Center on Budget and Policy Priorities

1275 First Street NE, Suite 1200
Washington, DC 20002

Tel: 202-408-1080
Fax: 202-408-1056

center@cbpp.org
www.cbpp.org

September 13, 2021

Ways and Means Revenue Bill Major Step Forward But Additional Steps Available

By Chuck Marr and Samantha Jacoby

The revenue package the House Ways and Means Committee released September 13 is a major step toward enacting economic recovery legislation based on President Biden's "Build Back Better" agenda. After two decades dominated by regressive tax cuts that weakened both revenues and investment in the building blocks of shared prosperity, the legislation would raise more than $2 trillion in revenue — secured through progressive measures — over the decade to fund investments to reduce child poverty, expand health coverage, address climate change, and increase economic opportunity and security for families across the country.

Combined with the bill's health savings, these revenue raisers would offset most of the bill's $3.5 trillion in investments. The House recovery package's *net* cost, a far more appropriate way to evaluate its fiscal and economic impact than the oft-cited $3.5 trillion *gross* cost, would be a small fraction of the gross cost and quite small relative to the size of the economy, which the Congressional Budget Office (CBO) projects to be $288 trillion over the next decade.[1]

Like the Biden plan, the Ways and Means package would raise substantial revenue in three major ways: from high-income and wealthy individuals, from profitable corporations, and from better enforcement of the nation's tax laws to close the gap between the taxes owed and taxes paid — a gap that is disproportionately due to high-income filers' and profitable companies' failure to comply with the law. These revenue raisers would make the tax code more equitable and adequate without undermining economic growth. Indeed, the investments funded by these revenues will strengthen the economy and broaden opportunity over the long run.

While the package is robust, it does omit some key proposals that the President, Senate Democrats, or other policymakers have called for that would strengthen the package and raise additional revenues. In particular, the package should include President Biden's proposal to require financial institutions to provide certain information that will help the IRS identify households that are underreporting their income and cheating on their taxes. This will both raise revenues and make our tax system fairer.

[1] Sharon Parrott, "Commentary: Evaluating BBB Requires Considering Sound Fiscal Metrics and Merits of Investments," Center on Budget and Policy Priorities, August 31, 2021, https://www.cbpp.org/research/federal-budget/evaluating-bbb-requires-considering-sound-fiscal-metrics-and-merits-of.

The package could also do more to ensure that high-income people can't shield their income from taxation as well as reduce incentives for multinational corporations to shift profits to overseas tax havens.

As the debate proceeds, policymakers should make the package stronger and resist pressure from critics to scale back the ambitions of the revenue policies. Even without these improvements, the House made good on its promise to offset most or all of the cost of the investments with sound revenue raisers and health savings. This should end vague debates about the "size" of the package and focus discussion on the specific policies included in this groundbreaking legislation.

Taken together, the investments and revenue raisers in the House Build Back Better package are historic and would promote racial equity. They would result in large advances in reducing child poverty, expanding health coverage, improving housing, and expanding educational opportunity while closing gaping racial and ethnic disparities in each of these areas. And these advances would be financed by measures that raise revenues on the most well-off in our country — who disproportionately are white people — who have benefitted greatly from public investments in areas including research, technology, infrastructure, and education.

Ensuring That Wealthy Individuals Pay Fairer Amount of Tax

Much of the income of wealthy households doesn't appear on their annual tax returns,[2] and much of what does appear enjoys special tax breaks[3] or discounted rates. Prominent examples include realized capital gains, dividends, pass-through business income,[4] and carried interest, all of which are heavily concentrated among wealthy people and are taxed at rates far below the rate on wages and salaries.

The Ways and Means bill would raise the top tax rate on each of these forms of income, thereby reducing (but not eliminating) the special discounts. These changes would make the tax code more equitable by taxing income from *wealth* more like income from *work*. They also would encourage more productive investments by reducing the incentive for investors to pursue investments for the tax savings rather than for economic reasons. These policies, plus the bill's modest 3 percent surtax on household incomes over $5 million, would raise roughly $1 trillion over the decade.

The Ways and Means bill, however, fails to address a significant flaw in the tax code known as the "stepped-up basis" loophole, which allows many extremely wealthy people to pay little or no individual income tax. (A major ProPublica investigation this summer brought public attention to

---

[2] Chuck Marr, "ProPublica Shows How Little the Wealthiest Pay in Taxes: Policymakers Should Respond Accordingly," Center on Budget and Policy Priorities, July 15, 2021, https://www.cbpp.org/research/federal-tax/propublica-shows-how-little-the-wealthiest-pay-in-taxes-policymakers-should.

