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## STATEMENT FOR THE RECORD BEFORE THE U.S. SENATE COMMITTEE ON FINANCE

### “THE 2025 TAX DEBATE AND TAX AVOIDANCE STRATEGIES”

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Chairman Wyden, Ranking Member Crapo, and members of the U.S. Senate Committee on Finance:

As a leading representative of America’s 34 million small businesses, Small Business Majority is pleased to provide written testimony to the U.S. Senate Committee on Finance regarding the 2025 tax debate and the importance of ensuring our tax code supports a thriving and equitable small business economy.

Small Business Majority is a national small business organization that empowers America’s diverse entrepreneurs to build a thriving and equitable economy. From our ten offices across the country, we engage a network of more than 85,000 small businesses and 1,500 business and community organizations to deliver resources to entrepreneurs and advocate for public policy solutions that promote inclusive small business growth. Our work is bolstered by extensive research and deep connections with the small business community that enables us to educate stakeholders about key issues impacting America’s entrepreneurs, with a special focus on the smallest businesses and those facing systemic inequities.

For more than a decade we have examined the reality of how taxation affects America’s small businesses and have effectively advocated for policies that support a resilient, inclusive economy. Our work has combined analyses of tax policies’ impacts on Main Street along with scientific research into small business needs and attitudes. Our work is bolstered by the stories of real small business owners.

#### **Today’s tax code is needs to be reformed to increase investment in Main Street**

In August 2024, we conducted a national opinion poll to better understand the perspectives of small business owners when it comes to tax policy. The survey revealed that 82% of business owners agreed that the current tax system favors large corporations over their small business. 75% also agree that wealthy individuals and large corporations don’t pay their fair share of taxes. Overall, small businesses feel disadvantaged by loopholes that allow larger and wealthier businesses to avoid paying taxes.<sup>1</sup> As I stated in my testimony to the Senate Committee on the Budget on the impact of tax loopholes on the small business community, while large corporations continue to get away with outsourcing production, investments, and output to pay fewer taxes, our nation’s smallest businesses, those that policymakers regularly acknowledge are the backbone of this economy, do not have the same luxury.<sup>2</sup>

Like most small enterprises across the country, 75% of the small businesses in our network have fewer than 10 employees (one-third of which are solopreneurs). These business owners need more support from Congress, which includes advocating for bottom-up tax reform that would actually deliver for Main Street. In fact, our opinion polling found that an overwhelming 76% of respondents said that more tax incentives

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<sup>1</sup> “Opinion Poll: Small Businesses Support Bottom-Up Tax Reforms.” Small Business Majority. August 28, 2024. <https://smallbusinessmajority.org/our-research/taxes-budget-economy/opinion-poll-small-businesses-support-bottom-tax-reforms>

<sup>2</sup> “Small Business Majority testifies in support of closing corporate loopholes in tax code.” January 17, 2024. <https://smallbusinessmajority.org/policy/small-business-majority-testifies-support-closing-corporate-loopholes-tax-code-0>

for small businesses should be provided. These sentiments underscore the fact that today's tax code is not benefiting small businesses.

### **Examining the impacts of tax disparities from the 2017 Tax Cuts and Jobs Act—a promise that failed to deliver for Main Street**

The enactment of the 2017 Tax Cuts and Jobs Act (TCJA) was largely touted by lawmakers as much-needed tax relief for America's small businesses, but it has since failed to deliver on that promise. Instead, it actually increased opportunities for wealthier corporations to exploit our tax system. This law has not only incentivized larger companies to outsource production to avert taxation, but it has not delivered for most Main Street businesses.

