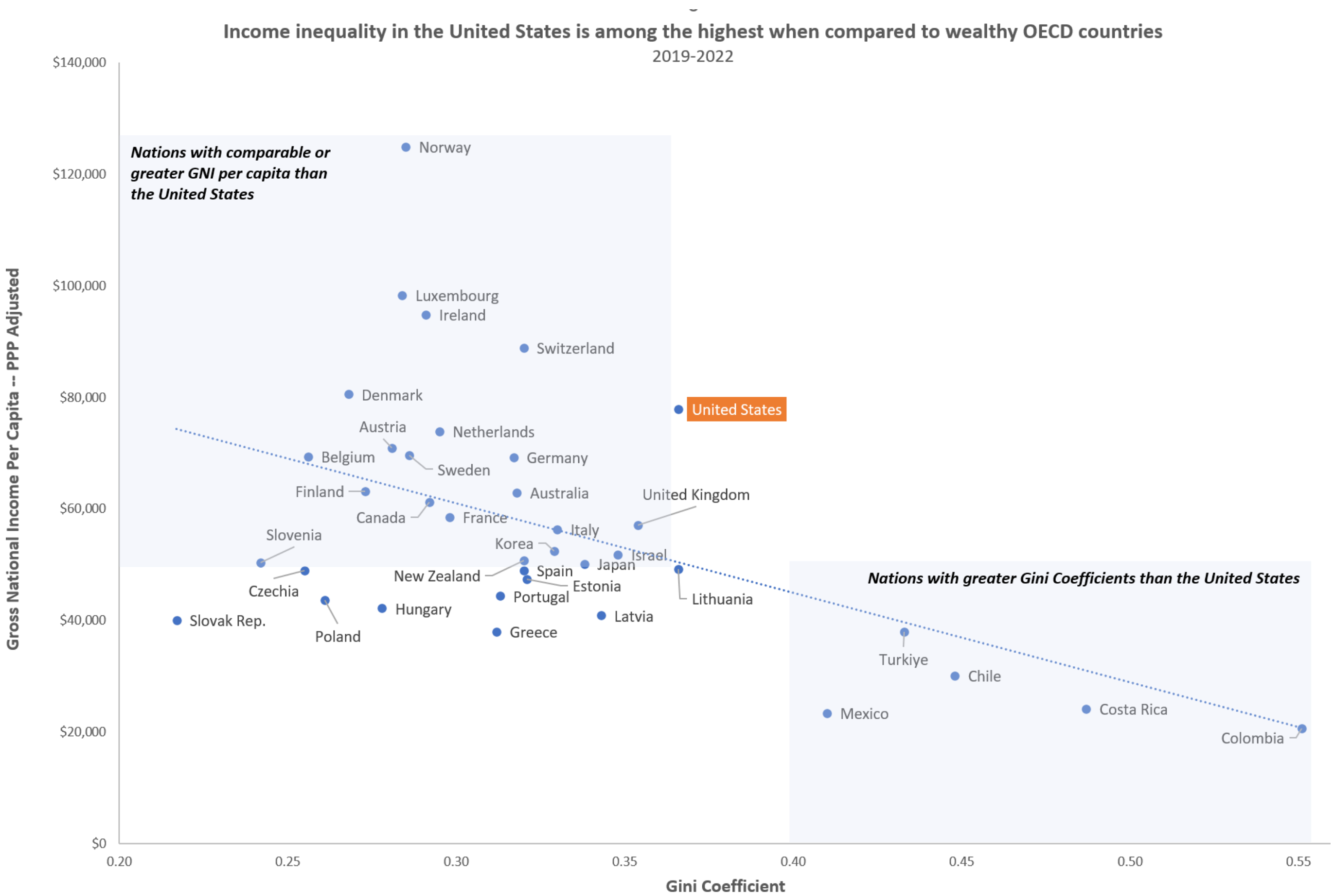
A. Income Inequality is Extreme and Harmful

Income inequality is extreme by historical and international standards, and income inequalities are even more pronounced when comparing identifiable groups with each other, including by race, gender, and place (geography). This level of inequality undermines desirable social and economic outcomes.

