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Moore v. United States – High Court Limits Scope of Tax Case but Leaves Door Ajar for Wealth Tax

Paul Kieffer, CPA/PFS, CFP,® Senior Wealth Planner

In a closely watched case, the Supreme Court issued a divided decision in Moore v. United States[1] on June 20, 2024, upholding the constitutionality of the Mandatory Repatriation Tax (MRT). The MRT is a provision of the 2017 Tax Cuts and Jobs Act (TCJA) that taxes U.S. shareholders on their pro rata share of the undistributed income earned by certain foreign corporations they control.

The court ruled 7–2 against Charles and Kathleen Moore, who challenged their tax liability on an investment in India that resulted from the 2017 law. Justices Clarence Thomas and Neil Gorsuch dissented. Justice Brett Kavanaugh wrote the majority opinion, but justice Amy Coney Barrett wrote a separate concurring opinion that Justice Samuel Alito joined. Justice Ketanji Brown Jackson also wrote a separate concurring opinion.

The Tax Foundation estimated that a ruling in favor of the Moores could have cost the US Treasury more than $300 billion in both refund claims and reduced future revenue.[2]

Perhaps a larger concern was the potential impact of this decision on the ability of Congress to create and impose wealth taxes. In the initial oral arguments, the justices indicated their concern about the unintended consequences of their ruling on both sides of the argument.

The court clearly did not want the case used as precedent for deciding whether a wealth tax is constitutional. The decision stated that the court's analysis does not address issues raised by taxes on holdings, wealth, or net worth.[3]

The decision could have significantly affected the US tax system but was narrowly focused so it would not. Consequently, the door on a wealth tax has not been shut completely, but it has not been opened any further, either.

Background of Moore v. US

In 2005, Charles and Kathleen Moore invested in a company in India. They held an 11% share of KisanKraft, which supplied modern tools to small farmers there. They never received any income (interest, dividends, or 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 TCJA, which included an MRT on foreign investments. Before the TCJA, a US taxpayer who held shares in a foreign corporation that earned income overseas did not 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% 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 challenged 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 was much more than just the Moores claim threatening the US Treasury's coffers.

The 16th Amendment to the US Constitution, ratified in 1913, allowed Congress to levy an income tax without apportioning it to the states. Historically, the government imposed those taxes on realized income (earnings, interest, rents, dividends, etc.).

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

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

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 attorneys countered that there was never a constitutional realization requirement. They said imposing one now would upend a significant amount of the current tax code.

What is a wealth tax?

A wealth tax differs from the traditional system of taxation, in which rates increase as more taxable income is earned. A wealth tax is imposed on the taxpayer's net worth regardless of income. It can take several 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 buys a security for $5,000 and continues to own it while its 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.

Senator Ron Wyden introduced one such wealth tax 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.

Continued on page 3

Marketable securities would be valued on an annual basis. Any increase in value would be taxable regardless of whether the securities have been sold. 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.

Wyden's proposal and others did not get very far in Congress, but they could be an indicator of some of the thinking in Washington that could affect future tax policy.

For more information, please contact your advisor.

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[1] 601 U.S. ___(2024)
[2] Moore v. United States: Tax Unrealized Income Case (taxfoundation.org)
[3] 22-800 Moore v. United States (06/20/2024) (supremecourt.gov)

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