A prime example of how the TCJA failed to help the smallest businesses can be seen in the distribution of the Section 199A pass-through deduction. The Section 199A Qualified Business Income (QBI) Deduction allows pass-through entities to deduct up to 20% of their eligible, pass-through business income from their federal taxes. Given that 95% of small businesses are classified as pass-through entities, which include sole proprietorships, partnerships, LLCs, and S-Corporations, many believed the deduction would provide relief to Main Street businesses.<sup>3</sup> However, based on 2022 Tax Policy Center data, 69.2% of all pass-through deduction benefits flowed to the wealthiest 4.5% of businesses.<sup>4</sup> While the wealthiest passthrough entities claimed an average deduction of over \$1 million in 2021, claimants with adjusted gross incomes (AGI) below \$100,000 took home an average deduction of just \$1,997.<sup>5</sup>

Overall, the concentration of pass-through income at the top has also resulted in the concentration of deductions among high-earning individuals and businesses. Taxpayers with more than \$200,000 in AGI claimed more than two-thirds of 199A deductions, while taxpayers with more than \$1,000,000 in AGI claimed over one-third of the deduction at a cumulative level.<sup>6</sup> The financial benefits for a pass-through entity making \$500,000 are 20 times higher than the benefits for a business making \$75,000. While many argue that this is proof of a progressive tax system working as it should, it is difficult to agree with those sentiments when the smallest businesses are unable to access these benefits at similar rates.

Furthermore, the current tax code is characterized by a substantial gap between top individual rates and top pass-through rates, which incentivizes wealthy individuals to manipulate the system by declaring themselves as pass-through business entities, otherwise known as the pass-through loophole. Although the law restricts certain industries from accessing the pass-through rate, there is no effective mechanism to prevent the abuse of the deduction, which we see play out in real time, especially among top earners. Since the passage of the 2017 tax law, we have seen that the benefits continue to go directly to millionaires and billionaires, not Main Street businesses. For example, Americans for Tax Fairness found that billionaires became \$2.2 trillion richer since the law was enacted; while at the same time, our federal programs supporting small businesses continue to struggle for funding following an increased demand during the COVID-19 pandemic.<sup>7</sup> The permanency of this package, as it stands in the law, would cost American taxpayers another \$3.8 trillion.<sup>8</sup>

The forthcoming expiration of numerous provisions set in place by the 2017 tax law, including the 199A pass-through deduction, presents a critical opportunity for impactful reform that can have a direct benefit to small businesses and self-employed individuals, as opposed to large businesses. Small businesses that

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<sup>3</sup> "9 facts about pass-through businesses." Brookings Institution. May 15, 2017. <https://www.brookings.edu/articles/9-facts-about-pass-through-businesses>

<sup>4</sup> "Sources of flow-through business income by statutory marginal tax rate; current law, 2022." Tax Policy Center. March 1, 2023. <https://www.taxpolicycenter.org/model-estimates/distribution-business-income-february-2023/t23-0028-sources-flow-through-business>

<sup>5</sup> "The 2017 Tax Bill's Pass-Through Deduction Largely Favors the Wealthy and Encourages Gaming of the Tax Code," Center for American Progress, 2024. <https://www.americanprogress.org/article/the-2017-tax-bills-pass-through-deduction-largely-favors-the-wealthy-and-encourages-gaming-of-the-tax-code/>

<sup>6</sup> "How do business owners respond to a tax cut? Examining the 199A deduction for pass-through firms." Columbia Law School. [https://www.law.columbia.edu/sites/default/files/2023-03/Goodmanetal\\_199A\\_Deduction\\_2022.pdf](https://www.law.columbia.edu/sites/default/files/2023-03/Goodmanetal_199A_Deduction_2022.pdf).

<sup>7</sup> "Billionaires are \$2.2 trillion richer since 2017 Trump-GOP tax law." Americans for Tax Fairness. September 28, 2023. <https://americansfortaxfairness.org/billionaires-2-2-trillion-richer-since-2017-trump-gop-tax-law/>

<sup>8</sup> Ibid.

see a benefit in this deduction simply will not receive enough savings to grow or invest back in their businesses, as their minimal profits leave them with little to nothing to put back into their enterprises.