1. Overall Income Inequality is Extreme and Harmful.

Income inequality in the United States is extreme by nearly any standard. Using data from the Congressional Budget Office, the average *after*-tax-and-transfer income of the highest 1% in 2020 was approximately 35 times greater than that of the bottom 20%.[2] Income inequality has grown over the past four decades (1979-2020), with the highest 0.01% experiencing *before*-tax-and-transfer income growth (424 percent) that is nearly ten times faster than that of the bottom 20% (45 percent).[3] Even the ratio of before-tax cash income at the 95th percentile to the 10th percentile was near all-time highs (since 1967) in 2022 (3.96) and more than 1.5 times higher than the low point in 1968 (2.56) according to Census Bureau data.[4] While taxes and transfers have helped push back on that growing inequality, after-tax-and-transfer inequality remains markedly higher today than in 1979.[5]

Income inequality in the United States is the highest or among the highest when compared to similarly wealthy nations. Using data compiled by the OECD (Organisation for Economic Co-operation and Development), the United States' Gini coefficient or index, a common measure of income inequality, ranks as among the most unequal countries among those for which after-tax-and-transfer disposable income data are available in 2021.[6] Only Costa Rica, Chile, Colombia, Mexico, and Türkiye—far lower income countries by any measure—are more unequal.[7] In contrast, Luxembourg, Norway, and Ireland have higher per capita Gross National Income (GNI)[8] and substantially lower income inequality than the United States (see chart below).[9]



Source: Organisation for Economic Co-operation and Development (OCED) Data Explorer and World Bank Open Data (Accessed September 10, 2024)

Notes: This chart relies plots two types of data: (i) 2022 Gross National Income per capita adjusted by Purchasing Power Parity (PPP) sourced from the OECD Data Explorer and (ii) 2021 disposable income Gini coefficients data sourced from the OECD Data Explorer with some exceptions due to data availability: Denmark uses 2019 OECD data; Australia, Switzerland, and New Zealand use 2020 OECD data; Mexico and Chile use an average of 2022 and 2020 OECD data; 2021 data points for Türkiye and Colombia were sourced from the World Bank; and South Korea is excluded from the chart due to limited recent Gini coefficient data availability.

If we consider that Ireland's tax policies distort their GNI data, the data on median disposable income similarly shows that among highest income OECD countries (the top five from lowest to highest medians in 2021 are Canada, Switzerland, Norway, the United States, and Luxembourg), the United States has significantly higher income inequality.[10]

The consequences of this growing income divide likely include slower economic growth, reduced economic mobility, and political polarization:

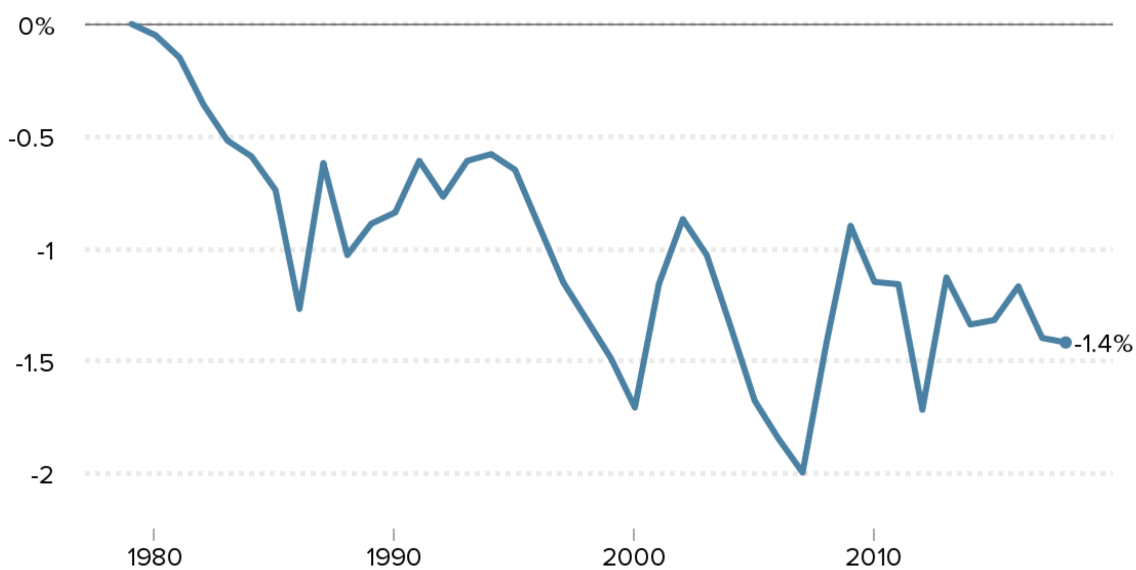
- *High levels of income inequality can hinder overall economic growth.* Research from the OECD concludes straightforwardly, "When income inequality rises, economic growth falls."[11] This effect results from a reduction in educational investments and attainment among the lowest 40 percent of the income distribution. Low- and moderate-income households. Notably, the same research finds that a tax and transfer system that reduces inequality can be consistent with higher economic growth.[12] The Economic Policy Institute estimated that since 1979, growing income inequality had reduced aggregate demand in the U.S. economy by up to 2 percentage points annually through 2018 (see chart below).[13]

