Walmart's Executive Bonuses

Cost Taxpayers Millions

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June 2014

Credits

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Americans for Tax Fairness is a diverse coalition of 400 national and state organizations that collectively represent tens of millions of members. The organization was formed on the belief that the country needs comprehensive, progressive tax reform that results in greater revenue to meet our growing needs. ATF is playing a central role in Washington and in the states on federal tax-reform issues.

The **Institute for Policy Studies** (www.IPS-dc.org) is a 50-year-old multi-issue research center that has conducted path-breaking research on executive compensation for 20 years. A May 2013 IPS report, '*Fix the Debt' CEOs Enjoy Taxpayer-Subsidized Pay,* was the first to put a price tag on the tax subsidies specific corporations have enjoyed from the "performance pay" loophole.

The Institute for Policy Studies web site http://inequality.org/ is a portal into all things related to the income and wealth gaps that so divide us, in the United States and throughout the world.

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Key Findings

Walmart, the largest private U.S. employer with 1.4 million employees,[1] has been widely criticized for shifting the costs of its low-wage model onto taxpayers. Hourly employees receive low-level if not poverty wages and inadequate benefits and many of them are forced to work part-time, leaving thousands with little choice but to rely on public assistance.

While Walmart is shortchanging its employees, it is lavishing excessive pay on its executives.

This report reveals that taxpayers subsidize much of the cost of these "bonuses."[2] Specifically, the report calculates the cost of a tax loophole that allows Walmart and other corporations to deduct unlimited amounts from their income taxes for the cost of executive compensation if it is in the form of stock options and other so-called "performance pay." This tax loophole serves as a massive subsidy for excessive executive compensation and leaves other taxpayers to pick up the tab. **In effect, the larger the executive payouts the less Walmart pays in taxes**.

Key findings in this report include:

- **$104 Million:** Walmart reduced its federal tax bills by an estimated $104 million over the past six years by exploiting a tax loophole that allowed eight top executives to pocket more than $298 million in "performance pay" that was fully tax deductible. That sum would have been enough to cover the cost of free school lunches for 33,000 children for those six years.

- **$40 Million:** Michael T. Duke, Walmart's recently retired President & CEO and currently Chairman of the Executive Committee of the Board of Directors, pocketed nearly $116 million in exercised stock options and other "performance pay" during the period 2009-2014. That translates into a taxpayer subsidy for Walmart of more than $40 million—enough to cover the average cost of food stamps for 4,200 people for those six years.

- **$50 Billion:** Taxpayers would save $50 billion over 10 years, according to the Joint Committee on Taxation, if Congress closed this perverse "performance pay" loophole by capping the tax deduction at $1 million for each employee's total compensation, with no exceptions for performance pay.

These new findings underscore the findings from a recent report by Americans for Tax Fairness, Walmart on Tax Day: How Taxpayers Subsidize America's Biggest Employer and Richest Family.[3] It estimated that taxpayers spend $7.8 billion a year subsidizing Walmart and the Walton family, which owns more than 50 percent of Walmart, by providing public assistance to the company's employees and through various other subsidies and tax breaks.

In effect, taxpayers pay twice for Walmart's pay practices—they subsidize the company's excessive executive pay and they subsidize its low wages paid to rank-and-file employees.

Taxpayers Pay Twice for Walmart's Pay Practices

Walmart ranked number one on the *Fortune* 500 and number two on the Global 500 in 2013,[4] with $16 billion in profits on revenues of $473 billion.[5] One way the corporation boosts its bottom line is through pay practices that place a double burden on U.S. taxpayers. First, Walmart takes advantage of tax subsidies for excessive executive compensation, so that the more Walmart pays its top executives the more it cuts its tax bill. Second, taxpayers provide public assistance to Walmart workers to subsidize the low-wages the company pays its employees.

Burden #1: Taxpayer Subsidies for Executives' Pay at the Top

Walmart's executive pay practices are a burden on taxpayers because they subsidize pay at the top of the corporate ladder. These subsidies are the result of a loophole that allows all U.S. publicly held corporations to deduct unlimited amounts from their income taxes for the cost of executive stock options, certain stock grants and other forms of so-called "performance pay." In effect, these companies are exploiting the U.S. tax code to send taxpayers the bill for the huge bonuses they're doling out to their top executives.

