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Paying for a Strong Economy

Seven New Revenue Sources that Can Revitalize America and Reduce Financial Speculation

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Institute for Policy Studies (IPS-DC.org) strengthens social movements with independent research, visionary thinking, and links to the grassroots, scholars and elected officials. Since 1963 it has empowered people to build healthy and democratic societies in communities, the United States, and the world.

Wealth for the Common Good, a new project of the Institute for Policy Studies, is a campaign that mobilizes business leaders and wealthy individuals in support of public policies that promote shared prosperity and fair taxation.

The Working Group on Extreme Inequality (EXTREMEINEQUALITY.org) is coordinated by the Institute for Policy Studies and was formed to promote public policies to reduce the concentration of wealth and power – and promote investments in education, housing, and asset-building that broaden prosperity.

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Executive Summary

To address our nation's economic crisis and maintain our nation's fiscal health, we desperately need new sources of federal revenue. Without additional federal financial resources, we as a nation will either have to shortchange long-overdue investments in infrastructure, health, energy, and economic opportunity or leave an unsustainable debt to generations ahead.

The Institute for Policy Studies has identified a package of practical and politically viable policies that could raise the revenues we need. These policies would:

- Collect revenue from those with the greatest capacity to pay;
- Discourage financial speculation; and
- Strengthen the overall economy.

The Institute for Policy Studies, in the weeks and months ahead, will actively refine these policy proposals and solicit input and analysis.[1]

The Fiscal Endgame: Over $500 Billion in Potential Revenue

1. **Repeal tax breaks for households with annual incomes over $250,000:** $43 billion per year. President Obama, in his campaign, called for reversing the Bush tax cuts for households with incomes over $250,000.[2] Many high-income households, polling shows, voted for Barack Obama because they believed his policies will help restore our economic stability. These households see higher taxes on high incomes as fiscal medicine our nation needs to take.[3]

2. **Tax speculative financial transactions: $100 billion per year.** A modest tax on every transaction that involves the buying and selling of stock and other financial products — a penny, for instance, on every $4 traded — would both generate substantial revenue and, if calibrated to impose a stiffer burden on rapidly flipped investments, discourage economically reckless speculation. Several European countries already tax stock transactions.[4]

3. E**liminate the high-income tax preference for capital gains and dividends:** $95 billion per year. Current law subjects most dividend and capital gains income — the income that flows overwhelmingly to wealthier Americans — to a 15 percent tax rate. The tax on wage and salary income, by contrast, can run up to 35 percent. With carefully structured rate reform, we can end this preferential treatment while, at the same time, encouraging average families to engage in long-term investing.[5]

4. **Levy a significant estate tax on grand fortunes:** $40-60 billion per year. The estate tax, under current law, will expire in 2010, then revert to the 2000 status quo the following year. Congress needs to reform the estate tax in 2009 to avoid the confusion

this public policy roller coaster will create — and make sure that the fortunes amassed over recent decades do not escape taxation. This reform should put in place steeply graduated tax rates, with no tax at all on estates worth under $2 million, or $4 million for a couple. Such an approach would generate $40 billion a year immediately — while taxing no more than one of every 200 estates — and over $100 billion a year a decade from now.[6]

5. **Establish a recovery emergency tax rate on extremely high incomes:** $60-105 billion per year. High-income Americans currently face a top tax rate that runs less than half the top rate in effect over the half-century before 1981. Restoring a higher tax rate on high incomes could help finance our economic recovery. We are currently exploring two approaches to this restoration. The first would institute two new tax rates: a 50 percent rate on annual income over $5 million and a 70 percent rate on income over $10 million. These new rates would generate $105 billion a year.[7] A second approach would increase the top tax rate on incomes over $1 million by 10 percent for five years. This would generate an estimated $60 billion a year and $300 billion over five years.

6. **End overseas tax havens: $100 billion per year:** Individual American taxpayers are now annually evading between $40 and $70 billion in U.S. taxes through offshore tax dodges.[8] U.S. corporations use similar offshore schemes to evade another $30 billion per year. The Stop Tax Haven Abuse Act (S. 681) would curtail these activities and generate $100 billion from wealthy individuals and corporations that have been failing to pay their fair share of the nation's tax bill.[9]

7. **Eliminate subsidies for excessive executive compensation:** $18 billion per year. As taxpayers, we subsidize over-the-top management pay through a host of tax loopholes. Congress should close these loopholes, starting with immediate action to deny all corporations, not just companies getting bailout dollars, tax deductions on any executive compensation that runs over $500,000, or 25 times, the pay of a company's lowest-paid workers.[10]

Introduction

President Obama has set his aim on an ambitious goal. He seeks to make a major investment in America's future without drowning future generations in debt. We believe he can succeed — but only if his administration actively explores new sources of federal revenue.