"When income inequality rises, economic growth falls."

- The Impact of Income Inequality on Economic Growth (OECD)

Income concentration at the top has dragged on household spending since 1979

How much the upward redistribution of income lowered economywide household spending, as a share of GDP



Notes: To estimate the drag on household spending stemming from the upward redistribution of income, we subtract the savings rates by income group (See Figure D for savings rates calculations) from 1, and then multiply this derived propensity to consume out of income by the income shares for each group to estimate household spending for each group. Then, we sum across all groups to get an aggregate household spending estimate. We do this with actual data, and then construct a counterfactual level of spending that holds 1979 income shares constant. The difference between these is the "all else equal" effect of changing income shares on household spending. We express this spending drag as a percent of overall U.S. GDP.

Source: Congressional Budget Office household income data (CBO 2021) for savings rates and income shares and GDP and personal income data from the Bureau of Economic Analysis's National Income and Product Accounts (BEA 2021a; 2021b).

Economic Policy Institute

- *Higher income inequality in the United States likely contributes to lower income mobility.* Research on high-income countries strongly suggests that high income inequality causes low income mobility with that income inequality shaping access to opportunity, incentives, and more.[14] More recent research suggests that the relationship is compelling for absolute income mobility but may be offset by countervailing forces for relative income mobility.[15]

- *Income inequality appears to contribute to our political polarization.* One analysis found that, "…income inequality has a large, positive and statistically significant effect on political polarization."[16] Other research finds a similar relationship between income inequality and political polarization.[17]

2. Income Inequality by Race and Gender is Sharp and Harmful

Income and earnings inequality is especially extreme by race. From 1972 to 2022, White (non-Hispanic) Americans have consistently had median household incomes 53 percent to 80 percent higher than Black (non-Hispanic) Americans.[18] In 2019, just 1 in 20 Black-headed or Hispanic-headed households had incomes of $200,000 or more, compared to 1 in 10 households overall.[19] Black households comprise approximately 13 percent of US households while making up only about 7 percent of those in the top income quintile.[20]

Gender earnings inequality is significant. Because a large share of households includes more than one gender, and the vast majority of households have incomes that are comprised overwhelmingly of pay from work among adults in the household, it is useful to focus on wages and salaries to understand gender disparities. Economywide, women are paid 84 cents for each dollar paid to a man of the same race.[21] That ratio falls to 77 cents in management, business, and financial occupations and 72 center in professional and related occupations.[22]

Race and gender together can amplify earnings inequities. For instance, in 2023 Black and Latina women were paid significantly less than their White counterparts, with Black women earning only 69% and Latina women just 57% of White men's earnings.[23] The Department of Labor's estimates that earnings disparities from job segregation amounted to a loss in wages equal to $42.7 billion for Black women and $53.3 billion for Hispanic women in 2023.[24]

Racial and gender inequality harms not only communities of color and households with women but all households. For example, growing overall inequality and persistent racial and gender inequality have contributed to a growing Social Security funding gap.[25] More generally, because a sizeable body of research makes clear that racial and gender earnings and income disparities have nothing to do with any group's innate abilities, these inequities reflect our failure to maximize our nation's economic potential.[26] Indeed, research has demonstrated that eliminating racial disparities across the board could dramatically increase economic output in the United States.[27] Federal Reserve Bank of San Francisco research suggests closing gender gaps in the labor market could have raised GDP by

