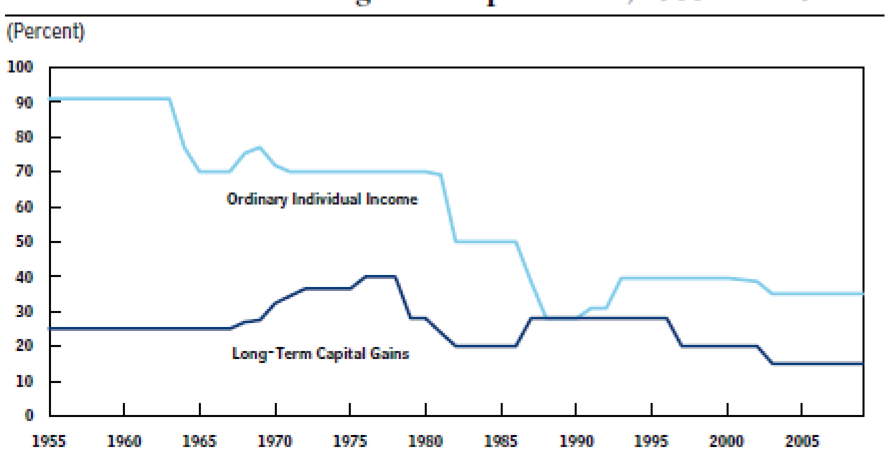
Tax income from wealth at the same rate as income from work: $918 billion over 10 years

The Idea: Currently, profits from the sale of stocks, bonds, real estate, and other assets – also known as capital gains – can only be taxed at 15 percent on every dollar, while the highest tax rate for wages is 35 percent. If capital gains were taxed at the same rate as wages and salaries, the country could raise roughly $918 billion[1] over the next 10 years.

The Rationale: Between the establishment of the federal income tax in 1913 and 1921, the government taxed income from wealth at the same rate as earned income. In 1918, the highest tax rate was at 77 percent for all income, regardless of source. However, in 1922, the government began taxing income from wealth at a lower level than earned income, reducing the top wealth tax rate to 12.5 percent. In the early 1940s, the capital gains tax rate was raised to 25 percent, and in the 1970s, the top rate went up to 39.9 percent. Then Congress began cutting the rates. In the 1980s, in Ronald Reagan's second term, income and wealth were both taxed at 28 percent; President Clinton reduced the capital gains rate to 20 percent, and George W. Bush reduced the capital gains tax rate to the exceptionally low level of 15 percent, almost to its 1922 rate when the bulk of federal tax receipts came from excise taxes.

Maximum Statutory Marginal Income Tax Rates on Ordinary Individual Income and Long-Term Capital Gains, 1955 to 2009



Sources: Department of the Treasury, Internal Revenue Service and Office of Tax Analysis.

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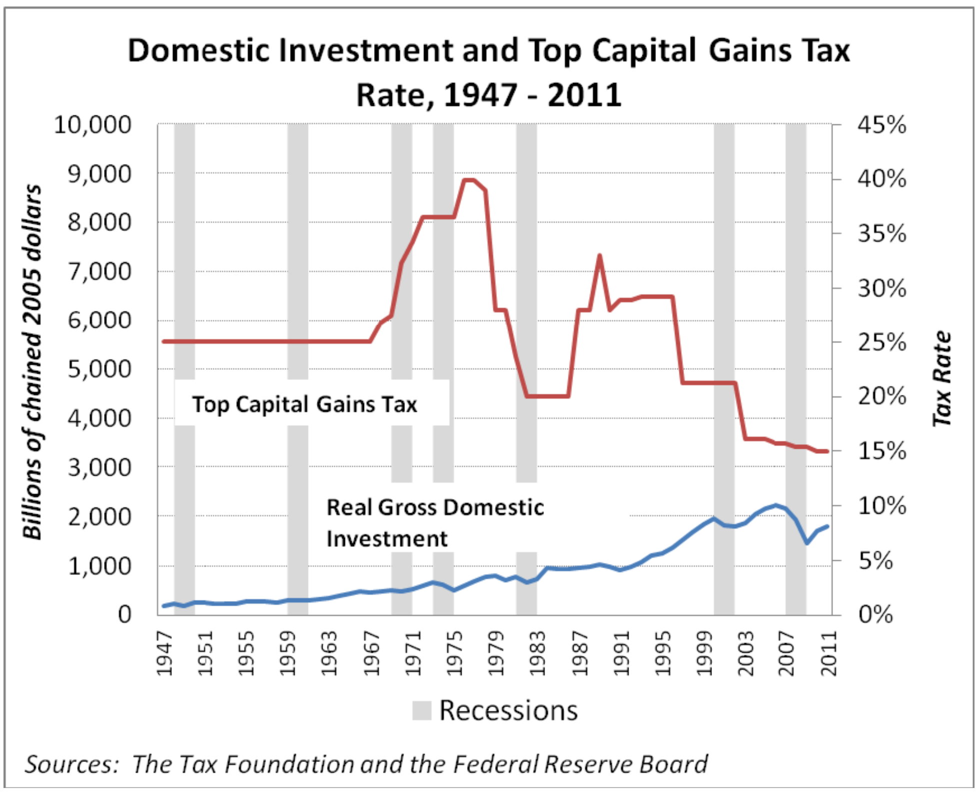
Proponents of raising the capital gains tax argue that it would increase fairness: why should someone earning $100,000 in salary pay more taxes than someone receiving $100,000 in stock dividends? And since it is the wealthy who disproportionately rely on income from stocks and bonds, a low capital gains tax rate means lower-income people are paying more in taxes than higher-income individuals.

Those who want to keep lower taxes on the profits from trading argue that lower taxes on investors increases investment dollars and will stimulate the economy. However, as the following graph (and other evidence) shows, there is little correlation between domestic investment and low tax rates on capital gains. Real domestic investment had been growing steadily when the capital gains tax was at 39.9 percent and fell during the period when the rate was 15 percent.



Support for the idea: Recent polls show a majority of the public approves of taxing capital gains as ordinary income. Warren Buffet, one of the wealthiest men on the planet, who makes his fortune from capital gains, has famously said that his tax rate should not be lower than his secretary's. President Obama would raise the capital gains rate back to 20 percent. However, neither has called for taxing capital gains at parity with earnings.