To ensure our tax code reflects the needs of America’s smallest businesses that keep our economy running, we propose replacing or reforming the 199A deduction to function in a way that delivers bottom-up benefits. Through this proposal, small businesses could deduct their first \$25,000 of qualifying business income (QBI), thus benefiting the very small businesses rather than continuing to deploy current and unevenly distributed top-down tax breaks that only help a select few. Under this proposal, the smallest businesses, specifically those earning a net income less than \$125,000 per year, may benefit. This deduction should be accompanied by a phase-out for business owners with \$400,000+ in income to ensure it benefits the entities most in need. Notably, small businesses see this proposal as a viable path forward. Our national polling revealed that more than half (53%) of small businesses that aren’t C-corporations support this change.<sup>9</sup>

We encourage Congress to consider this proposal and get serious about passing legislation that stimulates the economy at the very bottom, which would provide simplified and streamlined tax relief to millions of small businesses, giving them the ability to save and invest back into their businesses to grow their operations. Continuing 199A outright without any consideration for microbusinesses and those with smaller revenues would be a missed opportunity for Main Street.

### **Small businesses support revenue raisers that would lead to increased investments in the small business ecosystem**

It is no secret that small businesses are growing, with an estimated 19 million new business applications filed in the last three years alone.<sup>10</sup> To sustain this historic small business boom, it is paramount that federal agencies receive the proper funding and resources to carry out their mission of serving small businesses that rely on federal programs to start, scale and improve their ventures. Recovering lost revenue from the exploitation of corporate and international tax loopholes presents an opportunity to bolster domestic federal programs that are critical to small business growth. Small businesses support multiple levers that could be used to generate revenue and fund these investments and initiatives.

1. **Closing offshore tax loopholes:** Small business owners recognize the need to close offshore tax loopholes that continuously shift our nation’s tax burden to the smallest businesses. In fact, 77% of small business owners agree that large corporations unfairly leverage their foreign presence to reduce their U.S. tax liability.<sup>11</sup> According to the Joint Committee on Taxation, the TCJA’s provision taxing foreign profits of U.S. multinationals at a lower rate than the rate that applies to domestic profits will cost more than \$200 billion in revenue over the 2023-2027 time period.<sup>12</sup> This system has allowed a few multinational corporations to continue funneling their profits to the lowest-taxation foreign jurisdictions, a privilege small firms cannot exploit. To ensure large, multinational corporations pay the same tax rate on profits earned abroad as they do in the U.S., we urge Congress to enact the *No Tax Breaks for Outsourcing Act*, which would be a significant first step in bringing much needed parity to the tax code. Small Business Majority national polling found that 71% of small business owners support setting a minimum tax rate of 21% on corporate offshore profits.<sup>13</sup>

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<sup>9</sup> “Opinion Poll: Small Businesses Support Bottom-Up Tax Reforms.” Small Business Majority. August 28, 2024. <https://smallbusinessmajority.org/our-research/taxes-budget-economy/opinion-poll-small-businesses-support-bottom-tax-reforms>

<sup>10</sup> “Statement from President Joe Biden on a Record 19 Million New Business Applications.” The White House. August 14, 2024. <https://www.whitehouse.gov/briefing-room/statements-releases/2024/08/14/statement-from-president-joe-biden-on-a-record-19-million-new-business-applications/>

<sup>11</sup> “Survey Toplines - Opinion Poll: Small Businesses Support Bottom-Up Tax Reforms.” Small Business Majority. August 28, 2024. <https://smallbusinessmajority.org/sites/default/files/research-reports/2024-august-tax-survey-toplines.pdf>

<sup>12</sup> “CBO Estimates TCJA Extensions Could Cost Up to \$2.7 Trillion.” Committee for a Responsible Federal Budget. June 28, 2022. <https://www.crfb.org/blogs/cbo-estimates-tcja-extensions-could-cost-27-trillion>

<sup>13</sup> “Survey: Small businesses support tax reforms to pay for robust infrastructure investments.” Small Business Majority. June 8, 2021. <https://smallbusinessmajority.org/our-research/infrastructure/survey-small-businesses-support-tax-reforms-pay-robust-infrastructure-investments>