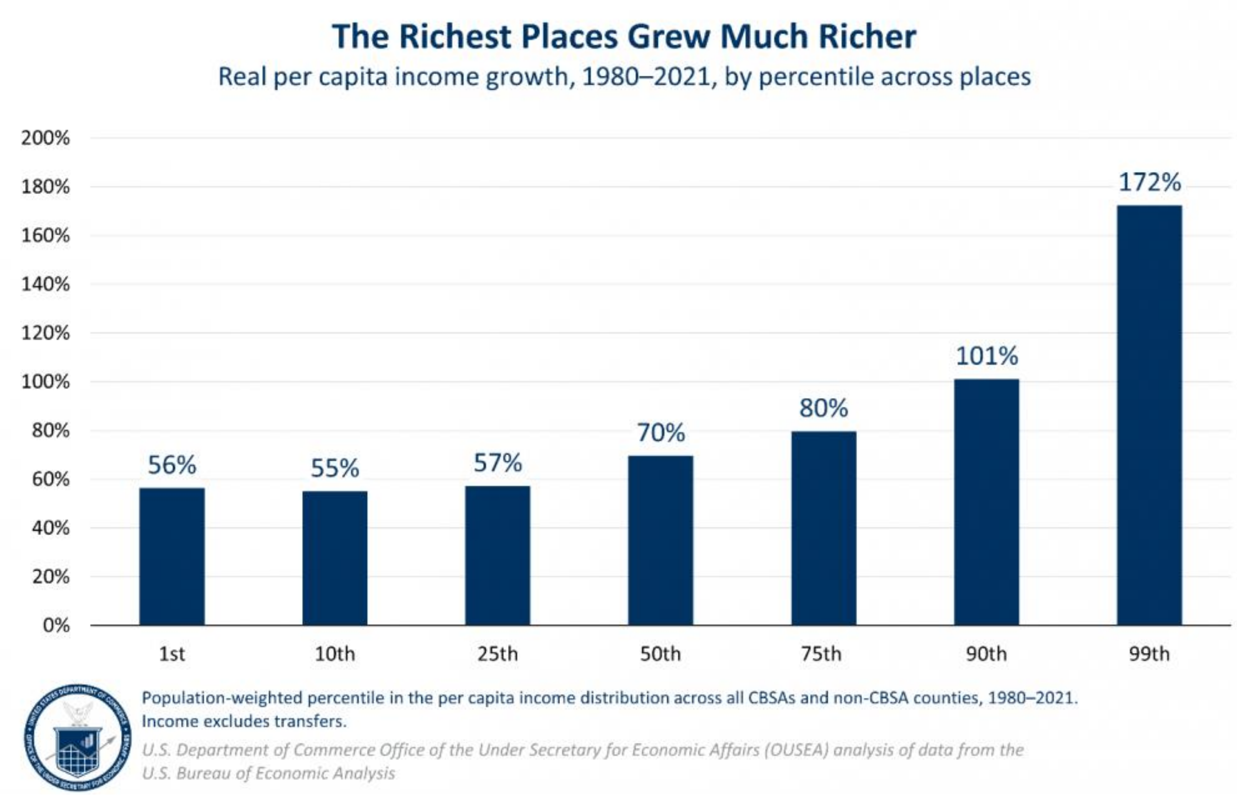
$1.67 trillion in 2019.[28] And eliminating the gender pay gap would significantly lower our nation's high poverty rates.[29] Taking race and gender together, the Federal Reserve Bank of San Francisco research suggests that 2019 economic output was $2.6 trillion less due to racial and gender labor market gaps.[30]

3. Income Inequality by Place is Leaving Communities Behind

Overall, income in the United States is disproportionately concentrated in specific geographic areas, particularly on the East and West Coasts, highlighting the significant regional differences in economic outcomes, with urban and coastal areas hosting large shares of top income households:

- **Metropolitan Areas Dominate the Top 5%**: Approximately 72% of high-income households (top 5%, earning $191,469 or more) are located in the 50 largest metropolitan areas, predominantly found on the coasts. The greatest concentration of high-income households are the metropolitan areas that include San Francisco and New York City, including Connecticut's Bridgeport, Stamford, and Norwalk, as well as California's San Jose and Santa Clara regions.[31]
- **Five States Dominate the Top 1%**: The highest 1 percent of households by income are heavily concentrated in California, New York, Texas, Florida, and Illinois—states which together account for about 40 percent of all U.S. income and half of top one percent income.[32]
- **Two Regions Dominate Top Incomes**: The Northeast and West have a disproportionate share of income among the top earners (53.5 percent of top one percent income versus 45.7 percent of total income) compared to the Midwest and South.[33]