Since the 1980s, lawmakers have chosen not to do this exploring. They have followed, instead, the path of least resistance. Rather than risk discomforting Americans of wealth and power, they have continued adding to the annual federal deficit — and the standing national debt — without considering the "revenue side."

The result? In the 2010 federal fiscal year, the national debt will top $12 trillion.

In some circumstances, a number that large would make societal sense. If that $12 trillion represented a good-faith effort to address short-term economic emergencies or invest in long-haul capital improvements, our debt would amount to a useful downpayment on a more secure economic future.

Unfortunately, most of the borrowing that has hiked our debt over the last decade has contributed little to our future economic viability. We have, as a result, maneuvered ourselves into a fiscal corner, with challenges coming at us from every direction. We currently face:

- An immediate economic crisis that requires borrowing for short-term stimulus;
- A crumbling public infrastructure that demands we start making long-delayed investments in our bridges and roads, our mass transit and schools;
- A health care crisis that calls for fundamental reforms and expanded coverage;
- An ecological crisis that will take the transitioning of our entire energy infrastructure to adequately address; and
- A global security crisis that necessitates more than shock-and-awe military responses.

We cannot afford, here early in the 21st century, to ignore any of these challenges. But we cannot afford to address them either — not as long as politics as usual rules any serious debate over new sources of revenue out of order. Our political refusal to consider the revenue side has created our current fiscal predicament. We won't escape this predicament until we reject the knee-jerk no-tax bromides of our recent past.

Criteria for Revenue Generation

We are now suffering through the worst economic downturn since the Great Depression. Any attempt to raise revenue by broadly raising taxes on the American people would, as virtually all observers agree, be coun-

terproductive. We need to encourage prudent consumption, not depress it. But taxes on the extremely wealthy do not depress the consumption the economy needs to thrive.

Higher taxes on the wealthy, in our current economic situation, would actually have a positive impact. Appropriately targeted, these taxes would dampen the speculative frenzy of the last several decades. Over these years, grand concentrations of private wealth have been the engines behind the high-risk, high-return speculation that fueled economic bubbles in technology, housing, and commodities. Reducing these grand concentrations of wealth will help discourage future economic bubbles.

By the same token, carefully targeting higher taxes on U.S. corporations that have hidden dollars overseas to game the tax system would also raise federal revenues and, at the same time, help strengthen our basic economic foundation.

Borrowing and Squandering vs. Taxing and Investing

Our federal government, since the turn of the century, has squandered hundreds of billions of borrowed dollars on tax cuts for the wealthy, militarized solutions to global problems, and massive bailouts for the Wall Street investment firms that created the current economic crisis.

President Obama, with his stimulus plan, is proposing to invest hundreds of billions of dollars in the overdue investments on public infrastructure, energy, education, and health care that our nation's future demands. We cannot just borrow to pay for these investments. We also need to tax — the top.

These seven proposals would do just that and, in the process, raise over $500 billion a year and over $3 trillion over the next five years:

1. Repeal tax breaks for households with annual incomes over $250,000: $43 billion per year.
2. Tax speculative financial transactions: $100 billion per year.
3. Eliminate the high-income tax preference for capital gains and dividends: $95 billion per year.
4. Levy a significant estate tax on grand fortunes: $60 billion per year.
5. Establish a recovery emergency tax rate on extremely high incomes: $60-105 billion per year.
6. End overseas tax havens: $100 billion per year.
7. Eliminate subsidies for excessive executive compensation: $18 billion per year.

