

Key Wealth Institute

Moore v. United States – Small Tax Case Before Supreme Court Could Have Huge Impact on US Tax System

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The US Supreme Court heard oral arguments in December in Moore v. United States, a case that could have major ramifications for the US tax system. The plaintiffs sued for a refund of a tax bill of less than \$15,000, but the court's decision could affect some of the basic tenets of the tax code.

The potential impacts range from the elimination of existing taxes to opening the door for Congress to impose a wealth tax. The elimination of the tax provision in dispute, the mandatory repatriation tax (MRT), would have an immediate impact on the US Treasury. However, the more significant impact could be the ripple effect on similar tax principles.

The case could even challenge the constitutionality of a wealth tax, which has been proposed several times in the past by senators such as Elizabeth Warren (D-MA) and Bernie Sanders (I-VT) and most recently by Ron Wyden (D-OR).

Background of the case

In 2005, Charles and Kathleen Moore invested in a company in India. They never received any income (interest, dividends, or any other distributions) from the company, which reinvested its profits. But the Moores acknowledged that the value of their investment increased by more than \$500,000.

The case stems from the 2017 Tax Cuts and Jobs Act (TCJA), which included a MRT on foreign investments. Before the TCJA, a US taxpayer who held shares in a foreign corporation that earned income overseas did not need to pay taxes on those earnings until they were repatriated into the United States.



The 2017 change in the law required taxpayers like the Moores with 10 percent or more ownership in a foreign corporation to pay a tax even if they had not received any of the gains on their investment.

The Moores are challenging the MRT, which is essentially a tax on capital appreciation. The Tax Foundation projected that this provision would generate hundreds of billions of revenue (paid mainly by corporations), so it is much more than just the Moores' claim posing a threat to the US Treasury's coffers.

The 16th Amendment to the Constitution, ratified in 1913, allowed Congress to levy an income tax without the need to apportion it to the states. Historically, those taxes have been imposed on what we consider realized income (earnings, interest, rents, dividends, etc.).

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The Moores discovered in 2018 that they owed a \$14,729 tax bill on their investment in India as a result of the 2017 tax reform law. They paid the bill but sued for a refund, arguing that they are being taxed on appreciation of the value of assets from which they realized no income. Their suit claims the tax on unrealized gains is unconstitutional.

The oral arguments before the Supreme Court lasted more than two hours, and the lawyers for both sides made the potential ramifications of the decision apparent throughout the session.

The Moores' attorney, Andrew Grossman, said that taxing investments where no income was received was outside the scope of the 16th Amendment's intentions.

The government countered that there was never a constitutional realization requirement and that imposing one now would upend a significant amount of the current tax code.

The justices also indicated their concerns about unintended consequences of ruling on either side of the argument, ranging from the loss of tax dollars to the Treasury to the impact on well-established tax law.

Potential impact on wealth taxes

The potential impact of a SCOTUS ruling to uphold the tax would be to open the door to additional wealth taxes, which would be a departure from the traditional method of imposing taxes on earned income.

The 16th Amendment imposed a progressive income tax (in which rates increase as more taxable income is earned) on various income sources, such as employment, investment, rents, and other sources of income. A wealth tax could take several different forms, such as applying a tax rate to a taxpayer's net assets above a certain level or assessing a tax on unrealized income. For example, assets like marketable securities or real estate that appreciate and are not sold could be subject to a wealth tax.

Currently, if an investor were to buy a security for \$5,000 and continue to own it while the value increases to \$12,000, the \$7,000 increase would not be taxable until the gain is realized in a sale. Under a wealth tax, the \$7,000 gain could be taxable, regardless of whether the security is sold.

One such wealth tax was introduced by Senator Ron Wyden on November 30, 2023. Under the Billionaires Income Tax Act, taxpayers with more than \$100 million in annual income or more than \$1 billion in assets for three consecutive years would be affected.

Marketable securities would be valued on an annual basis, and any increase in value would be taxable whether they have been sold or not. Decreases in values would be deductible with a three-year carryback provision. Non-tradable assets, such as real estate or business interests, would not be subject to the annual tax but would include an additional tax on sale. That's basically an interest charge on the tax deferral while the taxpayer held the asset.

In its current form, Wyden's proposal would only apply to approximately 700 individuals in the US, but it could set a precedent for further wealth taxes.

The impact of a SCOTUS ruling striking down the MRT would depend on how broadly or narrowly the court words its decision.

A ruling that broadly finds against repatriation of corporate and noncorporate taxpayers' capital appreciation could cost the Treasury more than \$300 billion in both refund claims and reduced future revenue, according to the Tax Foundation. A more narrow ruling that would apply only to individuals and pass-through entities would cost the Treasury approximately \$3.5 billion. In addition, the ruling could also affect other corporate foreign tax provisions.

Perhaps more importantly, if the court decides that the tax is not constitutional because income was not realized, the ability to implement a wealth tax such as the one proposed by Wyden could be unconstitutional.

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Some of the comments made by the justices demonstrated concerns about the impact of this decision in both directions — calling other tax provisions into question or giving Congress the green light to

assess taxes with no regard to realization. It will be interesting to see the decision on this case because of the potential ramifications.

A final decision is expected by June 2024 at the latest.

For more information, please contact your advisor.

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About the Author

As a Senior Wealth Planner for Key Private Bank, Paul focuses on ensuring his clients' wealth management plans are carried through to meet their unique financial objectives and grow and preserve wealth.

Paul most recently served as a Regional Planning Strategist for Key Private Bank. Prior to joining Key, Paul was the director of Wealth Planning at Wilmington Trust and was responsible for the delivery of planning services and the planning platform, including scalable advice-oriented solutions, thought leadership, and direct planning where appropriate. Paul contributed thought leadership and solutions to the Corporate Executive Practice Group, including direct planning for corporate executives. Prior to joining M&T Bank, which acquired Wilmington Trust in 2011, Paul was a tax manager with a CPA firm.

He holds an MBA from SUNY Buffalo and completed their Graduate Tax program. Paul is a Certified Public Accountant and a Chartered Global Management Accountant and has the Certified Financial Planner®, Personal Financial Specialist, Certified Life Underwriter, Retirement Income Certified Professional®, Certified Advisor in Philanthropy, Chartered Advisor in Senior Living, Chartered Financial Consultant, and Certified Retirement Counselor designations. Paul instructed courses in the Certified Financial Planner Program as an adjunct faculty member of Canisius College in Buffalo New York. He is currently the treasurer and member of the board of directors for Musically Theater in Amherst, New York. Previously, he served on the board of directors and as the treasurer of the Make-A-Wish Foundation of Western New York and BNSME. Paul is a member of the FPA, AICPA, and NYSSCPA.

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