[3] Chuck Marr, Samantha Jacoby, and Kathleen Bryant, "Substantial Income of Wealthy Households Escapes Annual Taxation or Enjoys Special Tax Breaks," Center on Budget and Policy Priorities, November 13, 2019, https://www.cbpp.org/research/federal-tax/substantial-income-of-wealthy-households-escapes-annual-taxation-or-enjoys.

[4] Samantha Jacoby, "Repealing Flawed 'Pass-Through' Deduction Should Be Part of Recovery Legislation," Center on Budget and Policy Priorities, June 1, 2021, https://www.cbpp.org/research/federal-tax/repealing-flawed-pass-through-deduction-should-be-part-of-recovery-legislation.

the loophole, noting that billionaires Jeff Bezos and Elon Musk avoid tax on much of their incomes.)[5] Currently, when an investor holds an asset (such as stock) until death, neither the investor nor their heirs *ever* owe capital gains tax on its growth in value during the investor's lifetime.

Congress can rectify this omission by including in final legislation the Biden proposal to end the stepped-up basis loophole for wealthy households; the proposal includes special protections for family farms, small businesses, and personal residences. This change is necessary to ensure that a lifetime of previously untaxed capital gains do not continue to go untaxed when wealthy filers die.

Strengthening Corporate Taxes, Discouraging Overseas Tax Shifting

The 2017 tax law slashed the corporate tax rate from 35 percent to 21 percent, disproportionately benefiting wealthy shareholders while failing to generate the large economic benefits that its proponents had promised.[6] The economy (gross domestic product or GDP) didn't grow faster in the two years after the law's enactment, and the major private domestic components of GDP actually slowed, including growth in consumption, business fixed investment, and residential investment.[7]

The Ways and Means bill would partially reverse this rate cut, setting the top corporate rate at 26.5 percent. This would make the tax code more progressive and raise $540 billion over ten years. Still, policymakers should go further and adopt President Biden's proposed 28 percent corporate rate, which would raise more progressive revenue for needed investments.

The 2017 law also made some changes to international tax rules but left in place large incentives for multinationals to shift profits and operations to low-tax countries (known as "tax havens") and even created new incentives.[8] While proponents of the 2017 law claimed it would significantly reduce profit shifting, two years after the law's enactment the amount of profit shifting was virtually identical to that before the law.[9]

The Ways and Means package includes some measures to reduce shifting of profits and investments, such as strengthening the minimum tax on certain foreign profits so that more of firms' foreign income faces the tax and that it's taxed at a higher rate (16.5 percent, versus 10.5

---

[5] Jesse Eisinger, Jeff Ernsthausen, and Paul Kiel, "The Secret IRS Files: Trove of Never-Before-Seen Records Reveal How the Wealthiest Avoid Income Tax," ProPublica, June 8, 2021, https://www.propublica.org/article/the-secret-irs-files-trove-of-never-before-seen-records-reveal-how-the-wealthiest-avoid-income-tax.

[6] Steve Rosenthal and Theo Burke, "Who's Left to Tax? US Taxation and Corporations and Their Shareholders," New York University School of Law, October 27, 2020, https://www.law.nyu.edu/sites/default/files/Who%E2%80%99s%20Left%20to%20Tax%3F%20US%20Taxation%20of%20Corporations%20and%20Their%20Shareholders-%20Rosenthal%20and%20Burke.pdf.

[7] Jason Furman, "Prepared Testimony for the Hearing 'The Disappearing Corporate Income Tax,'" February 11, 2020, https://www.congress.gov/116/meeting/house/110494/witnesses/HHRG-116-WM00-Wstate-FurmanJ-20200211.pdf.

[8] Chye-Ching Huang, "Testimony for the Hearing 'How U.S. International Tax Policy Impacts American Workers, Jobs, and Investment,'" March 25, 2021, https://www.finance.senate.gov/imo/media/doc/Huang%20testimony%2003220221%20rev.pdf.

[9] Kimberly A. Clausing, "Testimony Before the Senate Committee on Finance," March 23, 2021, https://www.finance.senate.gov/imo/media/doc/DAS%20Clausing%20SFC%20Testimony_FINAL.pdf.

percent today). These provisions would raise roughly $350 billion over the decade. This represents an improvement over the 2017 law, but more can and should be done.

Lawmakers should adopt President Biden's proposal to raise the minimum tax rate to 21 percent, which is much closer to the domestic corporate tax rate and would better reduce profit-shifting incentives, as well as his other proposals to close loopholes in the international tax system, such as denying certain deductions to multinationals that operate in tax havens.