An Analysis of the Individual Options

1. Repeal tax breaks for households with annual incomes over $250,000.

Revenue Potential: $43 billion

Description: During the 2008 presidential campaign, Barack Obama proposed repealing the Bush-era income, capital gains, and dividend tax breaks enacted for households with Adjusted Gross Income, or AGI, of $250,000 or more ($200,000 or more for individuals). This repeal would have a substantial impact on federal revenues, as this chart details:

These tax changes would affect only a small fraction of U.S. taxpayers. According to an October 2008 Citizens for Tax Justice analysis, only 2.5 percent of taxpayers will fall above the $250,000/$200,000 AGI threshold in 2009.[11]

Increasing taxes on the wealthiest Americans will not harm the economy. Increasing taxes on America's wealthiest will not reduce consumption. Even with higher tax rates, the wealthy will have the means to maintain their current lifestyles. And raising taxes on the wealthy will not result in job losses. Consumer demand, not the tax rate, drives hiring.[12]

2009-2010 Revenue Impact of the Obama Tax Proposal (in $billions)

Tax Change	2009	2010
Income Tax: Repeal 2001 income tax cuts for taxpayers with AGI above $250,000 ($200,000 for individuals) • Top tax bracket would rise from 35 percent to 39.6 percent • Second-highest tax bracket would rise from 33 percent to 36 percent • The tax bracket thresholds would be adjusted so that no married couple with AGI below $250,000, and no single filer with AGI below $200,000, would be affected.	$24.8	$37.3
Capital Gains and Dividend Tax: Repeal 2003 capital gains and dividend tax cuts for taxpayers with AGI above $250,000 ($200,000 for individuals) • Tax rate on capital gains and qualified dividends would rise from 15 percent to 20 percent	$18.2	$7.9
Totals	**$43.0**	**$45.2**

Source: Tax Policy Center, "Senator Barack Obama's Tax Proposals of August 14, 2008: Economic Advisers' Version (No Payroll Surtax), Impact on Tax Revenue, 2009-18," Table T08-192, http://www.taxpolicycenter.org/numbers/displayatab.cfm?DocID=1956

Obama's election demonstrates broad public support, even among the wealthy, for the idea that the wealthiest Americans should pay more. As a presidential candidate, Barack Obama pledged to raise taxes on households with incomes over $250,000 by reversing the 2001 and 2003 Bush tax cuts. A majority of these high-income individuals, 52 percent, still voted for him.[13]

For More Information

Robert Frank, "Why Wait to Repeal Tax Cuts for the Rich?" The New York Times, December 7, 2008.

Citizens for Tax Justice, "Only 2.5 percent of Taxpayers Would Lose Some of the Bush Income Tax Cuts under Obama's Tax Plan in 2009: State-by-State Figures," October 23, 2008.

2. Tax speculative financial transactions.

Revenue Potential: $60 - $100 billion

Description: The Wall Street meltdown has highlighted the widespread role that unproductive speculative investment has played over recent years. We can discourage this unproductive activity, while raising significant revenue, by imposing a small tax on financial transactions. A set of well-designed Financial Transactions Taxes (FTTs) of 0.5 percent or less, depending on the type of security traded, would discourage wasteful speculation while allowing long-term investment to continue with minimal distortion. Rep. Peter DeFazio (D-OR) has introduced a securities transaction tax in the U.S. House (H.R. 1068).[14]

Model: The British stock sales tax. The UK imposes a 0.5 percent stamp tax on each London Stock Exchange trade, with each party to the transaction assumed to pay 0.25 percent. The tax applies to all firms incorporated in the UK, regardless of where in the world the trade takes place. But this British stamp tax only applies to stock sales, an unfortunate loophole that leaves traders untaxed if they speculate on other assets, or even on stocks themselves via futures or options. By learning from the British experience, U.S. lawmakers could craft a more effective anti-speculation transaction tax. The current British tax annually raises £4 billion, the equivalent, in an economy the size of the United States, to about $40 billion. A U.S. transaction tax, with loopholes removed, could raise as much as $100 billion.

An effective FTT would be broadly based. The tax would cover all standardized financial assets, with varying tax rates scaled to the expected life of the asset. One recent proposal[15] envisions the following fee structure:

Stocks	0.5 percent of sale price
Bonds	0.01 percent per year until maturity
Futures	0.02 percent of notional value of underlying asset
Options	0.5 percent of premium paid for the option
Interest Rate Swaps	0.02 percent of asset value per year of the agreement
Credit Default Swaps	0.02 percent of asset value per year of the agreement

Why is the tax rate so modest? Part of the reason: The financial markets have become so huge that even a tiny tax rate can raise significant revenue. In addition, a small tax would discourage short-term speculation on tiny movements in security prices while imposing a negligible effect on long-term investment.

How can the revenue potential be accurately calculated? Our target revenue projection — between $60 and $100 billion a year — reflects trading volume for 1997, extrapolated to 2008, and adjusted to reflect an expected fall in trading volume in 2009 as a result of the economic downturn.[16]

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3. Eliminate the high-income tax preference for capital gains and dividends.