Growing income inequality has meant that as the economy has grown, the gains have gone disproportionately to a small share of communities in the country. Commerce Department analysis shows that indeed the highest income places in the United States have seen per capita income rise by two or three times as much as lower-income communities (see chart).[34]



B. Wealth Inequality is Extreme and Harmful

Wealth inequality, including by race and gender, is high and holds back our nation's economic potential. The top 0.1 percent's share of total net worth in the United States is near a 35-year high and 60 percent greater than in 1989.[35] Wealth disparities by race and gender are sharp. Research suggests that reducing wealth inequality overall and closing racial inequities would boost our nation's economy.

Wealth inequality in the United States is even more extreme than income inequality. In the third and fourth quarters of 2021, the top one percent of households held 30.9 percent of total net worth,[36] while 2021 tax data indicate that the top one percent of households by income received 26.3 percent of all AGI (Adjusted Gross Income).[37]

A substantial portion of wealth in the U.S. is held by a small fraction of households. Even as the top one percent of households held 30.4 percent of net worth in the first

> "Wealth inequality is high and has risen substantially over recent decades."
>
> *- Matthew Smith, Owen Zidar, and Eric Zwick (The Quarterly Journal of Economics)*

quarter of 2024, the top 0.1 percent held a disproportionate share of overall net worth—13.6 percent.[38] Recent research documenting top wealth shares and growth even within the top 0.1 percent has found that even the top 0.01 percent grew its share of total wealth from 1989 to 2016.[39] As the authors of that 2022 study find, "...wealth inequality is high and has risen substantially over recent decades."[40]

Wealth is heavily concentrated in specific parts of the United States. Specifically, over one-fourth of the nation's wealth is owned by households with net worth exceeding $30 million, with New York alone accounting for more than 20% of this extreme wealth.[41] The Northeast region, particularly New York, Connecticut, and Massachusetts, has the highest concentration of extreme wealth, driven largely by the financial sector and other high-income industries.[42]

Racial and gender wealth disparities are sharp. In 2022, median Black and Hispanic households own only about 16 and 21 percent, respectively, of the wealth held by White households, a gap that has been relatively persistent over recent decades.[43] The largest gender wealth gap appears when comparing men and women who have never been married, with the women having just 34 cents for every dollar of men's wealth; controlling for a range of factors still leaves a large gender wage gap ($0.71 for each $1 of men's wealth).[44]

Wealth disparities hold back our economy. One multi-country study that included the United States found that when billionaires acquire wealth through political connections, it can hold back economic growth.[45] Researchers at McKinsey Global Institute estimate that closing Black-White wealth gaps could raise U.S. GDP by 4 to 6 percent in 2028, by increasing consumption and investment.[46] White households face similar wealth inequality as Black households,[47] suggesting that reducing overall wealth inequality could also allow more White households to prosper in our economy.

