



WRITTEN TESTIMONY BEFORE THE JOINT ECONOMIC COMMITTEE

Building on the Success of TCJA: The 2025 Tax Policy Debate

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Chairman Heinrich, Vice Chairman Schweikert, and members of the Joint Economic Committee:

Thank you for inviting me to speak about the importance of ensuring that we have a tax code that supports a robust, innovative and inclusive economy anchored by our nation's 34 million small businesses.

I am the founder and CEO of Small Business Majority, a national small business organization that empowers America's diverse entrepreneurs to build a thriving and equitable economy. Prior to launching Small Business Majority nearly 20 years ago, I was the founder and CEO of an award-winning interactive communications company, which I ran for 12 years. I am particularly qualified to speak to the impact of our tax code on America's Main Street small enterprises, and to recommend changes that would help ensure the success of our nation's smallest firms.

At Small Business Majority, we engage our network of more than 85,000 small businesses and 1,500 business and community organizations to advocate for public policy solutions and deliver resources to entrepreneurs that promote equitable small business growth. As a leading representative of America's primary job creators, I am here to testify about the opportunity that lies ahead in next year's tax debate to enact meaningful tax reform that can have a direct benefit for our nation's smallest, most under-resourced businesses that continue to be left behind.

America's small business owners want a level playing field on which to do business. To create a level playing field, policymakers must ensure that all stakeholders in our economy are working in good faith to meet tax obligations necessary to fund investments in our country.

For two decades, we have examined the reality of how taxation affects America's small businesses and have advocated for tax policies that maximize entrepreneurial growth. Our work includes scientific research into small business needs bolstered by the stories of America's small business owners.

The current tax code is not working for "Main Street" America; small businesses support bottom-up reforms to level the playing field.

Congress has a historic opportunity to better support small businesses and entrepreneurship through the upcoming expiration of many of the Tax Cuts and Jobs Act (TCJA)'s provisions. However, rushing a partisan solution through in the first 100 days would be inconsistent with considering alternative proposals that could make a real difference for Main Street. While there are a host of current provisions within the tax code that purport to support small businesses, they are too often structured without the smallest businesses in mind.

Eighty-two percent of small business owners agree that the current tax system favors large corporations over small businesses according to a national opinion poll conducted by Small Business Majority in August 2024. The same poll found that 75% believe that wealthy individuals and large corporations don't pay their fair share of taxes. Overall, small businesses feel disadvantaged by tax loopholes that disproportionately advantage larger and wealthier businesses.¹

¹ "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>

Small businesses clearly need tax reforms from Congress that would create a bottom-up, simplified, tax system that better delivers for Main Street. Our opinion polling finds that an overwhelming 76% of respondents say that more tax incentives for small businesses should be provided. These sentiments underscore the fact that today's tax code is in fact not benefiting small businesses despite certain narratives to the contrary.

The expiration of the Tax Cuts and Jobs Act presents an opportunity for Congress to reform the Section 199A pass-through tax deduction in a way that benefits the vast majority of true Main Street small businesses.

The leading example of how the TCJA has failed to help the smallest businesses is the Section 199A provision which allows pass-through entities to deduct up to 20% of their eligible, pass-through Qualified Business Income (QBI) 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, TCJA proponents claimed that this would provide relief to Main Street businesses.² However, based on 2022 Tax Policy Center data, 69.2% of all pass-through deduction benefits flowed to the wealthiest 4.5% of small business owners.³ While the richest pass-through 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 \$1,997.⁴ Indeed, the financial benefits for a pass-through entity earning a profit of more than \$500,000 are 20 times higher than the benefits for a business making \$75,000.

The distribution of the pass-through benefit has also widened racial disparities, with a staggering 90% of the benefit being claimed by white entities while Black and Hispanic entities received just 7% of the benefit from the pass-through deduction.⁵ Given that the rate of new business ownership for Black and Hispanic individuals is growing at an unprecedented pace, this disparity further indicates that millions of small businesses aren't receiving the tax relief necessary to support the sustainability of their operations. If the goal is to provide the maximum benefit for the smallest businesses, we owe it to Main Street to ensure an optimal tax incentive that works to expand access to the American Dream.