Revenue Potential: $80 - $100 billion

Description: Income from capital gains and dividends currently carries a lower rate than ordinary income. The basic capital gains and dividend tax rate runs 15 percent, while ordinary income can be taxed at rates as high as 35 percent. Taxing capital gains and dividends at the same rate as ordinary income, as was done in the late 1980s after the 1986 tax reform act, would make the tax code fairer and raise serious revenue.

The tax preference for capital gains fails the economic productivity test. A 1999 analysis by Leonard Burman, at that time deputy assistant secretary for tax analysis at the U.S. Treasury, found that the tax preference for capital gains is "more likely to depress economic productivity than improve it." Burman found that subsidizing capital gains through the tax code has little effect on the overall incentive to save, reduces tax revenues, and encourages wasteful and unproductive tax shelters designed to artificially convert other forms of income into capital gains.[17]

The 2003 cuts in the capital gains and dividend tax rates failed to deliver promised economic growth. The growth in GDP, wages, and salaries between 2003 and 2006 dropped below average for a post-World War II recovery. Economic growth after the 2003 cuts actually proved weaker than economic growth during the 1990s, when tax rates on capital gains and dividends ran higher.[18]

The tax preference for capital gains and dividends overwhelmingly benefits the wealthiest Americans. Capital gains and dividend income goes disproportionately to the wealthiest Americans. Not surprisingly, these wealthy Americans reap the benefits from our current preferential tax treatment for capital gains and dividend income. Last October, the Tax Policy Center reported that the top 1 percent of taxpayers receive 75 percent of these benefits. Individually, the top 1 percent average $91,469 in capital gains and dividend tax savings. For the top 0.1 percent, the average tax cut amounts to a whopping $616,071. Meanwhile, the bottom 80 percent of taxpayers receive only 4.4 percent of the benefit of lower tax rates on capital gains and dividends. Their average tax cut: only $58.[19]

Income earned from work ought to be taxed at the same rate as income earned from investments. The current tax preference for investment income means that a nurse making $50,000 a year can pay taxes at a marginal rate of 40 percent a year, after taking federal payroll as well as income taxes into account, while an investor making millions of dollars in dividends and capital gains pays taxes at only a 15 percent rate.

The tax preference for capital gains encourages speculation at the expense of real investment. As Nobel laureate Joseph Stiglitz has recently written, "Why should those who make their income by gambling in Wall Street's casinos be taxed at a lower rate than those who earn their money in other ways? Capital gains should be taxed at least at as high a rate as ordinary income. (Such returns will, in any case, get a substantial benefit because the tax is not imposed until the gain is realized.)"[20]

The recent financial crisis will depress potential revenue from higher tax rates on dividends and capital gains, but revenue should rise as the economy recovers. Citizens for Tax Justice has found that the lower rates on capital gains and dividends cost the U.S. Treasury $92 billion in 2005.[21] In 2007, the Tax Policy Center estimated that taxing capital gains and dividends as ordinary income would bring in $100 billion in 2009, and between $84 and $107 billion a year through 2017.[22] New estimates aren't yet available.

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4. Levy a significant estate tax on grand fortunes.

Revenue Potential: $40-60 billion per year.

Description: The future of the estate tax will likely be addressed in 2009. President Obama advocates freezing the estate tax at current 2009 exemption levels — $3.5 million and $7 million for a couple — and indexing these thresholds for inflation. Progressive alternatives would maintain a lower wealth exemption, at $2 million, and introduce a progressive rate structure, with steeper rates on larger estates.

Why action now? Under the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001, the federal estate tax will disappear totally in 2010. The entire Act then sunsets in 2011, restoring the estate tax to the year 2000 wealth exemption level — $1 million per spouse — and tax rate schedule. Since 2001, opponents of the estate tax have pushed for "permanent repeal," but have failed to win enough votes. All observers agree that Congress, for the sake of estate tax planning and predictability, needs to settle the estate tax future before 2010.