Burden #2: Public Assistance for Walmart Employees at the Bottom

As documented in the report Walmart on Tax Day, Walmart receives an estimated $6.2 billion annually in taxpayer subsidies (and another $1.6 billion in tax breaks, some of which goes to the Walton family). The reason: Walmart pays its employees so little that many of them and their families rely on food stamps, Medicaid, public housing, school food programs and other taxpayer-funded assistance.

Ironically, while Walmart relies on public subsidies to support its employees, the company also benefits significantly from taxpayer-funded public assistance programs that pump up the retailer's sales. For example, Walmart had an estimated $13.5 billion in food stamp sales last year.[6]

> ***"Taxpayers are losing billions of dollars; shareholders are being taken for a ride."***
>
> **—Former Labor Secretary Robert Reich, commenting on the "performance pay" loophole**

Origin of the “Performance Pay” Tax Loophole

In 1993, Congress took action to discourage excessive executive compensation. The result was section 162(m) of the tax code, which caps the amount corporations can deduct from their income taxes for executive pay at no more than $1 million per executive.[7]

Without putting a ceiling on executive pay, this reform aimed to set a limit on what could be considered a reasonable business expense worthy of a tax deduction. But the law included a huge loophole exempting “performance-based” pay from the $1 million limit. This quickly led to an explosion of tax-advantaged compensation, particularly in the form of stock options.

Does High Performance Pay Mean High Performance?

The initial rationale for the “performance pay” loophole was that stock options were a means to align the interests of executives and shareholders. But that hasn’t been the case in practice. When a firm’s shares decline in value, shareholders lose, while corporate boards often position executives for huge windfalls by doling out new options with lower exercise prices. For example, the board of Goldman Sachs awarded ten times as many executive stock options when the firm’s stock was trading at record lows in 2008, compared to pre-crash years.[8]

Stock options have also been widely criticized for encouraging reckless executive behaviors designed to jack up share prices in the short-term—even if they undermine the corporation’s long-term health. In response, many firms have shifted some executive compensation from stock options to grants of stock conditioned on meeting specific performance metrics. A 2013 Bloomberg investigation revealed, however, that this form of pay can also be easily manipulated to reward poor performers.[9] According to the report, CEOs at 63 companies in the S&P 500 got “performance pay” increases in 2012 even though their share returns had underperformed their index peers.

A more recent paper by the consulting firm Arthur J. Gallagher & Company found similar disconnects between performance pay metrics and corporate performance.[10] One of the paper’s authors told the *The New York Times* he suspects corporate boards favor metrics that are easily manipulated.[11]

Walmart is a case in point. This year the company “replaced a crucial metric for assessing executives’ performance,” according to the *The New York Times*.[12] This helped executives meet their bonus benchmarks—and helped Walmart obtain their “performance pay” tax subsidy.

The “performance pay” loophole, in short, serves as a critical subsidy for excessive compensation. The larger the executive payout, the less the corporation pays in taxes. And average taxpayers wind up footing the bill. As former Labor Secretary Robert Reich, a long-time critic of the “performance pay” loophole, told Bloomberg News: “Taxpayers are losing billions of dollars; shareholders are being taken for a ride.”

Taxpayer Subsidies for Walmart's Executive Bonuses

During the past six years, eight top executives at Walmart pocketed $298.6 million in fully deductible "performance pay," lowering the company's federal tax bills by an estimated $104 million.

The table below provides a summary of the pay subsidies for each of the Walmart executives that were covered by the "performance pay" loophole during 2009-2014. See Appendix I for a fuller detailing of the pay subsidies and Appendix II for an explanation of the sources and methodology for calculating pay subsidies.

Tax Subsidies for Walmart's Executives' Bonuses, 2009-2014

Years Listed in Proxy as Top Executive During FY09-14	Executive	Position	Total Taxable Compensation in Year Surveyed	Portion of Compensation that is "Performance-based"	Value of Walmart's Executive Pay Subsidy
6	Michael T. Duke*	President & CEO	$125,908,779	$115,788,856	$40,526,100
6	Doug McMillon*	Executive VP	$65,289,514	$58,276,364	$20,396,727
4	Bill Simon	Executive VP	$33,013,862	$28,777,510	$10,072,129
2	Neil Ashe	Executive VP	$5,121,954	$3,584,918	$1,254,721
2	Rosalind Brewer	Executive VP	$13,484,900	$11,221,295	$3,927,453
2	Brian Cornell	Fmr. Executive VP	$14,427,097	$10,477,918	$3,667,271
1	Lee Scott	Fmr. President & CEO	$35,574,881	$33,466,396	$11,713,239
3	Eduardo Castro Wright	Fmr. Vice Chair	$41,387,749	$36,564,615	$12,939,975
	TOTAL		**$334,208,736**	**$298,564,615**	**$104,497,615**

*McMillon replaced Duke as CEO on Jan. 31, 2014. Duke remains Chair of the Executive Committee of the Board.