Of the plans reviewed for this revenue project, the following support raising capital gains tax rates: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *First Step* and *Budgeting for Growth*, Andy Stern's *21st Century Plan*, the Institute for America's Future *Citizens' Commission*, the National Commission on Fiscal Responsibility's *Moment of Truth*, Rep. Jan Schakowsky's *Deficit Reduction Plan*, Steven Peralstein's *Deficit Reduction Op-Ed*, Joseph Stiglitz's *Principles and Guidelines for Deficit Reduction*, Citizens for Tax Justice's *Policy Options*, Comeback America's *Restoring Fiscal Sanity*, the Congressional Progressive Caucus' *People's Budget*, the Bipartisan Policy Center's *Restoring America's Future*, and the Congressional Black Caucus' *The Responsible Path*.

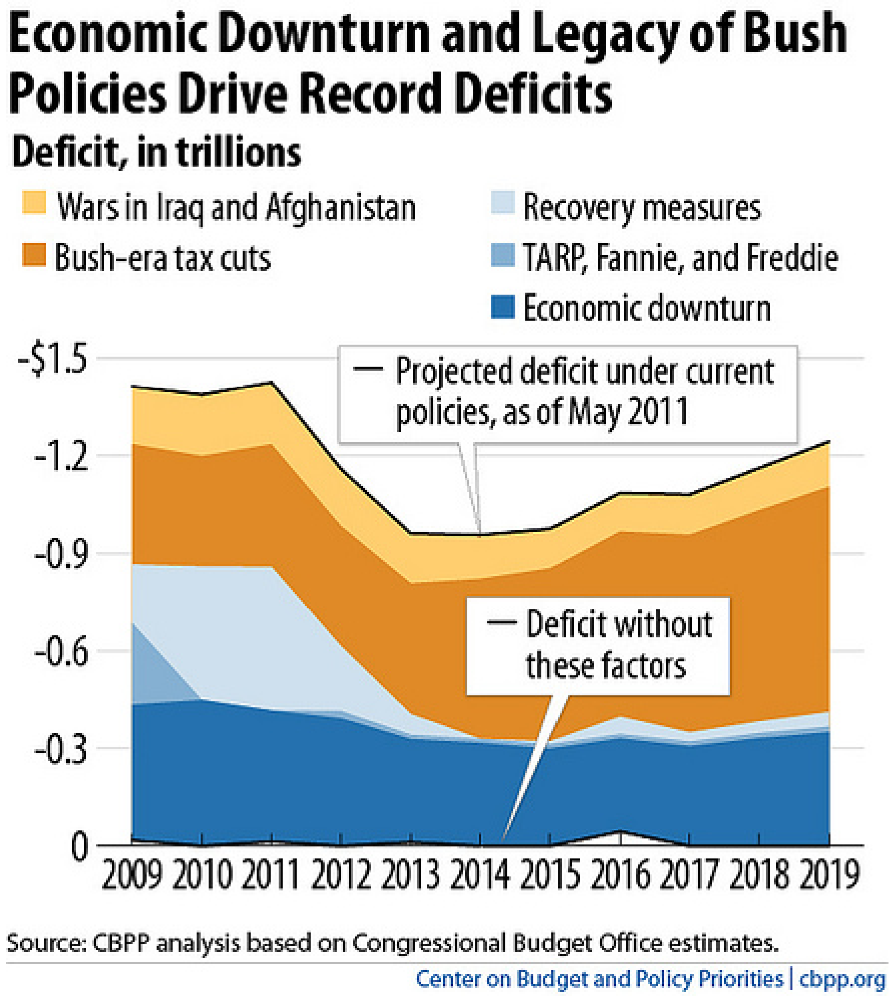
[1]*Investing in America's Economy*, Our Fiscal Security, pg. 31-2.

Repeal Bush tax cuts for upper-income households: $849 billion over 10 years

The Idea: In 2000, the federal government had a surplus of $236 billion, but over the next ten years the Bush tax cuts for the rich helped plunge the nation into debt. If Congress were to repeal a number of the tax benefits for upper-income households from the Bush tax cuts, the nation could raise roughly $849 billion[2] over the next 10 years. This would include reinstating the limitation on itemized deductions for upper-income taxpayers, which would bring in $123 billion; reinstating the personal exemption phase-out, which would bring in $42 billion; and reinstating the 36 and 39.6 percent income tax rates, which would bring in $442 billion. It would also include taxing qualified dividends as ordinary income for upper-income taxpayers, which would bring in $206 billion, and taxing net long-term capital gains at 20 percent for upper-income taxpayers, which would bring in $36 billion.

The Rationale: A 1993 tax reform package raised the tax rate on households earning over $250,000 from 31 percent to 39.6 percent and added a 36 percent bracket for households with incomes between $140,000 and $250,000. Strong economic growth throughout the 1990s and this deficit reduction package paved the way for budget surpluses in 1998, 1999, 2000, and 2001. Economists projected the surplus would eliminate the national debt entirely by 2010.

Instead, President George W. Bush reduced the top two tax rates to 33 percent and 35 percent. The Bush tax cuts were a major contributor to current budget deficits and the national debt. These tax cuts disproportionately benefited the wealthy: in 2010, a family with an income of $500,000 received about $25,200 in tax breaks; a family with an income of $50,000 received $1,400 in tax breaks under the combined effects of the 2001 and 2003 tax cuts.



If all the Bush-era tax cuts, including the middle-income cuts, were repealed, the deficit would be lowered by $3.7 trillion over ten years.

Support for the Idea: President Obama has repeatedly called for Congress to abolish the upper-income tax cuts. However, the cut-off point has been a point of contention. Some only want to tax those with incomes over $1 million (see the millionaires surtax) while others propose a return to 1993 tax rates, which today would cover families earning more than $200,000 a year, or less than three percent of taxpayers.

At the end of 2012, tax rates on all Americans are scheduled to revert to their 2001, or pre-Bush tax cut, levels. Of the plans reviewed for this revenue project, the following support restoring 2001 income tax rates on high-income households: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *First Step*, the House Democratic

2012 budget, the Institute for America's Future *Citizens' Commission*, President Obama's *2012 budget* and *Living within Our Means*, and the Congressional Progressive Caucus' *People's Budget*. Two plans propose to repeal immediately the top two Bush tax rates and allow the remaining Bush tax cuts to expire in 2012: the Congressional Progressive Caucus' *People's Budget*, and Comeback America's *Restoring Fiscal Sanity*.

[2] *President Obama's Fiscal Year 2013 Budget*, Office of Management and Budget, Summary Tables, pg. 219-20.