Why retain the estate tax? The estate tax remains our nation's only federal tax on inherited wealth. A century ago, President Theodore Roosevelt called for estate and inheritance taxes to slow the build-up of concentrated wealth in the hands of a few. The federal estate tax, enacted in 1916, has been in effect ever since. A reformed estate tax that takes a meaningful bite out of huge private fortunes would raise $1 trillion in revenue over the next decade, provide a powerful incentive for

charitable giving, and help reduce our nation's staggering inequalities in asset ownership.[23]

The estate tax, as Bill Gates Sr. has written, "is a means by which wealthy people pay back the society and the commonwealth that has made their wealth possible." Eliminating the estate tax — or gutting it with irresponsible reforms — would shift our nation's revenue obligations onto lower-income taxpayers and future generations.[24]

Most estate tax reform proposals now pending in Congress would undermine what our society needs from the estate tax. Most of the over dozen proposals to reform the estate tax currently before Congress are missing many of the valuable provisions from the pre-George W. Bush estate tax.[25] These provisions simplified estate planning and smoothed interactions between state and federal estate taxes. The current estate tax debate in Congress is operating at a level of abstraction that ignores the revenue consequences of estate tax rate and exemption changes. We urgently need legislation that retains an estate tax robust enough to both raise badly needed revenue and put a brake on America's ever more narrowly concentrated wealth.

Key Provisions of Progressive Estate Tax Reform

- **A wealth exemption at $2 million.** Setting the exemption at $2 million for individuals and $4 million for couples would freeze the wealth exemption at the 2008 level. At this level, only multi-millionaires and billionaires — who make up just one of every 200 decedents — would pay any estate tax.
- **Wealth exemption indexed to inflation.** The amount of wealth exempted should be indexed to inflation on an annual basis. This will reduce the need for legislation to revise the exemption level in the future.
- **Progressive rate structure.** Instead of the current flat estate tax rate, a graduated rate structure. The rate should be 45 percent for estates between $2 million and $5 million, 50 percent for estate values between $5 million and $10 million, and 55 percent for estates valued over $10 million. In practice, after deductions for charitable giving, the actual effective tax rate would be considerably lower.
- **Restoration of state credit.** Before 2001, the estate tax provided a credit, against federal estate tax liability, for state estate or inheritance taxes. Given this credit, almost all states had some form of estate or inheritance tax, often explicitly tied to the level of the federal credit. The 2001 law reduced and then repealed the credit. Since 2001, in about 27 states, inheritance and estate taxes have either expired automatically, because they were tied to the existence of the federal credit, or been repealed. Restoring the state credit would reduce federal estate tax revenue. But this step would encourage states to complement otherwise regressive state tax systems with a progressive estate tax.[26]
- **Administrative reforms.** Real legislation would simplify estate and gift tax planning by relinking the two taxes under uniform rules and by allowing a surviving spouse to

automatically acquire the unused estate tax credit of a deceased spouse.

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"Spending Millions to Save Billions: The Campaign of the Super Wealth To Kill the Estate Tax" by Conor Kenny and Chuck Collins, Public Citizen and United for a Fair Economy (April 2006). http://www.citizen.org/documents/EstateTaxFinal.pdf

5. Establish a recovery emergency tax rate on extremely high incomes: $60-105 billion per year.

Revenue Potential: $60 - $100 billion, depending on the rate schedule

This emergency tax rate hike could take several different forms. We detail two approaches here.

Proposal 1: Set two new top tax rates.

- A 50 percent rate on annual income from $5 million to $10 million.
- A 70 percent rate on income over $10 million.
- Number of households impacted: 38,410.
- Share of U.S. households impacted: 0.03 percent (3 out of 1,000).
- Estimated revenue in 2008: $105 billion. (Source: Institute on Taxation and Economic Policy Tax Model, May 2007, preliminary)

Proposal 2: Establish a five-year, 10 percent surtax on million-dollar incomes. Last October, Senator Bernie Sanders (I-VT) introduced an amendment to the Wall Street bailout legislation that would have imposed a five-year, 10 percent surtax on couples making more than $1 million a year and individuals making more than $500,000. The surtax, noted Sanders, would raise $300 billion over five years, or $60 billion a year.[27]

The public supports the idea that the wealthy should pay more in taxes at a time to help the economy recover. The Sanders proposal for a five-year surtax on million-dollar incomes drew 48,000 citizen co-signers on his Web site in less than a week.

Since World War II, the effective tax rate on the wealthiest Americans has fallen dramatically. In 1943, with the top statutory tax rate at 88 percent, the 25,000 highest-income Americans paid 68 percent of their total incomes in tax. The top rate the next year went to 94 percent. In 1967, with the top marginal rate at 70 percent, the effective tax rate on the top 25,000 American incomes stood at 41 percent. By 2004, the top statutory rate had dropped to just 35 percent, resulting in a mere 22 percent effective rate on the top 25,000.[28]

Taxes on the wealthy can be safely raised, even in an economic downturn, without hurting economic growth. During most of the heyday of American middle class prosperity, in the mid 20th century, the tax rate on income in the nation's highest-income bracket hovered around 90 percent. These high rates on high incomes went hand-in-glove with the most rapid economic growth rates in U.S. history. Recessions in these years never produced deep social dislocations, and recovery always came quickly and fully.