Source: Wal-Mart Stores, Inc. proxy statements filed with the Securities and Exchange Commission.

Social Costs of Tax Subsidies for Walmart's Executive Bonuses

At a time of budget squeezing in Washington, tax dollars devoted to subsidizing executive bonuses really add up.

For example, the $104 million in total pay subsidies to Walmart executives would be enough to cover the cost of free school lunches for 33,000 children for six years.[13] Although exact numbers are unavailable, we estimate that hundreds of thousands of Walmart workers' families qualify for free and reduced-price school lunches.[14]

Or consider another public assistance program on which millions of low-wage workers rely—the Supplemental Nutrition Assistance Program, commonly known as food stamps. On average, this program costs $133 per month per household.[15] The $40.5 million tax subsidy over six years related to executive compensation for just one individual—Michael T. Duke, Walmart's recently retired CEO—would be enough to cover the average cost of food stamps for more than 4,200 people for six years.[16]

Then there's the $50 billion total cost of the executive pay tax loophole over 10 years, as estimated by the Joint Tax Committee.[17] That is two-thirds the $75 billion cost over 10 years of President Obama's plan to provide all low- and moderate-income 4-year-olds with high-quality, publicly funded preschool.[18]

Social Costs of Tax Subsidies for Walmart's Executive Bonuses

$104 Million	
Cost of tax subsidies for 8 Walmart executives' pay over 6 years	**Cost of providing 33,000 children with school lunches for 6 years**
$40.5 Million	
Cost of tax subsidies for Walmart's CEO pay over 6 years	**Cost of providing food stamps to 4,200 people for 6 years**
$50 Billion	
10-year savings from closing the executive pay tax loophole	**Two-thirds of the $75 billion cost (over 10 years) of President Obama's plan to provide pre-K education to all 4-year-olds**

Ending Taxpayer Subsidies for Executive Bonuses

Congress passed legislation in 1993 that capped the tax deductibility of executive pay at $1 million but with a huge exemption – corporations could still deduct unlimited amounts of "performance-based" pay from their federal income taxes.[19]

To close this perverse "performance pay" loophole, members of Congress have introduced bills that would set a $1 million cap on the tax deductibility of compensation for all employees – with no exceptions. Senators Jack Reed (D-R.I.) and Richard Blumenthal (D-Conn.) have introduced S. 1476, the Stop Subsidizing Multimillion Dollar Corporate Bonuses Act.[20] Rep. Lloyd Doggett (D-Texas) has introduced a companion bill, HR 3970.[21] The Joint Committee on Taxation estimates this legislation would generate more than $50 billion over 10 years.[22]

Rep. Dave Camp (R-Mich.), Chairman of the House Ways & Means Committee, made a similar proposal in his comprehensive tax reform plan (Section 3802).[23] Camp's proposal, which would cover only a company's top five executive officers, would generate $12.1 billion over 10 years.

Rep. Barbara Lee (D-Calif.) has introduced another variation, the Income Equity Act (H.R. 199), which would deny all firms tax deductions on any executive pay that exceeds over 25 times the pay of a firm's lowest-paid employee or $500,000, whichever is higher.

The Income Equity Act could have an important impact on lower-level workers as well. By including the option of limiting deductibility to no more than 25 times the pay of the lowest-paid employee, Rep. Lee's bill would encourage corporations to raise pay at the bottom of the corporate pay ladder. The greater the pay for a company's lowest-paid worker, the higher the tax-deductible pay for the company's highest-paid executives.

These bills do not set a ceiling on, or dictate in any way, how much corporations can pay their executives. Corporations could still freely pay their executives outlandishly large sums. But the federal government—and average American taxpayers—would no longer pick up the tab.