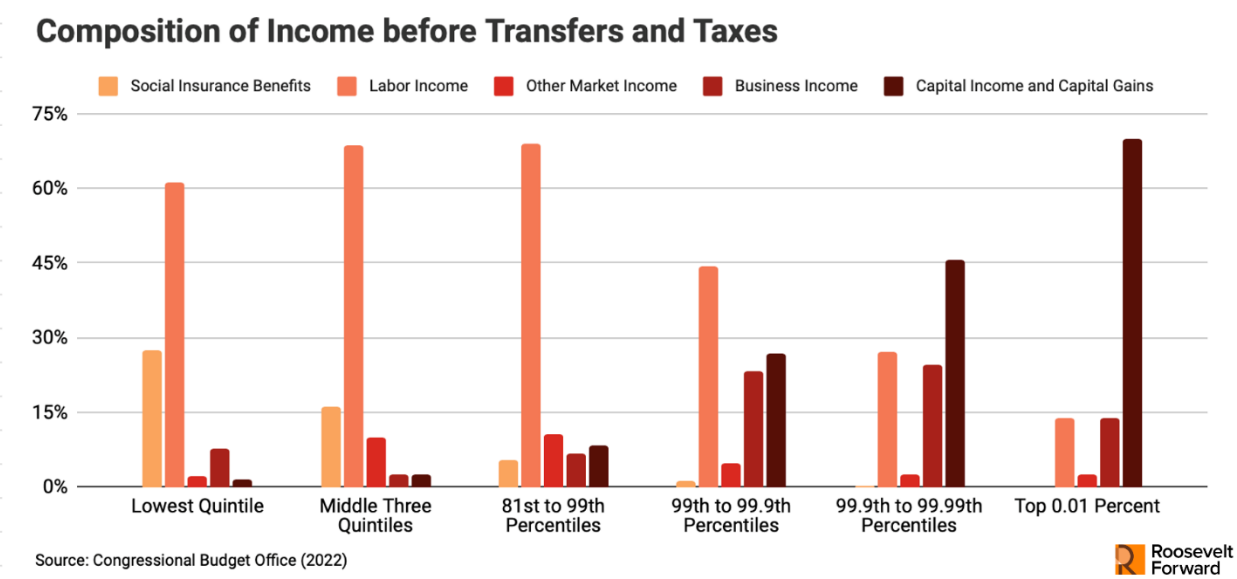
III. Our Tax System Contributes to Extreme Inequality

Our tax system privileges income from wealth over income from work. When considering income (excluding unrealized capital gains), our tax system overall (federal, state, and local) is progressive, thanks largely to the federal income tax system. However, when considering wealth, the progressivity of our tax system is less clear. Much of the returns to wealth, even relatively liquid wealth and wealth that is converted into spending, goes untaxed for the wealthiest, even as state and local property taxes (a form of wealth tax) are regressive on balance and are paid regardless of an exchange or sale. Here, this testimony illustrates how features of our federal tax system encourage the ultrawealthy to accumulate wealth in ways that avoid taxation.

Our tax system privileges income from wealth over income from work.

A. The Ultrawealthy Face a Different Tax System than the Rest of us and Have Taken Advantage of That System

While 99 percent of American households receive a supermajority of their incomes (before transfers, excluding social insurance benefits) from work, the top 1 percent earn a majority of their income from non-labor income sources, including especially income and gains from capital, according to 2019 Congressional Budget Office data.[48]



While labor income is generally taxed at the highest rates, capital income in particular is generally taxed at lower rates. And gains from capital are generally only taxed upon a sale or exchange, even if the asset is easily valued. The gains are permanently exempt from the income tax when transferred upon death due to a "stepped-up basis" through which the capital gain—the typical gap between the capital's current higher value and its original value at purchase—is simply ignored.[1] These features of the federal income tax system mean that, when counting income from unsold stock, the wealthiest 400 families paid federal income tax rates of 6-12 percent from 2010 through 2018.[49]

1. The Ultrawealthy Have Tax-Free or Nearly Tax-Free Income Have a Free Lunch

Unsurprisingly, these realities of the federal tax system create incentives for keeping wealth as capital and passing that capital upon death to heirs. But even billionaires want cashflow, albeit for purchasing yachts and islands rather than food and clothing. The ultrawealthy pledge stock or other assets in exchange for personal loans, effectively converting their capital into cash without paying any tax on gains in that income. Then, their spouses and children can inherit the asset and sell it without a single dollar in income tax ever being paid. Professor Ed McCaffery concisely described this scheme as, "Buy, Borrow, Die".[50] This set of maneuvers creates meaningful cashflow for the wealthiest to consume while evading taxes altogether.

2. Capital Gains and Dividend Taxes are Suboptimal and Low by Historic Standards

One prominent study suggests that the revenue-maximizing capital gains tax rate is 38 to 47 percent.[51] Yet, the individual capital gains tax rate, which the wealthy generally pay at a time of their choosing, typically 20 percent[2]—even for the wealthiest among us.[52] In general, capital gains tax rates are at post-WWII (80-year) lows.[53] As shown earlier, capital gains disproportionately comprise the incomes of the wealthy and ultrawealthy, ensuring that low capital gains tax rates disproportionately enrich the richest Americans.