Millionaires benefited during the Wall Street boom. Now taxpayers are picking up the tab for the Wall Street bust. The question becomes: Which taxpayers should bear the biggest burden, the wealthy taxpayers who spent the Bush years benefiting from one tax cut after another, or the middle-income families who saw little tax relief in the Bush years and watched their median incomes fall?

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Office of Senator Bernie Sanders, "Make Wall Street Pay for Bailout," October 1, 2008.

6. End overseas tax havens.

Revenue Potential: $70 - $100 billion

The Senate Permanent Subcommittee on Investigations, chaired by Sen. Carl Levin (D-MI) reports that affluent Americans now have over $1 trillion in assets offshore and annually evade between $40 and $70 billion in U.S. taxes each year through offshore tax dodges.[29] U.S. corporations, meanwhile, go offshore to evade another $30 billion in taxes each year. Thanks in part to these evasions, the Government Accountability Office reported last August, two-thirds of U.S. corporations paid no income taxes between 1998 and 2005.[30]

Overseas tax havens generate a significant portion of the annual "tax gap" — the billions of dollars of taxes that are owed but not paid each year. The latest estimate for the tax gap: $345 billion in unpaid taxes each year owed by individuals, corporations, and other organizations eager to shift their tax obligations onto the backs of honest taxpayers.[31]

"Tax haven banks" enable tax cheats to hide assets from U.S. authorities. In July 2008, the Senate Permanent Subcommittee on Investigations released a 115-page joint staff report detailing how tax haven banks, including LGT Bank in Liechtenstein and UBS Bank in Switzerland, help U.S. taxpayers evade taxes, mainly by enabling their U.S. clients to open accounts offshore, then structuring these accounts to avoid disclosure to U.S. authorities.[32]

Financial institutions also enable foreign taxpayers to evade taxes on U.S. stock dividends. Last September, the Senate Permanent Subcommittee on Investigations released a 77-page joint staff report finding that U.S. financial institutions, including Lehman Brothers, Morgan Stanley, Merrill Lynch, and Citigroup, developed and marketed divided-dodging products for their foreign clients.[33]

In February 2007, Sen. Levin introduced legislation, the Stop Tax Haven Abuse Act (S. 681) — along with co-sponsor Barack Obama — that would curtail these offshore tax havens.

For More Information

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7. Eliminate subsidies for excessive executive compensation.

Revenue Potential: $18 billion

Description: Top U.S. CEOs benefit from an array of tax loopholes that cost taxpayers on the order of $18 billion per year. Closing those loopholes would restore some fairness to the tax code and raise significant revenue.

The good news: The bailout has already eliminated a $2 billion subsidy for excessive executive pay. The Emergency Economic Stabilization Act of 2008 closed a loophole that allowed hedge fund managers to defer massive amounts of compensation in accounts set up by offshore subsidiaries.[34]

Current Tax Subsidies for Excessive Executive Pay

1. **Preferential capital gains treatment of carried interest.** Estimated annual cost: $2.7 billion.[35] Private investment fund managers pay a 15 percent capital gains tax rate on the profit share — the "carried interest" — they get paid to manage investment funds they do not own. If this income were taxed as ordinary income, the rate would be 35 percent. In November 2007, the House passed a tax reform bill that would have closed this loophole (H.R. 3996), but the Senate failed to take up the matter. Taxing capital gains as ordinary income, as proposed above, would have the same impact as ending this preferential treatment for carried interest income.

2. **Unlimited deferred compensation. Estimated annual cost: $80.6 million.**[36] CEOs at large companies shield unlimited amounts of compensation from taxes through special deferred accounts. By contrast, ordinary taxpayers face strict limits on how much income they can defer from taxes via 401(k) plans. In 2007, the Senate passed a measure that would have limited annual executive pay deferrals to $1 million (S. 349), but the measure stalled in conference committee deliberations.