These bills would build on precedents in the Troubled Assets Relief Program (TARP) and the Affordable Care Act that set a $500,000 deductibility cap on pay for bailout recipients and health insurance firms.[24] The deductibility caps on health insurance firms, designed to discourage these corporations from using profits from premiums to overcompensate their executives, go into effect this year.

It's time Congress closed the "performance pay" loophole to end taxpayer subsidies for excessive executive pay.

Appendix I: Pay Subsidies Among Walmart's Top Executives (Expanded Version)

For a spreadsheet showing the basis for the calculations in the table, click this link.

Executive	Position	Fiscal Years	Total Taxable Compensation in Year Surveyed	Portion of Compensation that is "Performance-based"	Value of Walmart's Executive Pay Subsidy
Michael T. Duke*	President & CEO	2014	$24,572,506	$22,715,823	$7,950,538
	President & CEO	2013	$27,760,161	$25,799,980	$9,029,993
	President & CEO	2012	$19,650,818	$18,008,785	$6,303,075
	President & CEO	2011	$23,154,123	$21,444,886	$7,505,710
	President & CEO	2010	$16,272,726	$14,751,280	$5,162,948
	Vice Chairman	2009	$14,498,445	$13,068,102	$4,573,836
		Subtotal	**$125,908,779**	**$115,788,856**	**$40,526,100**
Doug McMillon*	Executive VP	2014	$10,893,231	$9,684,732	$3,389,656
	Executive VP	2013	$16,024,578	$14,806,372	$5,182,230
	Executive VP	2012	$ 9,362,165	$8,267,607	$2,893,662
	Executive VP	2011	$13,408,410	$12,321,594	$4,312,558
	Executive VP	2010	$7,805,308	$6,478,122	$2,267,343
	Executive VP	2009	$7,795,822	$6,717,937	$2,351,278
		Subtotal	**$65,289,514**	**$58,276,364**	**$20,396,727**
Bill Simon	Executive VP	2014	$10,112,500	$9,044,214	$3,165,475
	Executive VP	2013	$12,678,954	$11,565,607	$4,047,962
	Executive VP	2012	$6,510,019	$5,455,300	$1,909,355
	Executive VP	2011	$3,712,389	$2,712,389	$949,336
		Subtotal	**$33,013,862**	**$28,777,510**	**$10,072,129**
Neil Ashe	Executive VP	2014	$4,584,918	$3,584,918	$1,254,721
	Executive VP	2013	$537,036	$0	$0
		Subtotal	**$5,121,954**	**$3,584,918**	**$1,254,721**
Rosalind Brewer	Executive VP	2014	$7,703,144	$6,509,691	$2,278,392
	Executive VP	2013	$5,781,756	$4,711,604	$1,649,061
		Subtotal	**$13,484,900**	**$11,221,295**	**$3,927,453**
Brian Cornell	Executive VP	2012	$10,677,423	$9,145,315	$3,200,860
	Executive VP	2010	$3,749,674	$1,332,603	$466,411
		Subtotal	**$14,427,097**	**$10,477,918**	**$3,667,271**

Executive	Position	Fiscal Years Employed	Total Taxable Compensation in Year Surveyed	Portion of Compensation that is "Performance-based"	Value of Walmart's Executive Pay Subsidy
Lee Scott	President and CEO	2009	**$35,574,881**	**$33,466,396**	**$11,713,239**
Eduardo Castro Wright	Vice Chairman	2011	$18,756,930	$17,287,790	$6,050,727
	Vice Chairman	2010	$10,591,587	$9,273,288	$3,245,651
	Vice Chairman	2009	$12,039,232	$10,410,280	$3,643,598
		Subtotal	**$41,387,749**	**$36,971,358**	**$12,939,975**
		TOTAL	**$334,208,736**	**$298,564,615**	**$104,497,615**

*McMillon replaced Duke as CEO on Jan. 31, 2014. Duke remains Chair of the Executive Committee of the Board.

Source: Wal-Mart Stores, Inc. proxy statements filed with the Securities and Exchange Commission.

Appendix II: Pay Subsidies Sources & Methodology

1. Walmart's Top Executives

Walmart's corporate proxy statements were accessed in May 2014. All executives listed in the proxy statements were included except the chief financial officers, which are currently exempted from the relevant tax loophole (see #3 below).