Tax the sales of stocks, bonds, options, futures, and other financial products: $391 billion to $1.8 trillion over 10 years

The idea: A financial transactions tax (also known as a financial speculation tax) is a tiny tax placed on the trading of Wall Street financial instruments, including stocks, bonds, derivatives, futures, options, and credit default swaps. If Congress enacted a financial speculation tax, the country could raise between $391 billion[3] to $1.8 trillion[4] over the next 10 years, depending on which financial products are taxed at what rates. Several financial transactions tax proposals exist. One would tax stocks at $3 on every $10,000 traded, exempting pensions, mutual funds, education savings accounts, health savings accounts, and individual retirement accounts. Another proposal would tax all financial products at different rates ($50 per $10,000 stocks traded to $1 per $10,000 on bonds, and other products in between). The first would raise an estimated $391 billion in revenues over 10 years, while the latter could raise more than $1.8 trillion over 10 years.

The rationale: A financial transactions tax would increase tax fairness. Most goods and services are taxed at point of sale. There is no reason to exempt stocks and bonds from sales taxes. In fact, the United States had a financial speculation tax in place between 1914 and 1966, when the federal government levied a tax of $2 on every $10,000 on all sales or transfers of stock. In 1932, Congress more than doubled the tax to help financial recovery and job creation during the Great Depression. Even today, the government levies an infinitesimal financial transactions tax on stocks that is used to finance the Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), and other financial regulatory agencies. Because of the high volume of trading on the New York stock exchange, the transactions tax can produce a large stream of revenue.

The financial transactions tax could help reduce speculative trading. The tax falls most heavily on high-volume, high-speed trading, discouraging short-term speculation in financial markets and the proliferation of ever more complex financial products. By

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reducing the profitability of complex, short-term trading, the tax could encourage Wall Street to put more money into longer-term investments in the real economy.
At least 29 countries – including Australia, Hong Kong, Switzerland, and the U.K. – levy some form of a financial transactions tax. International financial regulatory bodies have recommended establishing a financial speculation tax.

This tax would also address the larger issue of Wall Street's responsibility for the Great Recession. Since ethically and legally questionable practices by large banks and trading companies were largely responsible for the financial meltdown in 2008-2009 that cost the American economy eight million jobs and is the principle cause of the immediate revenue contraction, many consider it appropriate that the financial sector contribute more to rebuilding the economy.

Support for the idea: A growing number of economists and business, financial, and political leaders support the idea, including Warren Buffett, Bill Gates, John Bogle (founder of the Vanguard Group), Paul Volcker, and David Stockman, and Nobel Prize-winning economists James Tobin, Joseph Stiglitz, and Paul Krugman also support the idea; a majority of Americans support the idea when it is explained to them.

Several members of Congress have introduced legislation over the last two sessions to enact various forms of a financial speculation tax. Sen. Tom Harkin (D-IA) and Rep. Peter DeFazio (D-OR) introduced the "Wall Street Trading and Speculators Tax Act," which proposes a 0.03 percent tax on stock, bond, and derivative trades. Rep. Peter Stark (D-CA) introduced the "Investing in Our Future Act of 2011," which applies a tax of 0.005 percent on currency transactions and directs the revenues to childcare, global health, and climate change. DeFazio also introduced the "Taxing Speculators out of the Oil Market Act," which places a 0.01 percent tax on transactions in oil futures, options, and swaps.

Of the plans reviewed for this revenue project, the following plans support enacting a financial transaction tax: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *Budgeting for Growth*, Andy Stern's *21st Century Plan*, Institute for America's Future *Citizens' Commission*, Congressional Black Caucus' *The Responsible Path*, Congressional Progressive Caucus' *The People's Budget*, Comeback America's *Restoring Fiscal Sanity*, and Joseph Stiglitz's *Principles and Guidelines for Deficit Reduction.*

[3]Joint Committee on Taxation, Memorandum, Rep. Peter DeFazio (D-OR).
[4]*The Deficit-Reducing Potential of a Financial Speculation Tax*, Center for Economic and Policy Research, pg. 3.

Enact a 5 percent surtax on millionaires: $461 billion over 10 years

The Idea: To tax those who have benefited the most from the American economic system during this difficult period, some have argued for a five percent surtax on incomes over $1 million per year. If no other changes in the tax code were made, this would increase the top tax rate for millionaires to 40 percent, rather than the current 35 percent rate. Such a tax would raise roughly $461 billion[5] over the next 10 years, helping to pay for important investments in the nation.

The Rationale: Over the last 30 years, the income of the wealthiest one percent of households in the U.S. increased by over 220 percent, while the incomes of those in the bottom 90 percent of the income distribution grew by just five percent. As the pre-tax income of those at the top rose dramatically, steep declines in their income tax rates left them with a huge windfall. As a result, income inequality is rapidly increasing. A surtax on those earning over $1 million would help slow this trend.

Although the current tax code does ask more of the wealthy than of lower-income families, it doesn't distinguish between millionaires, multi-millionaires, and billionaires. A family earning $50 million a year will only have a slightly higher average tax rate than a family making $500,000, even though the first family's income is one hundred times as high.

Support for the Idea: An activist group, Patriotic Millionaires, is pushing for increased taxes for millionaires.

Several members of Congress have introduced legislation over the last two sessions to enact a surtax on millionaires. Sen. Bernie Sanders (I-VT) introduced the "Emergency Deficit Reduction Act," which would impose a 5.4 percent surtax on individual taxpayers whose modified adjusted gross income exceeds $1 million ($2 million in the case of a joint return). Sen. Harry Reid (D-NV) introduced the "American Jobs Act of 2011," which would impose a 5.6 percent surtax on adjusted gross income above $1 million. Sens. Robert Menendez (D-NJ) and Amy Klobuchar (D-MN) have both introduced legislation to impose a five percent surtax on adjusted gross income above $1 million.

Currently, there are more millionaires in the House and Senate than ever before.

Of the plans reviewed for this revenue project, the following support enacting some form of a high-income surtax: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *First Step* and *Budgeting for Growth*, the Congressional Black Caucus' *The Responsible Path*, the Institute for America's Future *Citizens' Commission*, Andy Stern's *21st Century Plan*, and the Congressional Progressive Caucus' *People's Budget*.

[5] *Investing in America's Economy*, Our Fiscal Security, pg. 40-1.