3. **Unlimited tax deductibility of executive compensation. Estimated annual cost: $5.2 billion.**[37] Corporations can currently deduct from their income taxes all the millions they shell out for executive compensation, so long as they define these millions as incentives. The Emergency Economic Stabilization Act of 2008 does set a $500,000 annual cap for the tax deductibility of executive pay at bailed-out firms. The pay restrictions in the bailout also deny participating companies the loophole that lets companies deduct unlimited sums for "performance-based" pay. Lawmakers now need to extend these reforms throughout the corporate economy. The Income Equity Act, legislation championed by Rep. Barbara Lee (D-CA), would cap the amount of pay that corporations can deduct from their taxable income at $500,000 or no more

than 25 times the pay of a firm's lowest-paid worker.

4. **Stock option accounting double standard. Estimated annual cost: $10 billion.**[38] Accounting rules value stock options on their grant date, while the tax code values stock options on the day that executives decide to cash them in. The two numbers rarely match, and in recent years, the actual "in-the-pocket" value has been significantly higher than the grant date estimate. As a result, companies can lower their tax bill by claiming deductions for options-related costs that are much higher than what they report in their financial statements. Senator Levin has introduced legislation that would require the federal corporate tax deduction for stock option compensation to be the same as the expense shown on corporate financial reports filed with the SEC.

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Notes

1. Our new project, Wealth for the Common Good, brings together business leaders and high net worth individuals to advocate for prudent and progressive tax policies.
2. Robert Frank, "Why Wait to Repeal Tax Cuts for the Rich?" *The New York Times*, December 7, 2008. http://www.nytimes.com/2008/12/07/business/07view.html?_r=1&scp=2&sq=Robert percent20Frank&st=cse. In January 2008, the Tax Policy Center estimated retaining the top rate cuts for incomes over $250,000 would cost $43 billion in revenue in 2009 and $45 billion in 2010.
3. Mark Penn, "Most affluent voters key to Obama sweep," *Politico*, November 11, 2008. http://www.politico.com/news/stories/1108/15471.html
4. See Dean Baker, "The Benefits of a Financial Transaction Tax," Center for Economic and Policy Research, December 2008. http://www.cepr.net/index.php/publications/reports/the-benefits-of-a-financial-transactions-tax/ Also see: Robert Pollin, Dean Baker, Marc Schaberg, "Securities Transaction Taxes for U.S. Financial Markets," *Eastern Economic Journal*, Vol. 29, No. 4, Fall 2003.
5. Citizens for Tax Justice, "Capital Gains and Dividends Tax Cuts Offer Almost No Benefit to Middle-Income Americans and Add to the Nation's Fiscal Problems," May 13, 2008. http://www.ctj.org/pdf/capgainsdivtaxcuts.pdf
6. See "Sensible Estate Tax Act" (HR 6499) introduced by Rep. Jim McDermott, http://www.govtrack.us/congress/bill.xpd?bill=h110-6499. Also see: Citizens for Tax Justice, "Latest State-by-State Data Show Why Obama Should Scale Back His Proposal to Cut the Federal Estate Tax." December 3, 2008. http://www.ctj.org/pdf/estatetax20081203.pdf
7. Estimates prepared by Citizens for Tax Justice for the Working Group on Extreme Inequality. See: http://extremeinequality.org/wpcontent/uploads/Extreme_Ineq_PP2008.pdf
8. See, e.g., Joseph Guttentag and Reuven Avi-Yonah, "Closing the International Tax Gap," in Max B. Sawicky, ed., Bridging the Tax Gap: Addressing the Crisis in Federal Tax Administration (2006), as noted in the U.S. Senate Permanent Subcommittee on Investigations, Staff Report on Dividend Tax Abuse: How Offshore Entities Dodge Taxes on U.S. Stock Dividends, September 11, 2008. http://levin.senate.gov/newsroom/supporting/2008/091108DividendTaxAbuse.pdf
9. Permanent Subcommittee on Investigations, Senate Committee on Homeland Security and Government Affairs, August 2006. http://levin.senate.gov/senate/investigations/index.html
10. "Executive Excess 2008: How Average Taxpayers Subsidize Runaway Pay," August 25, 2008. http://www.ips-dc.org/reports/#623
11. Citizens for Tax Justice, "Only 2.5 percent of Taxpayers Would Lose Some of the Bush Income Tax Cuts under Obama's Tax Plan in 2009: State-by-State Figures," October 23, 2008. http://www.ctj.org/pdf/obamathreshold.pdf
12. Robert Frank, "Why Wait to Repeal Tax Cuts for the Rich?" *The New York Times*, December 7, 2008. http://www.nytimes.com/2008/12/07/business/07view.html?_r=1&scp=2&sq=Robert percent20Frank&st=cse
13. Mark J. Penn, "Most Affluent Key to Obama Sweep," Politico.com, November 11, 2008. http://www.politico.com/news/stories/1108/15471.html
14. Representative Defazio's bill is called "Let Wall Street Pay for Wall Street's Bailout Act of 2009," HR 1068. http://www.govtrack.us/congress/bill.xpd?bill=h111-1068

