



January 23, 2019

The Honorable Steven T. Mnuchin
Secretary
Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

Dear Secretary Mnuchin:

I urge you to use your authority to modify the calculation of capital gains taxes to include an inflation adjustment. Ending the taxation of inflationary gains will have clear, immediate economic benefits and will increase the wealth of Americans across the country. There is also strong legal precedent, and historic support from Congress and within the administration for indexing capital gains taxes to inflation.

President Trump and Congress passed a bold, pro-growth tax reform bill late last year. However, because of legislative constraints, the bill could not contain every tax cut that Republicans have campaigned on.

The next step should be Treasury delivering a significant tax cut by using its regulatory authority to add an inflation adjustment to the calculation of capital gains taxes. I appreciate your acknowledgement that the policy of indexing capital gains to taxation is the right one, as noted in a [June 29 Wall Street Journal](#) article. However, I urge you to use Treasury's authority to add an inflation index rather than relying on Congress.

Treasury's authority to enact this tax cut has been analyzed by lawyers Charles J. Cooper, Michael A. Carvin and Vincent Colatriano in a [1993 legal memo](#) published in Virginia Tax Review, and again by Cooper and Colatriano in a [2012 legal memo](#) published in the Harvard Journal of Law and Public Policy.

Larry Kudlow, the Director of the National Economic Council, supports using your clear regulatory authority to index capital gains taxes to inflation. In a [CNBC op-ed](#) published on August 11, 2017, he described indexation as a way to "promote economic growth and prosperity:

President Trump's absolutely best economic policy so far has been his relentless rampage against onerous, burdensome, costly, prosperity-killing regulations on business. And the taxation of inflationary capital gains fits right in there. It is an unfair and misguided policy that punishes risk and success. The president should use his executive authority — as he so often has to drain the swamp — to remove this prosperity-killing practice.

This tax cut would have a strong, positive effect on the economy and will benefit millions of Americans that invest in the stock market, or own a 401(k) or IRA. This tax cut would also not require a Congressional Budget Office (CBO) score and would not need to be voted on by Congress.

Under current law, the capital gains tax fails to account for gains that are based on inflation. This unfairly exposes taxpayers to additional taxation. For example, an investor makes a capital investment of \$1,000 in 2000 and sells that investment for \$2,000 in 2017 will be taxed for a \$1,000 gain at a top capital gains tax rate of 23.8 percent. After adjusting for inflation, the "true gain" is much lower – just \$579. (1,000 in 2000 - \$1,421 in 2017).

According to a 2013 analysis by the Tax Foundation on individual capital gains taxes, the average effective rate excluding gains from inflation between 1950 and 2012 was [42.5 percent](#), nearly twice today's 23.8 percent top capital gains tax rate.

722 12th Street N.W.

Fourth Floor

Washington, D.C.

20005

T: (202)785-0266

F: (202)785-0261

www.atr.org

Treasury has the legal authority to index the calculation of capital gains taxes to inflation. Under the precedent set by the Supreme Court in *Chevron U.S.A. v. National Resources Defense Council (1984)*, the ability of Treasury to add an inflation adjustment hinges on whether a new definition of “cost” is plausible. Currently, the capital gains tax is calculated as the difference between the cost of the asset and the sale price of the asset.

While in this context, “cost” is commonly understood to mean historical cost, this definition is not explicitly enshrined in law and Treasury has utilized regulatory discretion in the past. For instance, in 1918, Treasury decided that an asset’s cost was not strictly purchase price but was purchase price less depreciation and depletion taken by the taxpayer prior to sale.

Recent legal precedent proves that there is precedent for the term “cost” to include inflation. For instance, in *Verizon v. FCC (2002)* the Supreme Court affirmed that the term “cost” was ambiguous and the use of historical cost was not required by law. *National Cable & Telecommunications Ass’n v. Brand X Internet Services (2005)*, affirmed the right of an agency to interpret an ambiguous provision of the law, while in *Mayo Foundation for Medical Education & Research v. United States (2011)*, the Supreme Court affirmed that the Chevron doctrine applies to Treasury regulations.

Further, in their memos, Carvin, Cooper and Coltriano explained how the Justice Department’s 1992 memo did not fully examine the issue of indexing capital gains to inflation. For example, the Department’s memo argued the term “cost” in the Revenue Act of 2018 was not ambiguous because several dictionaries gave one of the definitions of cost as price paid. However, Cooper and Coltriano pointed out that Congress has never defined the term “cost” and that many dictionaries define the term “cost” broadly, such as the Random House Dictionary. The Justice Department’s memo also cited cases where the courts have purportedly defined “cost” as price paid. However, these decisions never stated that Treasury could not index capital gains for inflation. In addition, more recent cases, such as [Mercy Community Hospital v. Heckler](#), have included inflation in cost. Finally, the Justice Department’s memo relies on legislative history, specifically Representative Hardy’s [amendment](#). However, Hardy’s amendment was not about indexing capital gains to inflation. Rather, Hardy was concerned that gains from prior years would be taxed when property was sold.

There is significant support for indexing the calculation of capital gains taxes to inflation in Congress, and from economists:

- Current and former members of Congress, led by Vice President Mike Pence support indexing capital gains taxes to inflation. In the 115th Congress, Senator Ted Cruz (R-Texas) introduced legislation in the Senate [\[link\]](#) and Congressman Devin Nunes (R-Calif.) introduced legislation in the House [\[link\]](#) that would index capital gains taxes to inflation. Pence introduced legislation in 2007 with 88 co-sponsors including now-Acting Chief of Staff Mick Mulvaney, former House Speaker Paul Ryan (R-Wis.) and former House Ways and Means Chairman Kevin Brady (R-Texas).
- Economist Richard Rahn’s recent op-ed in the *Washington Times*: “Capital gains must be protected from inflation” [\[link\]](#)
- Americans for Tax Reform recently led a coalition of 51 conservative free-market, pro-business, and pro-family activists and organizations in a letter calling for President Trump to end the inflation tax on capital gains. [\[link\]](#)

Given the clear economic rationale, strong legal precedent, and significant congressional and administration support for indexation, I urge Treasury to swiftly utilize its regulatory authority and index capital gains taxes to inflation.

Sincerely,

Grover G. Norquist



President

Americans for Tax Reform