To ensure our tax code reflects the needs of America's smallest businesses that keep our economy running, Small Business Majority has long advocated for replacing or reforming the 199A deduction to function in a way that delivers bottom-up benefits. For example, small businesses could deduct their first \$25,000 of QBI, thus benefiting very small businesses rather than continuing to deliver inequitably distributed top-down tax breaks that only help a select few. Under this proposal, the smallest businesses, specifically the vast majority with a net income of less than \$125,000 per year, would benefit.⁶ This deduction should be accompanied by a phase-out for business owners with more than \$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 polling found that 2.5 times more pass-through small business owners support vs. oppose such a change (53-22%).⁷

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

³ "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>

⁴ "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/>

⁵ Ibid.

⁶ "The average small business profit is less than \$71,000 annually. "How Much Do Small Business Owners Make? The Answer May Surprise You" Patriot Software. August 13, 2024. <https://www.patriotsoftware.com/blog/accounting/how-much-do-small-business-owners-make-average-income>

⁷ "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>

Revenue raisers supported by small businesses to offset investments in Main Street

For Congress to effectively support our nation's small businesses, especially the microbusinesses that are rooted in local communities, it must allocate sufficient funding and resources to the agencies and programs that offer the training, technical assistance, and financing that is essential for entrepreneurial and business growth across the country. This cannot be achieved without implementing some form of the revenue raising provisions outlined above, which guarantee that the wealthiest corporations and individuals contribute fairly to the tax system, relieving small businesses of the disproportionate burden they currently bear.

- **Increase the corporate tax rate:** The TCJA gave large C-corporations another unnecessary tax cut when it permanently lowered the domestic corporate tax rate from 35% to 21% - lower than the rate paid by many pass-through small businesses. This further reduced the tax liability of our nation's largest businesses. Since only 5% of small businesses are organized as C-corporations, this tax cut has had minimal positive impact on small businesses. Our recent poll found that a majority of small business owners support increasing the corporate tax rate to 28% to generate revenue.⁸
- **Bring the capital gains tax rate more in alignment with ordinary income tax rates:** An additional revenue raising proposal targeted at ensuring wealthy individuals pay their fair share includes bringing the capital gains tax rates more in line with ordinary income tax rates. In our recent poll, by a two-one margin, this reform is supported by small business owners for individuals with more than \$1 million in income (53% in favor vs. 27% opposed).⁹
- **Maintain the current level of the IRS funding to access revenue and serve small businesses:** As our tax code has become increasingly exploited by individuals and corporations that 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.¹⁰ When asked if they would support continued additional funding for the IRS, our research found that more than half 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 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%).¹¹ We urge Congress to reject any further proposed cuts to the IRS and continue to provide additional funding which will empower the agency to recover lost revenue to pay for the tax cuts we propose in this document.
- **Closing offshore tax loopholes:** 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 through 2027.¹² This system has allowed a few multinational corporations to continue funneling their profits to the lowest-taxation foreign jurisdictions. Small business owners strongly support closing offshore tax loopholes. In fact, 77% of small business owners agree that large corporations unfairly leverage their foreign

⁸ "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

⁹ "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>

¹⁰ "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>

¹¹ "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>

¹² "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>

presence to reduce their U.S. tax liability.¹³ 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’s national polling found that 71% of small business owners support setting a minimum tax rate of 21% on corporate offshore profits.¹⁴

Beyond the TCJA: Maintaining subsidies to ensure small business access to quality affordable healthcare

If Congress is serious about supporting small businesses through the tax code, lawmakers must also consider how existing tax credits and deductions, not included in the TCJA, can be extended to enhance the economic well-being of America’s entrepreneurs.

The Premium Tax Credit (PTC), which was established through the enactment of the Affordable Care Act (ACA), helps eligible individuals and families cover the cost of premiums for health insurance purchased through ACA marketplaces. In 2021, the American Rescue Plan Act (ARPA) increased the amount of these tax credits for those who were already eligible while also expanding eligibility for the 2021-2022 tax years to individuals with income levels above 400% of the federal poverty line, an income level into which many small business owners fall. The Inflation Reduction Act (IRA) later extended the temporary exception through the 2025 tax year.