Until 2003, dividends were taxed similarly to earnings from work. After one temporary tax cut to dividends enacted that year, dividend tax rates were permanently cut to 20 percent, though both dividends and capital gains are subject to the Affordable Care Act's 3.8 percent Net Investment Income Tax.[54] Research

[1] To be sure, some gains may be subject to the estate tax, but that is easily and frequently avoided.
[2] The rate can be as high as 28 percent essentially only for collectibles.

shows no increase in employee compensation or corporate investment from that large 2003 cut,[55] but it does confirm that dividend income is heavily concentrated among the highest income households. Nearly half (46 percent) of dividend income goes to the highest 1 percent of households.[56]

3. Top Marginal Tax Rates are Low by Historic and Revenue-Maximizing Standards

Even if income from wealth were taxed more comparably to labor income, top marginal income tax rates are notably far below revenue-optimizing or historic standards. Top federal marginal rates were between 94 percent (1944 and 1945) and 50 percent from the 1932-1986 55-year period; they currently stand at just 37 percent,[57] while the overall (federal, state, and local) top rate was just 43.7 percent in 2022.[58] Yet, research considering the combination of a reduction in labor supply, increased tax avoidance, and bargaining over composition of compensation suggests an optimal top rate as high as 83 percent.[59]

B. Policymakers Have Many Worthwhile Proposals to Consider to Efficiently Raise Revenues from the Ultrawealthy

A more efficient & equitable tax system would include higher revenues from the ultrawealthy. In addition to raising corporate and other individual taxes, policymakers have many well-designed proposals to advance that goal:

- **IRS Enforcement Funding |** Funding sufficient capacity at the IRS (Internal Revenue to collect owed revenues from the wealthiest taxpayers has been demonstrated to raise substantial revenues at little cost. Before recent investments in IRS capacity, audit rates for high-income households plummeted, while the working and middle class faced a growing share of audits—even as the highest income Americans owed a wildly disproportionate share of taxes owed.[60] A 2024 Treasury analysis finds that sustaining IRA investments "would yield $390 billion in revenue during the period FY 2024–FY 2034".[61] Independent estimates of the return on investment for audits of the highest income households suggests that each dollar spent on these audits yields more than $12 in taxes.[62]
- **Taxing Income from Unrealized Gains |** There are several reasons to tax income as in the year it is made — and not solely at a point of sale or exchange. As noted earlier, we tax the value of property (real property) including increases in the value at the state and local level on an ongoing basis—not solely at the point of a sale or exchange. We also already tax unrealized gains in other instances.[63] As the Joint

Committee on Taxation explains, income from unrealized capital gains is textbook income: included in what economists a "Haig-Simons" income measure, which counts unrealized gains as a form of income that can be used to consume or invest, and so provides a proxy for well-being.[64] Indeed, the underlying assets—frequently publicly-traded equities—are nearly as liquid as cash. Billionaires demonstrate this feature of their wealth routinely, in part by borrowing against their accumulated wealth to convert capital gains into cash to avoid paying taxes.[65]

There are various ways to ensure that this income does not escape tax for years, decades, or forever. For instance, it can be taxed immediately in a "mark-to – market" system, such as the Chairman's Billionaire Income Tax proposal. Or, a system that achieves something similar to a mark-to-market tax can be achieved by triggering the final tax liability at some event (such as when the income is such as when it is passed to heirs or before), coupling that with a withholding system that ensures that tax is paid on incomes including unrealized gains annually.

An example of the latter approach is the Billionaire Minimum Income Tax, which is designed to handle losses and gain and is readily payable by the affected ultrawealthy through the sale of tradeable stocks.[66] Such a tax would ensure that just as the vast majority of workers must pay taxes on their wage incomes, the billionaire buying an asset for $1 billion that grows to $10 billion, providing $9 billion in gains that can provide billions in cashflow while avoiding taxation would pay taxes on those gains. In a time of extraordinary economic inequality, heightened along racial and gender lines, reforms like a well-designed mark-to-market tax applying to the ultrawealthy, accrual accounting, or anti-deferral system can help ensure that the wealthy pay their fair share, raise much-needed revenue, make the tax code more efficient, and further prosperity.