2. **Increase the corporate rate:** In addition to the expansion of the offshore tax loophole, the TCJA gave large corporations another unnecessary tax cut when it permanently lowered the domestic corporate tax rate from 35% to 21% further reducing the tax liability of our nation's largest businesses. Since most small businesses are not organized as C-corporations, this tax cut has had virtually zero positive impact on small businesses. Our recent poll found that 52% of small business owners support increasing the corporate tax rate to 28% to generate revenue.<sup>14</sup>
3. **Allow the IRS to access funds needed to enforce revenue raisers and serve small businesses:** As our tax code has become increasingly exploited by wealthy individuals and corporations that aim to game the system to avoid paying their fair share in taxes, a trend that has been compounded by the enactment of the TCJA, it is paramount that the Internal Revenue Service (IRS) be equipped with the adequate funding and resources necessary to close the annual tax gap of roughly \$700 billion.<sup>15</sup> When asked if they would support continued additional funding for the IRS, our research found that 51% of small business owners support additional funding to ensure the agency can fulfill its essential functions. A vast majority think that the IRS needs more funding to properly improve customer service (85%), audit large corporations (82%) and provide tax filing assistance (81%). Additionally, entrepreneurs also strongly believe that the IRS needs more funding to audit wealthy taxpayers (79%), audit individuals (67%) and audit small businesses and self-employed individuals (67%).<sup>16</sup> We urge Congress to reject any proposed cuts to the IRS and continue to provide additional funding which will empower the agency to recover lost revenue and provide critical tax filing services to small business owners and entrepreneurs who don't have the luxury of employing the services of private tax professionals year after year.

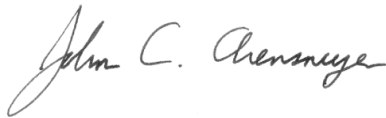
### **Small businesses need a fair tax code and a level playing field, especially when competing with larger companies in their communities**

Over the last few years, small business owners have made their message clear to Congress: They need a simplified and streamlined tax system that would also help level the playing with large corporations. Instead, they got the opposite. Small business owners seek fairness, not special treatment, in the tax code. They desire a level playing field for competition, including when competing with large-scale corporations. Navigating a complex tax code that is not designed for small businesses shouldn't be a hurdle for American entrepreneurs striving to operate and expand their businesses.

2025 presents a critical opportunity to reevaluate our tax code, and Congress must act to hold wealthy corporations accountable for paying their fair share, and to deliver much needed tax relief to America's small businesses. We hope the conversation today sheds light on some of the solutions to achieving those goals to uplift our nation's smallest but most innovative job creators and economic contributors.

We thank you for the opportunity to comment on the 2025 tax debate and how tax avoidance strategies continue to shift the burden onto Main Street businesses. For any questions or additional information, please contact Government Affairs Director, Alexis D'Amato at [adamato@smallbusinessmajority.org](mailto:adamato@smallbusinessmajority.org).

Sincerely,



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<sup>14</sup> "Congress Should Revisit 2017 Tax Law's Trillion-Dollar Corporate Rate Cut in 2025." Center for Budget and Policy Priorities. March 21, 2024. [https://www.cbpp.org/research/federal-tax/congress-should-revisit-2017-tax-laws-trillion-dollar-corporate-rate-cut-in#\\_edn5](https://www.cbpp.org/research/federal-tax/congress-should-revisit-2017-tax-laws-trillion-dollar-corporate-rate-cut-in#_edn5)

<sup>15</sup> "IRS updates tax gap projections for 2020, 2021; projected annual gap rises to \$688 billion." Internal Revenue Service. October 12, 2023. <https://www.irs.gov/newsroom/irs-updates-tax-gap-projections-for-2020-2021-projected-annual-gap-rises-to-688-billion>

<sup>16</sup> "Opinion Poll: Small Businesses Support Bottom-Up Tax Reforms." Small Business Majority. August 28, 2024. <https://smallbusinessmajority.org/our-research/taxes-budget-economy/opinion-poll-small-businesses-support-bottom-tax-reforms>