Limit the deductions higher-income households can claim on tax returns to 28 percent ($584 billion), or to 15 percent ($1.2 trillion)

The Idea: Wealthy households use itemized tax deductions to reduce their tax bills each year. If Congress were to limit the amount of the deductions that higher-income households can use to reduce from their tax bills to 28 percent of their overall income, the country could raise $584 billion[6] in revenues over the next 10 years while increasing tax fairness. But, limiting the amount of itemized deductions to 15 percent would bring in $1.2 trillion[7] over 10 years.

The Rationale: When filing a tax return, a household may subtract, or deduct, some expenses (including gifts to charity and state and local taxes) from the income on which they must pay federal taxes. These itemized deductions essentially shield a certain amount of income from taxation, thus lowering the taxes owed (assuming the total deductions are worth more than the standard deduction). But because of the graduated tax rates, the more money you make and the higher your tax rate, the more beneficial itemized deductions become. Capping the amount of itemized deductions allowed would increase tax fairness.

For example, if a middle-income family earning $65,000 contributed $100 to a favorite charity or church, the family would save $15 from its tax bill. But a family earning enough to be in the 35 percent tax bracket could save $35 of every $100 given to the charity or church of its choice.

Take the largest itemized deduction that most people take: the home mortgage deduction. The table below shows that a family in the 15 percent tax bracket (with an income of $65,000) paying $10,000 a year in interest on their mortgage would be able to shield $10,000 of income from taxation, providing them with $1,500 in subsidy (15 percent of $10,000). A wealthy family paying the 35 percent tax rate paying the same mortgage interest of $10,000 would receive $3,500 in subsidy. But wealthy people generally have bigger homes and larger mortgages. For a wealthy family, mortgage interest of $40,000 would net $14,000 in tax subsidies.

The upside-down effect of the mortgage interest deduction

	Middle-income household	High-income household
Income	$65,000	$500,000
Tax bracket	15 percent	35 percent
Mortgage interest paid	$10,000	$40,000
Current value of subsidy for mortgage interest	$1,500 (15 percent of interest paid)	$14,000 (35 percent of interest paid)
Value of subsidy for mortgage interest under Obama proposal on itemized deductions	$1,500 (15 percent)	$11,200 (28 percent)

Chart: Center for American Progress

The result is that higher-income households receive a larger benefit from itemizing their income taxes. At the same time, this policy costs the U.S. Treasury significant amounts of lost revenue each year.

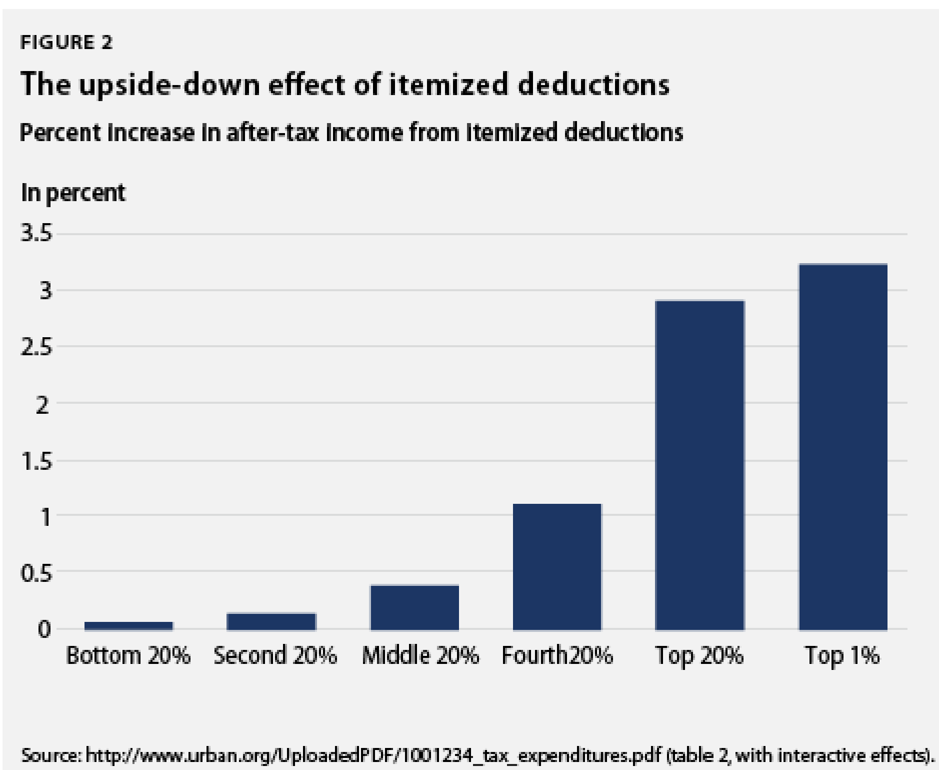

Chart: Center for American Progress

Support for the idea: The president has proposed capping the value of itemized deductions for high-income families at 28 percent. The Office of Management and Budget (OMB) estimates that this would raise about $584 billion in revenue over the next ten years. Tougher limits on itemized deductions would result in even greater savings. A plan that would limit itemized deductions to 15 percent would bring in $1.2 trillion in additional revenue over the next ten years.

Of the plans reviewed for this revenue project, the following proposed either limiting itemized deductions or eliminating them altogether: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *Budgeting for Growth*, Esquire's *Commission to Balance the Federal Budget*, the Institute for America's Future *Citizens' Commission*, President Obama's *2012 budget* and *Living within Our Means*, Rep. Mike Quigley's *Reinventing Government*, Andy Stern's *21st Century Plan*, Stephen Pearlstein's *Deficit Reduction Op-Ed*, the Bipartisan Policy Center's *Restoring America's Future*, the National Commission on Fiscal Responsibility's *Moment of Truth*, and the Congressional Progressive Caucus' *People's Budget*.

[6] *President Obama's Fiscal Year 2013 Budget*, OMB, Summary Tables, pg. 220.
[7] *Reducing the Deficit: Spending and Revenue Options*, Congressional Budget Office, pg. 151-2.

Reform the corporate tax code to eliminate two tax breaks: $404 billion over 10 years

The Idea: Corporate tax expenditures are rules in the tax code that essentially give some corporations tax breaks or subsidies. Eliminating just two key corporate tax expenditures - one that allows firms to deduct the costs of capital improvement quickly and another that subsidizes firms producing goods and services in the U.S. - could raise $404 billion[8] in revenues over the next 10 years.