The enhanced PTC has cut premium payments by an estimated 44% (\$705 annually) and expanded access to the create and healthcare coverage overall.¹⁵ With more than half of all ACA marketplace enrollees being either small business owners, self-employed individuals, or small business employees, and given that small business owners and self-employed individuals are three times more likely to rely on the ACA marketplace for coverage, these improvements have been a gamechanger for the small business ecosystem.^{16,17}

To ensure millions of Americans, including small business owners, entrepreneurs and their employees, can continue to access lower premium costs through the ACA, Small Business Majority urges Congress to make the tax credit enhancements included in the IRA permanent before they expire in 2025. If Congress fails to act, nearly 4 million Americans will become uninsured, and the average premium payment will increase by a staggering 93% from \$672 per year to \$1,296 per year in 2026.¹⁸ The permanency of the premium assistance will continue to keep health insurance premium costs affordable and expand access to coverage through the ACA Marketplace for entrepreneurs, providing them with the increased capacity to grow and expand their enterprises.

Tariffs and trade: The impact on a U.S. - China trade war on Main Street

Looking ahead to 2025, small business owners are already hunkering down to weather the almost painful impact of another potential trade war. For many business owners on Main Street, importing goods or parts from China is a common component of their supply chain. Therefore, it should come as no surprise that many businesses, from retailers to coffee shop owners, are expecting the proposed 60% tariffs on

¹³ “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>

¹⁴ “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>

¹⁵ “Inflation Reduction Act Health Insurance Subsidies: What is Their Impact and What Would Happen if They Expire?” KFF. July 26, 2024. <https://www.kff.org/affordable-care-act/issue-brief/inflation-reduction-act-health-insurance-subsidies-what-is-their-impact-and-what-would-happen-if-they-expire/>

¹⁶ “Small businesses see significant gains from the ACA.” Small Business Majority. October 16, 2018. <https://smallbusinessmajority.org/our-research/healthcare/small-businesses-see-significant-gains-aca>

¹⁷ “Affordable Care Act Marketplace Coverage for the Self-Employed and Small Business Owners.” U.S. Department of the Treasury. September 2024. <https://home.treasury.gov/system/files/131/ACA-Mkt-Coverage-Self-Employed-Small-Business-Owners09232024.pdf>

¹⁸ “Inflation Reduction Act Health Insurance Subsidies: What is Their Impact and What Would Happen if They Expire?” KFF. July 26, 2024. <https://www.kff.org/affordable-care-act/issue-brief/inflation-reduction-act-health-insurance-subsidies-what-is-their-impact-and-what-would-happen-if-they-expire>

Chinese imports to be detrimental. According to the National Retail Federation, American businesses, including those that are small, must shoulder the burden of tariffs. ¹⁹So far, the very same tariffs (section 301) imposed by the Trump administration in 2019 have cost Americans, including small business owners, a staggering \$129 billion. The incoming Trump administration has proposed also levying a universal 10% tariff across all imports, which would only harm the American economy as data consistently show that trade wars have raised prices and reduced growth.²⁰

When unilateral and retaliatory tariffs are implemented, the cost of goods and services will increase across the board. That is why businesses in our network have opposed tariffs, as we document below, but the sentiments remain consistent across industries represented: thoughtless and exorbitant tariffs will hurt America's smallest businesses the most. These quotes represent the thoughts and beliefs of members of our National Small Business Council, representing various industries across the U.S.