15. Dean Baker, "The Benefits of a Financial Transaction Tax," Center for Economic and Policy Research, December 2008. http://www.cepr.net/index.php/publications/reports/the-benefits-of-a-financial-transactions-tax/; See also Pollin, R., D. Baker, and M. Schaberg, 2002. "Financial Transactions Taxes for the U.S. Economy," Political Economy Research Institute. http://www.peri.umass.edu/236/hash/aef97d8d65/publication/172/
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20. Joseph Stiglitz, "Scarcity in an Age of Plenty," *The Guardian* (UK), June 15, 2008 http://www.guardian.co.uk/commentisfree/2008/jun/15/economics.food.
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27. "Sanders Amendment: Make Wall Street Pay for Bailout," Senator Bernie Sanders press release, October 1, 2008. http://www.sanders.senate.gov/news/record.cfm?id=303940
28. From AFL-CIO, Institute for Policy Studies, Center for Corporate Policy and Essential Information, Extreme Inequality: Starting a Strategic Discussion, rev. June 9, 2008: Actual share of income taxed, 25,000 highest-income Americans. Source: For 2004 tax data, Internal Revenue Service Statistics of Income Tax Stats: Individual Statistical Tables by Size of Adjusted Gross Income. http://www.irs.gov/taxstats/indtaxstats/article/0,,id=96981,00.html; For the 1943 data, Fritz Scheuren and Janet McCubbin, Individual Income Tax Shares and Average Tax Rates, 1916-1950, *Statistics of Income Bulletin*, Volume 8, Number 3, Winter 1988-89; For the 1967 data, Janet McCubbin and Fritz Scheuren, Individual Income Tax Shares and Average Tax Rates, 1951-1986, *Statistics of Income Bulletin*, Volume 8, Number 4, Spring 1989;The "top 25,000" figures round off actual average rates paid by the highest 23,730 incomes in 1943, the highest 27,066 in 1967, and the highest 24,440 in 2004.

29. See, e.g., Joseph Guttentag and Reuven Avi-Yonah, "Closing the International Tax Gap," in Max B. Sawicky, ed., *Bridging the Tax Gap: Addressing the Crisis in Federal Tax Administration* (2006), as noted in the U.S. Senate Permanent Subcommittee on Investigations, Staff Report on Dividend Tax Abuse: How Offshore Entities Dodge Taxes on U.S. Stock Dividends, September 11, 2008. http://levin.senate.gov/newsroom/supporting/2008/091108DividendTaxAbuse.pdf
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32. Office of Sen. Carl Levin, "Permanent Subcommittee on Investigations Issues Report on Tax Haven Banks Hiding Billions from the IRS," July 17, 2008. http://levin.senate.gov/newsroom/release.cfm?id=300844
33. Office of Sen. Carl Levin, "Permanent Subcommittee on Investigations Issues Report on Major Banks Helping Non-U.S. Clients Dodge U.S. Dividend Taxes," September 11, 2008. http://levin.senate.gov/newsroom/release.cfm?id=302807
34. The new section, 457A, will (1) largely terminate future deferrals under nonqualified deferred compensation programs maintained by offshore hedge funds and other entities and (2) require the pay-out of existing deferrals from such entities within the next 10 years.
35. Joint Committee on Taxation, JCX-105-07, October 31, 2007. http://www.house.gov/jct/x-105-07.pdf (See p. 5, line for "income of partners for performing investment management services treated as ordinary income received for performance of services.")
36. Democratic Policy Committee (press release) January 23, 2007. http://dpc.senate.gov/dpc-new.cfm?doc_name=lb-110-1-11. Note: The 10-year projected revenue figure was divided by 10 to obtain an annual cost to taxpayers.
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38. Senate Committee on Homeland Security and Governmental Affairs (press release), September 28, 2007. Note: Levin based his estimate on partial-year numbers for 2004 that were considerably lower than the IRS findings for 2005. This report uses the high-end estimate. http://hsgac.senate.gov/public/index.cfm?Fuseaction=PressReleases.View&PressRelease_id=661bf7cc-b067-4cf4-a02a-136ed7ed9160&Affiliation=R