The Rationale: Tax expenditures are tax breaks that cost the federal government revenue and have shifted the cost of government away from corporations to payroll taxes and individual income taxes. They seriously erode tax fairness by giving special breaks to firms in some industries or regions and not others and by giving preferential tax treatment to corporations that are able to hire lobbyists or make campaign contributions. The Joint Tax Committee estimates that there are over 120 tax expenditure programs that cost the U.S. government over $1 trillion dollars in revenues.[9] Eliminating just two loopholes would generate $404 billion over 10 years.

Two corporate loopholes, in particular, stand out because together they account for the majority of the benefits from corporate tax expenditures. The ***accelerated depreciation tax break*** allows corporations to "write down" capital investments quickly, so instead of gradually counting the depreciation costs of new equipment, firms can take most of the upgrade costs off their taxes in the first couple of years. Accelerated depreciation costs the government at least $241 billion in revenues over 10 years and may encourage corporations to unnecessarily invest in large capital projects.

The ***domestic production activities deduction***, passed in 2004, essentially provides a tax break/ subsidy for almost all businesses (with employees) operating in the United States. The deduction allows companies to shield a percentage of their profits simply because they are producing goods in the country. Over the next ten years, this deduction will cost the public at least $163 billion.

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Eliminating these two corporate tax breaks would ensure that corporations pay enough revenue to actually support the physical and institutional public structures they use when doing business in America.

Support for the Idea: Of the plans reviewed for this revenue project, the following support reforming the corporate tax code to reduce loopholes: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *First Step*, the House Democratic *2012 budget*, the Institute for America's Future *Citizens' Commission*, President Obama's *2012 budget* and *Living within Our Means*, and the Congressional Progressive Caucus' *People's Budget*.

[8] *Reducing the Deficit: Spending and Revenue Options*, CBO, pg. 180-2.
[9] *Estimated Revenue Effects of Corporate Tax Reform Revenue Raising Provisions That Repeal or Modify Tax Expenditures*, Joint Committee on Taxation, pg. 1-7.

Return the inheritance tax to the 2009 level: $113 billion, or to the 2001 level: $371 billion over 10 years

The Idea: To ensure that concentrated wealth does not undermine mobility and hard work, the federal government levies taxes on the fortunes that parents pass on to their children. This tax is structured so that some amount of a person's estate is exempted from all taxes, and then the rest is taxed at a higher rate than earnings.

The inheritance tax rate has been reduced twice in the past decade. Before the Bush tax cuts were enacted, the first $675,000 per person (or $1.35 million per couple) of inherited wealth was exempt from taxes, and the tax rate was 55 percent on amounts over this.

In 2001, the inheritance tax was changed so that the first million of wealth ($2 million per couple) was exempted from any tax and the rest was taxed at 55 percent. In 2009, the rate was reduced further: $3.5 million ($7 million per couple) of wealth was exempted from any inheritance tax, and the top tax rate was reduced to 45 percent. If the inheritance tax returned to its 2001 level, the country would raise $371 billion[11] in revenue over the next 10 years. If the tax were returned to its 2009 level, the nation could raise $113 billion[12] over the same period. The inheritance tax is scheduled to return to 2001 levels in 2012 if no congressional action is taken.

The Rationale: Created in 1916, the inheritance tax helps prevent the concentration of wealth, as many people feel that too much accumulated wealth and privilege can distort our political processes and undermine democracy. Inheritance taxes have been an important source of federal revenue. The tax also encourages billions of dollars in charitable donations, since charitable gifts reduce the taxes on large estates.

The inheritance tax had a top tax rate of between 10 percent and 45 percent for the first 15 years it was in existence. But in the post-Depression era and WWII, Congress upped the top tax rate on inherited wealth several times; it peaked at 77 percent, where it stayed for the next 34 years. This was an era of equality and rapid growth.

The inheritance tax came under attack in the 1970s. Exemption levels rose steadily through the 1980s and the top tax rate was severely reduced. Rates and exemptions stayed constant roughly through the 1990s, until President George W. Bush's 2001 and 2009 tax cuts reduced them further. In 2010, the inheritance tax temporarily disappeared completely, costing the nation billions in lost revenue. Today, fewer than three estates out of every thousand actually owe any inheritance taxes, and these typically amount to less than 20 percent of the total estate, according to the Urban Institute-Brookings Tax Policy Center.

Support for the Idea: Several members of Congress have introduced legislation over the last two sessions to enact a more progressive inheritance tax, one with graduated tax rates. Rep. Jim McDermott (D-WA) introduced the "Sensible Estate Tax Act of 2009," which would enact an inflation-adjusted inheritance tax that starts taxing estates worth $1.5 million at 45 percent, and gradually increases the rate so that estates worth more than $10 million are taxed at 55 percent. Sen. Bernie Sanders (I-VT) introduced the "Responsible Estate Tax Act," which would tax estates starting at $3.5 million at a 45 percent rate, increasing to a 65 percent tax on any estate worth more than $500 million ($1 billion for couples).

Of the plans reviewed for this revenue project, the following support returning the inheritance tax to 2001, 2009, or some other progressive level: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) *Investing in America's Economy*, Center for American Progress' *First Step* and *Budgeting for Growth*, the House Democratic *2012 budget*, the Institute for America's Future *Citizens' Commission*, President Obama's *2012 budget* and *Living within Our Means*, and the Congressional Progressive Caucus' *People's Budget*, Rep. Jan Schakowsky's *Deficit Reduction Plan*, and the Bipartisan Policy Center's *Restoring America's Future*.

[11] *Reducing the Deficit: Spending and Revenue Options*, CBO, pg. 216.
[12] ibid.