These changes would raise significant revenue to invest in infrastructure and workers, which is a far better way to strengthen the economy and support innovation than continuing to permit large-scale tax avoidance by multinationals.

Requiring High-Income People, Corporations to Pay Taxes Owed

Each year roughly $600 billion of legally owed taxes go uncollected; the top 1 percent of filers are responsible for fully $160 billion of this "tax gap." Yet a decade of cuts to the IRS budget has led to large reductions in the number of highly trained audit staff needed to review the largest corporations and the highest-income filers, whose returns are the most complicated. As a result, audit rates for both groups have dropped sharply.

The President has proposed a three-part plan to rebuild the IRS and reduce the tax gap: funding for more enforcement staff, funding to update the agency's antiquated computer systems, and new information reporting requirements for financial institutions to help the IRS target enforcement efficiently. The Ways and Means bill includes the President's full $80 billion funding proposal over ten years, which CBO estimates would generate roughly $200 billion of revenue over the period.

It is also crucial that the House add the information reporting proposal, which is an integral part of the Biden plan but not included in the Ways and Means package. The proposal, which would raise $460 billion over the decade according to the Treasury Department, would require financial institutions to report two new pieces of readily available information to the IRS — how much money flows into and out of bank accounts held by individuals and companies — on the form they already use to report interest income in these accounts. This would allow the IRS to identify individuals who may be sharply underreporting their income on their tax return and target enforcement efforts accordingly. As IRS Commissioner Charles Retting recently explained, "increased information reporting targets underreported income, which is the largest category of the tax gap."[10] A group of former IRS commissioners who served under both Republican and Democratic presidents also pointed out: "Research shows that when the IRS has access to third-party reporting, compliance rates top 95 percent. Without third-party information reporting, compliance rates are below 50 percent. Reliable information is critical to an effective and fair tax system."[11]

---

[10] Letter to Senator Elizabeth Warren, August 27, 2021, https://www.warren.senate.gov/imo/media/doc/Warren%20et%20al%20response%20to%20Warren%20082721.pdf.

[11] Lawrence B. Gibbs *et al.,* "Five former IRS commissioners: Biden's proposal would create a fairer tax system," *Washington Post,* May 4, 2021, https://www.washingtonpost.com/opinions/five-former-irs-commissioners-bidens-proposal-would-create-a-fairer-tax-system/2021/05/04/c4ee8346-acfc-11eb-ab4c-986555a1c511_story.html.

It is important to note that the reporting obligation falls on financial institutions, not on individuals or companies. The information is about gross inflows and outflows, not individual transactions, and important privacy protections are built into the proposal. For most people, it won't matter that this information is reported to the IRS, but the information will allow the IRS to better target enforcement efforts and identify tax cheating.

Robust Revenues Should Focus Debate on Package's True Cost, Benefits

As House committees draft and approve the different pieces of the recovery package, the discussion of its size — much of which has centered on its $3.5 trillion gross cost — and benefits can now become more concrete and specific. The package includes a series of spending provisions designed to help meet important national goals such as reducing child poverty, improving the human capital of our workforce, supporting workers, expanding health coverage, tackling climate change, and promoting equity across racial, ethnic, and gender lines. To help finance these investments, the package includes a series of revenue measures that require wealthy households and corporations to pay a fairer amount of tax, reduce the tax advantages of shifting profits overseas, and strengthen enforcement of the nation's tax laws. It also proposes higher taxes on tobacco and nicotine, which would lead to significant health benefits, as well as significant savings in health care.

The claim by some critics in recent weeks that the package would "cost" $3.5 trillion and thus is unaffordable is no longer credible because the Ways and Means bill shows that most or all of that amount would be offset. Those who believe the investments are too large regardless of whether they are paid for should specify which they would scale back or remove. Reducing the total size of the investments wouldn't make the package better for the nation if it means we accomplish less in critical areas. The debate should be about the merits of each investment and what the package is trying to achieve.

Similarly, those who seek to scale back the revenue increases should specify which of them — related to wealthy households, corporations, or filers not paying the taxes they owe — is more important to protect than to fund a specific investment, such as in child care, health care, or education.

This recovery legislation represents a historic opportunity not only to invest in broadening opportunity and making the nation more productive and more just, but also to start building a more equitable, sustainable, and adequate tax system. The Ways and Means revenue package would take important steps in this direction, and lawmakers should take further steps as the bill moves through the legislative process.