- Mike Roach, owner of Paloma Clothing in Portland, Oregon, opposes the prospect of higher tariffs on imports, stating that, “Our clothing store for women, Paloma Clothing, hopes to turn 50 next year. Our two top selling lines of clothing are made in China. The 60% proposed tariffs would make these lines unsellable and there are no comparable lines made in the U.S. or even in other countries at this time. The damage to our sales and to our long-time vendors would dramatically impact our business' ability to function long before those lines could pivot to other countries or the U.S. There are thousands of locally owned clothing stores in the country that are still trying to recover from the covid collapse of our industry. These tariffs could be the nail in the coffin for many of us.”
- Mike Brey, owner of Hobby Works in Laurel, Maryland, opposes the prospect of new tariffs, which would have a far-reaching negative impact on small businesses nationwide. Mike shared “We [Hobby Works] used to import accessory carrying bags of our own design through our WingTote subsidiary. Because it was a very heavy duty, but niche product, there was simply no way to manufacture this product in the U.S. We could only manufacture this product by piggybacking on other manufacturers' factory runs. Falling into the sewn sporting goods or luggage categories, they already carried a 17.9% tariff pre-pandemic. During the first Trump Administration an additional 25% tariff was added (not an increase of 25% as was widely reported) for a total tariff of 42.9%. There was simply no way to avoid passing virtually all of this cost on to the consumer because margins are already too narrow. Most toy, hobby, and game shops have net operating margins in the 5-10% range, which leaves very little room for retailers to absorb additional costs, so they get passed on to the consumer very quickly. The proposed tariffs would also have a negative impact on my cashflow, forcing me to raise the cost of goods just to stock my shelves. So, the negative effect of imposing tariffs is twofold: regressive tax on the consumer in the form of increased costs, PLUS delayed cash flow on the part of the retailer, manufacturer, etc. Those negative effects ripple all throughout the supply chain.”
- Clifton Broumand, Owner of Man and Machine in Landover, Maryland, strongly opposes the proposed tariffs, and is already considering moving his production out of the U.S. in response. Clifton shared, “If the new administration wants to damage export manufacturing and really kill domestic manufacturers, pass a bill similar to the Tarriff Act of 1930. We all want to strengthen our manufacturing base, but it's hard to understand how raising taxes through tariff increases aligns with the Republican value of lower taxes and lower costs for all Americans. If these tariffs go into place, I will have to move my production to Vietnam to compete with the Chinese in my export business. How does this help my employees? How does this help small businesses in our country?”
- Nikki Bravo, owner of Momentum Coffee in Chicago, Illinois shared “At Momentum Coffee, we're all about supporting our community and encouraging people to shop local. However, higher

¹⁹ “The Impact of Tariffs on Small Business” National Retail Federation. 2024. <https://nrf.com/hill/policy-issues/impact-tariffs-small-business>

²⁰ Trade Misery Impact Index. Americans for Free Trade. 2024. <https://americansforfreetrade.com/tariff-misery-impact/>

tariffs can make it tough because some of our supplies come from overseas. We have a real concern since we're a coffee shop, there's only so much we can pass on to our customers without affecting the neighborhoods we seek to serve and our mission to make quality coffee accessible. With a 60% tariff, it's hard to balance these added costs. Small margins made smaller can have some unintended consequences, especially for businesses like ours that are deeply tied to our communities. We know we'll need to explore options to offset the impact, but at this time, we're not certain what those options will look like."

While ensuring global competitiveness is a key issue for many small business owners, levying excessive tariffs on goods that small businesses depend on will not favor the smaller players in our economy. Instead, Congress should look to raise revenue in other ways that small business owners support, including revisiting the corporate rate, closing offshore loopholes, and bolstering tax enforcement across the board.

2025 offers a chance to address the shortcomings of the tax code and lay the foundation for a tax policy agenda that better serves small businesses

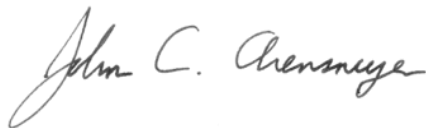
Small businesses need a simplified and streamlined tax system that will level the playing with large corporations. The TCJA was a false hope for our nation's smallest businesses that need the most relief, as it has failed to deliver for Main Street and instead has magnified the inequities in our tax code by slashing tax rates for wealthy corporations, expanding loopholes and further incentivizing corporations to move their profits offshore—leaving small businesses to bear the brunt of the tax burden head on.

The proposals outlined in my testimony reflect the opportunity for Congress to support Main Street entrepreneurs and put money back into their pockets. These priorities are shared by the diverse small business community that fuels economic innovation, local job growth, and the larger economy.

We hope the conversation today sheds light on some of the equitable solutions to achieving these goals to uplift our nation's smallest but most innovative job creators and economic contributors.

Thank you for your time and I look forward to taking your questions.

Sincerely,



John Arensmeyer
Founder & CEO
Small Business Majority