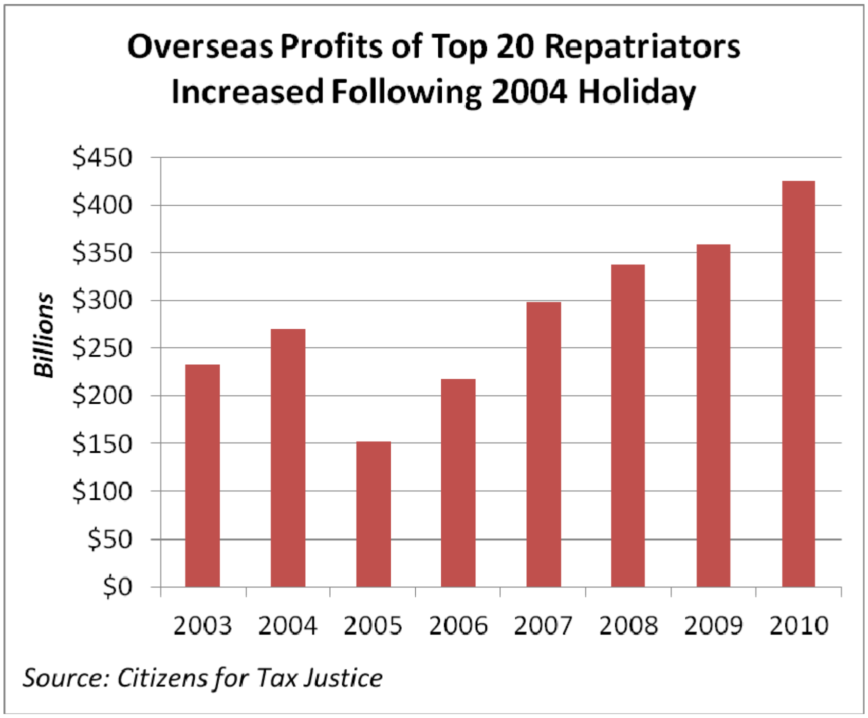
Tax the profits of corporations' foreign subsidiaries: at least $114 billion over 10 years

The Idea: U.S. corporations with businesses located in foreign countries do not have to pay taxes on the profits earned by their foreign operations (subsidiaries) if the profits are held overseas. Requiring corporations to pay taxes on the profits of their foreign subsidiaries as they are earned would bring in at least $114 billion[13] in revenues over 10 years. It would ensure that profits of U.S. firms are taxed regardless of where they are earned and take away the incentive to keep profits offshore.

The Rationale: The U.S. has a worldwide tax system, which means U.S. companies generally must pay federal income taxes on all of their income, no matter where they earn it. However, a tax loophole allows U.S. multinationals to delay paying U.S. taxes on overseas profits, as long as they keep those profits offshore. Until these profits are "repatriated" to the U.S. parent company, the profits are taxed.

The ability to defer overseas subsidiary taxes provides an incentive for overseas investments, as lower foreign taxes could encourage U.S. companies to create jobs overseas rather than bringing the money back to the United States. The loophole also encourages companies to record profits offshore, even if most of their business is actually done in the U.S., in order to artificially lower their tax rate.

Some members of Congress have called for a "repatriation holiday," which would give companies holding back profits a period of time when they could bring them back to the U.S. and pay low or no taxes. In 2004, a holiday was given and $182 billion in offshore profits was "repatriated." However, as soon as the amnesty period was over, the firms went right back to holding profits offshore, as the following graph shows.



Tax holidays actually create a stronger incentive for holding profits offshore, as companies start warehousing profits overseas and waiting for another "holiday." The Institute for Tax and Economic Policy estimates that a tax holiday like the one in 2004 would cost the country $79 billion in lost revenue over a ten-year period.

A better solution is to repeal the rule allowing the deferral of taxes on overseas profits. Corporations would still receive a foreign tax credit, which lowers their U.S. taxes by the amount of taxes they pay to other countries. This would eliminate the potential for double taxation as well as the incentive to keep profits in other countries.

Support for the Idea: Recent surveys show this reform is very popular among small business owners who feel the existing loophole gives unfair advantages to large corporations. They want to see large transnational firms pay their fair share of taxes.

Legislation was introduced recently in Congress to tax the profits of corporations' foreign subsidiaries. Sen. John Rockefeller (D-WV) introduced the "International Tax Competitiveness Act of 2011," which would treat foreign corporations managed from within the United States as domestic corporations, thus preventing businesses from deferring the taxes of a foreign subsidiary. Related legislation in the Senate, by Sen.

Carl Levin (D-MI), would give the government stronger tools to combat off-shore tax havens and sanction foreign financial institutions that impede U.S. tax enforcement.

Of the plans reviewed for this revenue project, the following plans support eliminating the deferral of foreign subsidiary income: the Congressional Black Caucus' *The Responsible Path*, and the Congressional Progressive Caucus' *People's Budget*. Citizens for Tax Justice has also been pushing for this option.

[13] *Reducing the Deficit: Spending and Revenue Options*, CBO, pg. 186.

Outlaw business accounting methods that artificially lower corporate taxes: $98 billion over 10 years

The Idea: Corporations enjoy numerous financial benefits through the tax code. These include certain business accounting methods – such as the so-called "last-in, first-out" (LIFO) and "lower-of-cost-or-market" (LCM) methods. If Congress were to eliminate these loopholes, which allow corporations to lower their taxable income artificially, the country could save roughly $98 billion[14] over 10 years.

Crafted in the 1970s to help reduce corporate taxes during inflationary times, LIFO is an accounting technique used in managing inventory where the most recently produced items are recorded as being sold first, even if the older goods are usually sold first. Since inflation is usually driving up prices, newer goods cost more to produce than older goods. By subtracting these higher costs from their revenue, a company can artificially lower its profits, and thereby lower its tax liabilities.

Here's how Citizens for Tax Justice puts it:

> For example, we normally think of profit this way: You buy something for $30 and sell it for $50 and your profit is $20 (ignoring any other expenses). But corporations, notably oil companies, use an accounting method that doesn't fit this picture. They might buy oil for $30 a barrel, and when the price rises they might buy some more for $45 a barrel. But when they sell a barrel of oil for $50, they get to assume that they sold the very last barrel they bought, the one that cost $45. That means the profit they report to the IRS is $5 instead of $20.

The Rationale: Throughout the world, only Japan and the U.S. allow for the use of LIFO accounting methods; other options are "first-in, first-out" (FIFO) accounting or the average cost method. Over a 10-year period, this accounting trick costs the government at least $52 billion in lost revenue.

LCM is a similar accounting method but allows a company to choose between valuing its inventory using its historical cost (i.e. what it cost to acquire it, using either LIFO or FIFO) or its replacement cost (i.e. what it costs to get new inventory). If the replacement cost is lower than its historical cost, then the inventory has lost value. LCM lets a company choose to value its inventory at whichever is the lower of the two costs, thus artificially reducing its profits and tax liability. While this accounting trick costs the government less than LIFO in foregone revenue, its costs are not inconsequential.