- **Inheritance and Gift Tax |** Well-designed inheritance and gift taxes, including ending stepped-up basis, can reduce dynastic wealth creation and encourage more productive uses of wealth. Prior estate and gift tax law was more progressive and raised more revenue than current law. Though the wealth and gift taxes partly serve as a backstop to untaxed wealth, establish new inheritance and gift taxes could generate significant revenue from the wealthiest Americans. Lily Batchelder has developed a proposal generating substantial revenues from the largest inheritances, arguing that, "Expanding and reforming the taxation of inheritances would improve the fairness and efficiency of the fiscal system, spur growth, and reduce tax complexity and associated tax planning."[67]

This list is illustrative of the possibilities for efficiently raising sizeable revenues from the wealthiest among us. Policymakers should consider including a wider range of policies in any 2025 tax reform, including increasing penalties for tax evasion, and raising revenues from corporations on other high-income households.

IV. Conclusion: Well-Designed Proposals can Generate Useful Revenues & Help Re-Balance the Economy

Income and especially wealth are heavily concentrated within a small share of households, and these extreme inequalities are economically and socially harmful. Some features of the tax code have contributed to the situation by favoring income from wealth over income from work. This situation can be addressed in ways that rebalance our economy—not solely for the purposes of addressing shortcomings from our economy but for shaping the economy in the first place.[3] Research suggests that people with the highest incomes and greatest wealth respond strongly to the tax system, including in bargaining for compensation and in holding untaxed wealth that may be more economically productive if sold or exchanged.

At the same time, the United States faces national needs best addressed through public investment[4]—investments that often provide unbeatable returns to our society. As a result, policies that generate additional revenues from the wealthy and ultrawealthy can provide additional social benefits, beyond reducing harmful inequality. For example, these revenues can help fund **a basic foundation for all, fair access to opportunity, and desirable scientific and technological advancement**:

- **Ensure a Basic Foundation for All |** Research increasingly makes clear that we all need a basic foundation in our lives to be able to access and take advantage of opportunity. That foundation includes **income, care, housing, and health**. Leading Child Tax Credit researchers estimate that societal benefits from a Child Tax Credit that does not discriminate against children in the lowest income households "would outweigh costs nearly 10 to 1, with most benefits due to the tax credit's [reach to the lowest income children]."[68] The Earned Income Tax Credit too has been highly

[3] To be sure, more equal and similarly (or even more) prosperous countries in Europe have generally ensured that labor unions and other labor market institutions ensure that people are fairly compensated rather than building tax and transfer systems that are markedly more redistributive than ours, but that is not the focus of this testimony.
[4] Securing these revenues should be a top priority for those who are concerned about federal budget deficits and debt as well.

effective at boosting employment and incomes but does far too little for those not raising children at home. The United States also faces substantial unmet caregiving needs—needs best addressed through public investments in paid family and medical leave, child care, and home and community-based supports for long-term care. Similarly, our nation's need for millions of additional affordable housing units and assistance for those who are rent-burdened requires public policies that include spending to boost housing supply and reduce costs faced by renters. Essentially alone among wealthy nations, the United States lacks a universal health coverage system, allowing millions of people who are uninsured or underinsured to go without needed care or experience financial distress due to health needs. Subsidies for private coverage and expanded public coverage together could finally establish universal or near universal health coverage in the United States. And research focused on narrowing and eliminating health disparities could help the United States achieve health outcomes that match our nation's wealth.

- **Provide Fair Access to Opportunity |** Education and workforce development investments are essential to weakening the counterproductively strong link between childhood financial circumstances and adult outcomes, as well as ensuring that living standards improve through innovation. Ensuring fair access to opportunity develop one's abilities to the fullest requires large public investments into an equitable education system through post-secondary education and an integrated workforce development system that meets the needs of workers and businesses alike. In addition, investments to promote equitable labor market and economic outcomes for people with disabilities would advance fairness and boost our economy. Comprehensive supports that ensure the nurturing of talent from and attainment of valuable credentials for people all backgrounds would benefit all of society.
- **Address Climate and Environmental Needs |** The nation faces a clear set of climate and environmental challenges that the private sector alone cannot solve. Public spending on climate adaptation and mitigation is essential in the face of increasing extreme weather, inadequate physical infrastructure, and insufficient private investment in research and technology needed to stabilize our planet and ensure a healthy environment for generations to come.

As James Madison wrote in the Federalist Papers, "the most common and durable source of factions has been the various and unequal distribution of property."[69] Fundamentally, higher taxes on the wealthy and ultrawealthy can be fair and efficient, creating equitable economic growth that raises living standards for all Americans—and strengthening our democracy as well.

Endnotes

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