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TAX & BUDGET

FACT SHEET

President Obama's FY 2016 Budget: Revenues

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President Obama's FY 2016 budget would promote tax fairness and raise revenue needed to support vital programs, finance new investments to help families get ahead, and reduce the deficit by closing tax loopholes and curbing tax breaks for wealthy investors, corporations, and large financial institutions. However, the budget could do even more to ensure that corporations pay their fair share of taxes.

Close Loopholes for High-Income Taxpayers

The budget proposes two major changes in the taxation of capital gains to close loopholes that perpetuate inequality by allowing the very wealthiest Americans to avoid paying their fair share of taxes on their accumulated wealth.

First, the budget would **raise the top capital gains and dividend rate for high-income households – those with incomes over $430,000 ($500,000 for couples) – to 28 percent**, the rate under President Reagan. This rate would be inclusive of the net investment income tax which brings the current top capital gains tax rate to 23.8 percent. It would still be below the top 39.6 percent rate on income from employment.

Second, the budget would **eliminate a provision that lets the wealthy avoid capital gains taxes on inherited, appreciated assets**. Under current law, capital gains on assets held until death are never subject to income taxes. Not only do bequests to heirs go untaxed, but the basis of inherited assets is immediately increased ("stepped up") to the fair market value at the date of death. For example, if a couple bought stock for $100,000 and it was worth $500,000 when they died, neither they nor their heirs would pay tax on the $400,000 capital gain. Under the President's proposal, transfers of appreciated property generally would be treated as a sale of the property and the deceased owner would realize a capital gain at the time the asset is bequeathed. To ensure the proposal creates neither tax nor compliance burdens for most families, decedents would be allowed a $100,000 per couple ($200,000 per couple) exclusion for capital gains income and a $250,000 ($500,000 per couple) exclusion for gain on the sale of personal residences. Bequests to a spouse or charity would continue current law to carry the basis of the decedent. Family members that inherited small, family-owned and operated businesses would not owe tax on the gains unless and until the asset were sold, and closely-held businesses would have the option to pay tax on gains over 15 years. Together, the two capital gains tax reforms would raise $207.9 billion over 10 years.

The budget would **limit the tax subsidies the wealthiest taxpayers get from itemized deductions and certain other tax preferences** (such as tax-exempt interest) to 28 percent. Under current law, a wealthy taxpayer in the 39.6 percent tax bracket who pays $10,000 in mortgage interest gets a tax savings of $3,960. But a middle-income taxpayer in the 15 percent tax bracket gets a tax savings of only $1,500 on the same $10,000 in mortgage interest. Like last year's budget, this proposal would limit the tax subsidy for taxpayers in the top three tax brackets to 28 percent. This would raise $603.2 billion over 10 years.

The budget proposes a **new minimum tax – the Fair Share Tax – on very high-income taxpayers to ensure that they don't pay a lower income tax rate than middle-class families**, a principle known as the

Buffett Rule. (Billionaire Warren Buffett famously called for reform of a tax code that allows him to pay a lower tax rate than his secretary.) Very high-income taxpayers would pay a minimum tax of 30 percent on ordinary income, less a credit for charitable contributions. This would raise $35.2 billion over 10 years.

This would **restore the estate tax to its 2009 levels**. The top tax rate would be 45 percent and the exclusion amount would be $3.5 million per person ($7 million for couples). This change and other proposed estate, gift, and generation-skipping tax reforms would raise $214.4 billion over 10 years.

International Tax Reforms

To offset the cost of repairing existing roads and bridges and modernizing America's transportation infrastructure, the budget proposes two provisions that would affect taxation of foreign earnings and lessen tax incentives for domestic companies to move profits and jobs offshore. However, offshore profits would continue to be taxed at a lower rate than domestic earnings.

The budget would **require that U.S.-based companies pay an immediate, mandatory 14 percent tax on previously-untaxed $2 trillion in corporate profits now stockpiled offshore**, whether or not those earnings are actually returned to this country (repatriated). The provision would raise an estimated $238 billion in one-time transitional revenue earmarked for the Highway Trust Fund and another $29.7 billion for deficit reduction.[1] Combined with other revenue already dedicated to the Highway Trust Fund, this proposal would provide for a $478 billion, six-year reauthorization in surface transportation spending.

In addition, the budget would **impose a 19 percent minimum tax on future foreign earnings of U.S. companies, regardless of whether the earnings are repatriated to the United States**. This would raise $206 billion over 10 years.

Other international reform proposals would prevent U.S. companies from avoiding tax through "inversions"—transactions in which U.S. companies buy smaller foreign companies and then reorganize the combined firm to reduce U.S. tax liability—and prevent foreign companies operating in the United States from using excessive interest deductions to "strip" earnings out of the United States and avoid U.S. tax.

Other Reforms

The budget would **make it more costly for an estimated 100 large, highly-leveraged financial firms (those with assets in excess of $50 billion) to finance their activities with excessive borrowing**, by imposing a seven basis point fee on liabilities. The provision would reduce risks to the broader economy and raise $111.8 billion over 10 years.

The President's budget would **increase the tax on cigarettes and other tobacco products**, discouraging children from smoking and funding the expansion of preschool programs for all four-year olds in low- and moderate-income families. This would raise $95.1 billion over 10 years.

The budget would **limit the extent to which wealthy taxpayers can accumulate amounts in tax-favored retirement accounts such as IRAs and section 401(a) plans**. Under the proposal, total contributions and accruals would be limited to the amount necessary to provide a maximum annuity of $210,000 at age 62 (about $3.4 million based on today's interest rates). The limit would be indexed and actuarially adjusted. This would raise $26 billion over 10 years.

In addition, the budget would close a number of other corporate tax loopholes and special preferences. However, under the budget, this revenue would be used to finance business tax reform that is revenue neutral in the long run, including **a reduction in the corporate tax rate from 35 percent to 28 percent** (25 percent for manufacturers) and some new permanent corporate tax breaks.[2]

Unless otherwise noted, all information is from U.S. Dep't of Treasury, General Explanations of the Administration's Fiscal Year 2016 Revenue Proposals (Feb. 2015), *available at* http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2016.pdf.

1 *See* The White House, Summary Tables, Table S-2. Effect of Budget Proposal on Projected Deficits, at 92-93 (Feb. 2015), *available at* http://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/tables.pdf. Business tax reform transition revenue finances the $126.5 billion in budget authority for new surface transportation investments (the PAYGO portion of the reauthorization proposal) plus $111.9 billion of cash transfers necessary to ensure Transportation Trust Fund solvency for all programs proposed to be funded via the Transportation Trust Fund over the six-year reauthorization period, leaving an additional $29.7 billion for deficit reduction.
2 Office of Management & Budget, Fiscal Year 2016 Budget of the U.S. Government, at 56 (Feb. 2015), *available at* http://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/budget.pdf.