Support for the idea: Several members of Congress have introduced legislation over the last two sessions, either to limit the use of LIFO and LCM or to repeal the loopholes. Rep. Earl Blumenauer (D-OR) introduced the "End Big Oil Tax Subsidies Act of 2011," which prohibited the use of LIFO by major oil companies. Reps. Gerald Connolly (D-VA), David Cicilline (D-RI), and Heath Shuler (D-NC) each introduced bills to repeal the LIFO accounting method. Rep. John Tierney (D-MA) introduced the "Tax Equity and Middle Class Fairness Act of 2011," which would repeal both LIFO and LCM.

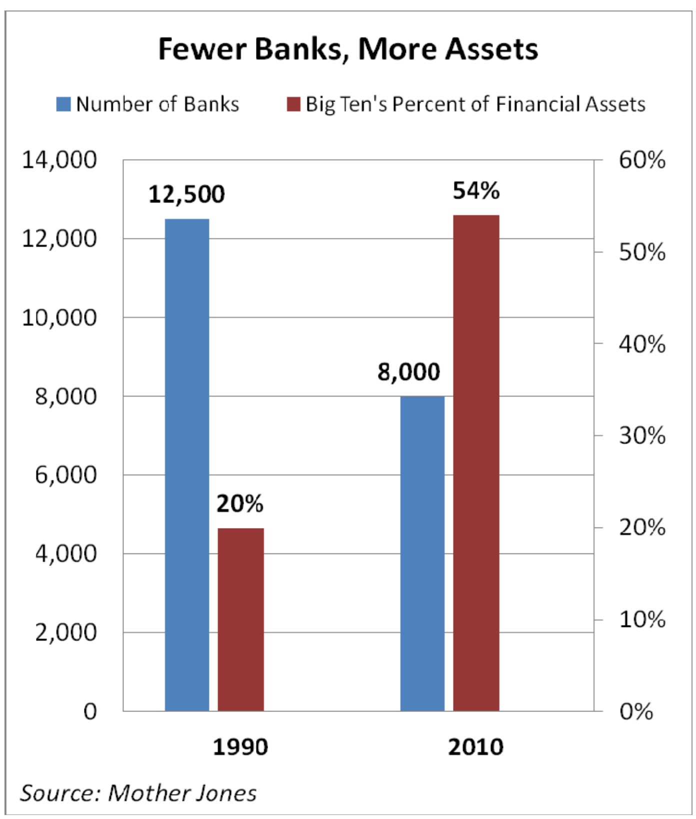
Of the plans reviewed for this revenue project, the following support repealing LIFO, LCM, or both accounting methods: the Citizens for Tax Justice's *Policy Options to Raise Revenue by Eliminating or Reducing Tax Subsidies for Wealthy Individuals and Profitable Businesses*, Center for American Progress' *Budgeting for Growth and Prosperity*, and both President Obama's FY 2012 budget and *Living within Our Means and Investing in the Future*.

[14] *Reducing the Deficit: Spending and Revenue Options*, CBO, pg. 177.

Enact financial crisis responsibility tax on big banks and financial firms: $71 billion over 10 years

The Idea: In 2008, the biggest banks and financial firms almost failed when their risky financial products imploded and they didn't have enough capital to pay off their investors. If Congress were to impose a special responsibility tax on the big banks and financial firms that Treasury bailed out in 2008-2009, the nation could raise $71 billion[15] in revenues over the next 10 years.

The Rationale: The implosion of the housing bubble and subsequent meltdown of the financial sector occurred because the financial sector rewarded the sale of risky mortgages and their bundling into questionable financial vehicles. In an attempt to prevent the economic system from collapsing further, the federal government established the Troubled Asset Relief Program (TARP) to extend credit to these institutions and buy up some of their worst products. Most of the cost of the TARP program has been repaid, but the program will end up costing the country about $47 billion.



The financial crisis set off a wave of further consolidation and concentration in the industry: the number of banks in the country has fallen by a third, and the ten largest banks now hold 54 percent of the country's financial assets, up from 20 percent in 1990. And in the first quarter of 2011, bank profits reached $29 billion, up 66.5 percent from the previous year.

A small fee of 0.15 percent on the assets of the roughly 60 bank holding and insurance companies with assets of more than $50 billion would be a way to help to recoup the cost of the bailout. It could also be extended to help pay for future financial crises. The fee would raise $71 billion over the next 10 years.

Support for the Idea: The financial crisis responsibility fee is popular among the public. President Obama has expressed support for the idea.

Of the plans reviewed for this revenue project, the following plans support enacting a financial crisis responsibility fee: Our Fiscal Security's (Economic Policy Institute, Demos, and The Century Foundation) Investing *in America's Economy*, Center for American Progress' *Budgeting for Growth*, President Obama's *2012 budget*, and the Congressional Progressive Caucus' *People's Budget*.

[15] *Reducing the Deficit: Spending and Revenue Options*, CBO, pg. 201.

Cut tax subsidies for oil and gas companies: $40 billion over 10 years

The Idea: Oil and gas companies have been receiving federal tax breaks for years. The three largest tax breaks, worth almost $40 billion over 10 years, were created to help make drilling a less risky endeavor. However, oil and gas companies are more profitable than ever, with the three largest earning tens of billions of dollars in profits per year. Removing these tax breaks would help lower the deficit while taking away a subsidy oil and gas companies simply do not need.

The Rationale: As petroleum-based energy sources began to fuel the U.S. economy at the end of the 19th century, and oil fields were drilled across large swaths of the country, the industry became ever more concentrated and the wealth of American oil producers exploded. (The head of Standard Oil, John D. Rockefeller, was the wealthiest man on the planet at the turn of the century.) As the wealth of oil magnates grew, so did their political power. In the early 1900s, they began to exercise their power in the political sphere, winning many concessions and favorable tax treatment. One of the most important was the oil depletion allowance, passed in 1913, which allowed oil companies to shield up to 27.5 percent of their profits from taxation.

Today, there are a wide range of oil and gas subsidies. The three largest subsidies cost the federal government almost $4 billion a year. All three allow oil and gas companies to deduct normal business expenses from their profit margins, reducing the taxes they pay.

