Why the Obamas Paid Too Much in Taxes
By Dorothy A. Brown

Dorothy A. Brown is a professor of tax law at Emory University.

The American tax system is supposed to be progressive. Yet, for the very rich, nothing could be further from the truth.

You know the expression that the rich are different. Well, we found out that President and Mrs. Obama made more than $5 million last year, and after examining their tax returns, I can say that they are different — but not in the way you might think. They are different because, for their income group, they paid too much in taxes.

The first couple earned more than $5 million and paid 32 percent in federal income taxes.1 When compared with only taxpayer paying too much in taxes. Every taxpayer why their tax rate was 32 percent. The president is not the beneficiaries of Obama's reform will be high-income taxpayers with significant percentages of capital gains.

The typical taxpayer with $5 million of income received almost half of it from capital gains and qualified dividends, which are taxed at the lower 15 percent rate.2 That is why their tax rate is 23 percent. The Obamas, however, had a negligible amount (less than $2,500) of income subject to the 15 percent rate, with the rest of their income subject to the maximum 35 percent rate.3 That is why their tax rate was 32 percent. The president is not the only taxpayer paying too much in taxes. Every taxpayer without income subject to the 15 percent rate is paying too much in taxes when she compares herself with someone who has income that is taxed at the 15 percent rate.

Taxpayers in households between $50,000 and $100,000 have no more than 3 percent of their income from capital gains and corporate dividends.4 Most of their income will be subject to tax at up to 35 percent. Taxpayers with between $100,000 and $200,000 of income pay the 15 percent rate on only 6 percent of their income.5 For households with income between $200,000 and $500,000, almost 13 percent of their income is subject to the 15 percent rate.6 However, the percentages steadily increase until finally we see 60 percent of income subject to the 15 percent rate for households with at least $10 million of income.7 Most of us do not benefit greatly from the 15 percent rate.

Obama’s solution to this problem is to let the Bush tax cuts expire for households with incomes greater than $250,000, which will increase their tax rate on capital gains to 20 percent and increase their tax rate on all other income to 39.6 percent.8 This misses the point. The differential between 39.6 percent and 20 percent will be virtually the same as we have now (35 minus 15). The real beneficiaries of Obama’s reform will be high-income taxpayers with significant percentages of capital gains.

What you often hear from those who support lower taxes on corporate dividends is that income has already been taxed once at the corporate level and that the lower tax rate reflects that fact. What they fail to tell you is that in some instances that income has never been taxed at the corporate level.9 Those who support lower taxes on capital gains argue that it generates additional government revenue. In the short term it does, especially when the lower rate is only temporary, as it was in 2003. In the long term, the government loses lots of money from capital gains rate cuts.10

In the final analysis, the question is clear. Should someone who receives $5 million in royalties from a book
he worked long and hard to write and get published pay
taxes at a higher rate than someone who receives $5
million from taking her stockbroker’s advice in deciding
when to buy and sell stock? Put another way, should
someone who works a 40-hour week and is busy trying
to raise a family pay more in taxes than someone who
never gets out of bed but earns the same money from
going to the mailbox and getting a dividend check (or
just going to the computer and checking their account
online)? Of course not — because all income should be
taxed the same. No type of income should get preferen-
tial treatment.

We profess to be the land of opportunity for all, yet
when it comes to our tax system, we become the land of
opportunity for some. To quote Warren Buffett: “There’s
class warfare, all right, but it’s my class, the rich class,
that’s making war, and we’re winning.”12 The time for
change is now. We need to have a progressive tax system
that applies to all taxpayers. Even the president should
have a dog in this fight.

estimated that extending the capital gains tax cut enacted in 2003
would cost $100 billion over the next decade”) (emphasis in origi-
12Ben Stein, “In Class Warfare, Guess Which Class Is Win-

FLPs, the Transfer Taxes, and the
Income Tax

By Laura E. Cunningham

Laura E. Cunningham is a professor of law at the
Benjamin N. Cardozo School of Law.

Despite repeated calls for reform, Congress has
deprecated act to curb transfer tax avoidance through
the use of family limited partnerships (FLPs). Use of
FLPs allows taxpayers to substantially leverage their
exemption from estate tax and reduce the effective rate
of tax on even the most liquid investment assets. This
article reviews the current state of the law in the Tax
Court on FLPs, renews the call for congressional
action, and explains why FLPs are not just a “death
tax” problem.

If and when Congress acts on the future of the federal
transfer taxes, there are several important issues it should
address. Even though these have been outstanding for
decades, they have yet to be dealt with in legislation
passed by the House or the Senate. I would like to bring
them back to the front burner.

My principal concern is with the valuation discounts
that have become part of the transfer tax landscape. The
IRS and Tax Court’s acquiescence in substantial valuation
discounts for interests in family limited partnerships
(FLPs) have allowed wealthy individuals to reduce the
value of their estates for transfer tax purposes with only
a modicum of careful planning. As the law has developed
in the Tax Court, the only unsuccessful taxpayers are
those not represented by skilled counsel. When taxpayers
observe the blueprint of formalities provided by the
court, even the most liquid assets transferred by the most
elderly taxpayers are discounted by as much as 40
percent (or more) for transfer tax purposes. The pro-
posals before Congress for continuing the transfer taxes
call for continuing the exemption of $3.5 million ($7
million for married couples) that was effective in 2009.1
That means that as the reach of the transfer taxes narrows
to only the wealthiest of decedents, the sophistication
level of counsel will increase. In other words, few tax-
payers potentially subject to the tax will die without a
carefully planned FLP.

To date, Congress has ignored all pleas for legislation
limiting valuation discounts, including some made by

1H.R. 4154, passed December 3, 2009. H.R. 439, offered by
House Ways and Means Committee member Earl Pomeroy,
D-N.D., in January 2009, contains a provision denying valuation
discounts for nonbusiness assets held within an entity. Those
provisions weren’t included in H.R. 4154, which was also
sponsored by Pomeroy.