The *domestic manufacturing deduction* benefits many American businesses and is not specific to oil and gas companies. It allows companies to deduct a certain amount of income for manufacturing goods in the United States. Beginning in 2004, Congress changed the tax code so that oil production could be considered a manufacturing activity (rather than an extractive industry). This allowed oil companies to suddenly deduct up to six percent of their net income from taxation. Expanding this subsidy to the oil industry costs the government $1.1 billion a year – or $11.6 billion over ten years.[1]

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A second major fossil fuel subsidy allows oil and gas companies to expense *intangible drilling costs*. This deduction allows oil companies to deduct a range of non-drilling costs, such as surveying, well development preparation, and wages leading up to drilling. Since 1986, this deduction has allowed major oil companies to deduct 70 percent of the basic expenses of doing business. The Congressional Research Service, Congress' nonpartisan research arm, notes that this expensing "allows for a quicker return of invested funds through reduced tax payments," thus making drilling itself a less risky investment. Expensing intangible drilling costs the U.S. almost $14 billion in revenue over ten years.[2]

The third subsidy is the *percentage depletion allowance*. Similar to the intangible drilling expensing, percentage depletion allows companies to recover the cost of their capital investments by deducting 15 percent of the revenue from the sale of oil and gas from their gross income (essentially depreciating oil fields as a manufacturing firm would depreciate a piece of capital equipment). Eliminating the deduction would give the government another $11.5 billion over ten years.[3]

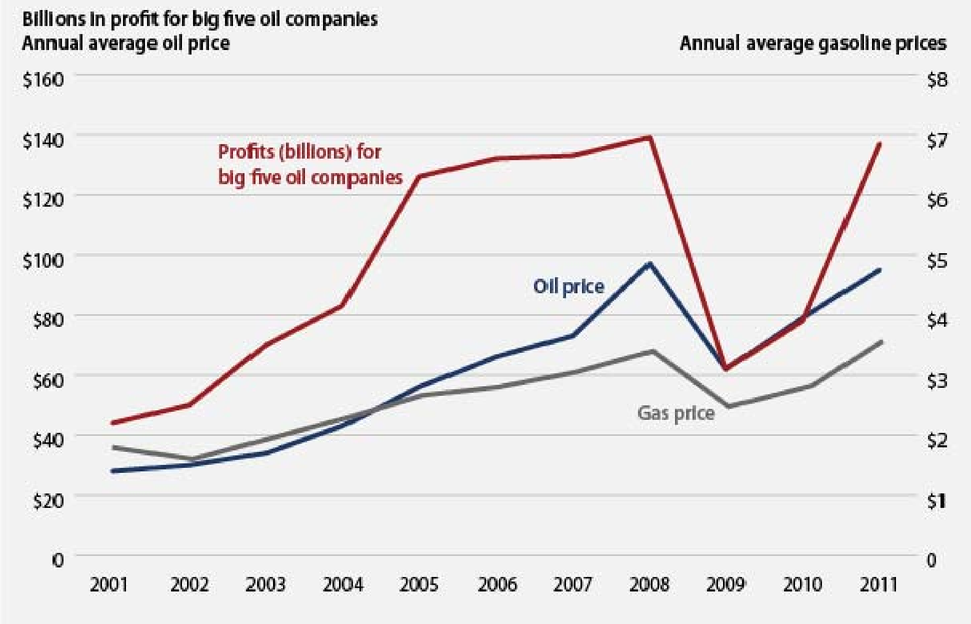

FIGURE 1
Higher prices help Big Oil
Big five oil companies' profits versus oil and gas prices

*All figures in 2011 dollars **2010 profits lower due to BP's Gulf oil spill, decreasing the company's profits by tens of billions of dollars
Sources: EIA and company profit reports

Source: Center for American Progress

With oil and gas companies reaping record profits, it is becoming hard to justify the continuation of these subsidies. As the Obama administration has noted, "In 2011 alone, the three largest American oil companies made a combined profit of more than $80 billion, or more than $200 million per day." And despite these record profits, the oil and gas industry laid off more than 11,000 workers between 2005 and 2010. A recent poll showed that 73 percent of Americans supported the proposal to end federal subsidies for oil and gas companies, making it one of the most popular budget and revenue options polled.

Support for the Idea: The Obama administration has repeatedly called for eliminating many fossil fuel subsidies, including the three listed above. In early 2012, the Senate voted on the Repeal Big Oil Tax Subsidies Act (S. 2204) by Sen. Robert Menendez (D-NJ), which would have repealed six subsidies for the five largest oil and gas companies, saving $24 billion over ten years. While the bill failed to pass, it fell only a few votes short. In 2007 and 2009, Sen. Chuck Schumer (D-NY) introduced similar bills, which never made it to the floor for a vote.

Of the plans reviewed for this revenue project, the following plans support eliminating the three subsidies: President Obama's *2013 budget* and Rep. Mike Quigley's *Reinventing Government.* The following plans support eliminating the domestic manufacturing deduction by itself: Center for American Progress' *Budgeting for Growth* and the Congressional Progressive Caucus' *People's Budget*.

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[1] "Oil and Natural Gas Industry Tax Issues in the FY2012 Budget Proposal," Congressional Research Service, 2011, http://budget.house.gov/UploadedFiles/CRSR42374.pdf
[2] Ibid
[3] Ibid

Tax the income of hedge fund managers as ordinary (wage) income: $21 billion over 10 years

The Idea: The "carried interest" loophole allows hedge fund managers to treat the commissions they earn as investment managers as capital gains. Since most of them are very wealthy, this loophole allows them to reduce what would probably be a tax rate of 35 percent to the capital gains tax rate, which is now just 15 percent. If the income of hedge fund managers was taxed like other commissioned workers or fee-for-service workers, the country would have another $21 billion[16] in revenue over the next 10 years.

The Rationale: Closing this loophole would make the tax system more equitable. Hedge fund managers are typically paid for their services through performance fees, charged as a percentage of the fund's profit. Since the fund's profits are capital gains, the carried interest loophole allows hedge fund managers to call the fees they earn capital gains for tax purposes, even though the fees are essentially salary or commission income.

There is little justification for the carried interest loophole, which treats the income of hedge fund managers differently from the income of other workers. It has allowed a small number of hedge fund managers to reap large windfalls over time. According to the Center for American Progress, the 25 richest hedge fund managers make as much as the combined income of 441,000 middle-class families.

Support for Idea: Public opinion polls show the public favors closing the carried interest loophole. Legislation has recently been introduced to do just that. Rep. John Tierney (D-MA) introduced the "Tax Equity and Middle Class Fairness Act of 2011," which would close the carried interest loophole and force hedge fund managers to pay the same tax rate on their income as regular workers do.

Of the plans reviewed for this revenue project, the following support closing the carried interest loophole: Center for American Progress' *Budgeting for Growth*, and President Obama's *2012 budget* and *Living within Our Means*.

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[16]*Reducing the Deficit: Spending and Revenue Options*, CBO, pg. 157.