2. Total Taxable Compensation

Analysis based on Walmart's corporate proxy statements. To analyze the tax implications, we included forms of pay that were taxable for the corporation in the years surveyed: salary, bonus, non-equity incentives, perks, and the value of options realized and vested stock. Corporations do not deduct the expense of stock options until the year in which they are exercised and do not deduct the expense of stock award grants until the year they "vest" (i.e., become the property of the employee).

3. Portion of compensation that is "performance-based"

Internal Revenue Code Section 162(m) imposes a $1 million deduction limit for compensation to a company's CEO and its three other highest-paid executive officers (excluding the CFO), unless the compensation is "performance-based" and provided under a plan that has been approved by the shareholders. The following is an analysis of how components of compensation packages are treated under this section of the tax code:

Bonus: Although we use the term "bonus" in the body of this report to refer to performance pay, the specific type of compensation labeled "bonus" in the summary compensation table of corporate proxy statements is generally not considered performance-based. This is because the type of bonus reported here is typically a cash payout awarded at the board's discretion rather than pursuant to a written plan approved by shareholders, one of the conditions for qualifying as "performance-based" under Section 162(m). At Walmart, none of the annual cash bonuses were configured to be 162(m)-compliant.

Non-equity incentive plan compensation: Similar to a bonus, but paid under a written plan and thus considered "performance-based."

Stock options: Considered "performance-based." We included the value of options exercised, rather than the estimated value of a stock options grant, since options are not taxable until an executive exercises them.

Stock grants: Considered "performance-based" under 162(m) only when tied to specific performance benchmarks. Time-based restricted stock units do not qualify for the "performance-based" exemption. Like stock options, stock grants are not taxable in the year they are granted, but rather when they vest. When proxy statements did not clarify whether stock grants had been structured to qualify for a deduction under 162(m), we did not include them in our calculations of executives' pay subsidies.

Salary, perks, pensions, and nonqualified deferred compensation are not considered "performance-based."

4. Value of Walmart's executive pay subsidy

Corporations can deduct up to $1 million of each executive's compensation whether it is "performance-based" or not. Thus, when executives earned less than $1 million in non-performance-based pay, we deducted the difference from the performance pay total. To compute the tax break on qualifying performance pay, we applied the federal corporate tax rate of 35 percent.

As with most tax matters, there is some gray area in the tax code when it comes to deductions for executive compensation. Some companies note in their proxy statements that the IRS may challenge some of a firm's claimed deductions. Unfortunately, due to lack of transparency in corporate taxation, such challenges are not public information.

Endnotes

[1] Alexander E.M. Hess, "The 10 largest employers in America," *USA Today* (August 22, 2013). http://www.usatoday.com/story/money/business/2013/08/22/ten-largest-employers/2680249/. Wal-Mart Stores, Inc., Form 10-K (filed March 21, 2014), p. 3. http://www.sec.gov/Archives/edgar/data/104169/000010416914000019/wmtform10-kx13114.htm

[2] The term "bonus" is used in the body of this report to refer to compensation that is awarded on top of an executive's base salary and perks. It should be noted, however, that the specific type of compensation labeled "bonus" in the summary compensation table of corporate proxy statements is generally not considered performance-based under Section 162(m) of the tax code. This is because the type of bonus reported in that table is typically a cash payout awarded at the board's discretion rather than pursuant to a written plan approved by shareholders, one of the conditions for qualifying as "performance-based" under Section 162(m).

[3] Americans for Tax Fairness (ATF), "Walmart on Tax Day: How Taxpayers Subsidize America's Biggest Employer and Richest Family" (April 2014). http://www.americansfortaxfairness.org/files/Walmart-on-Tax-Day-Americans-for-Tax-Fairness-1.pdf

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[8] Sam Pizzigati, "A Call from Labor: Ban Big Bank Stock Options," *Too Much* (June 3, 2011). http://toomuchonline.org/call-from-labor-ban-bank-stock-options/

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[12] Gretchen Morgenson, "Moving the Goal Posts on Pay," *The New York Times* (May 7, 2014). http://www.nytimes.com/2011/05/08/business/08gret.html

[13] For this calculation we used the cost of school lunches of $2.93 taken from the USDA *School Lunch Program* summary at http://www.fns.usda.gov/sites/default/files/NSLPFactSheet.pdf and the average number of school days per year of 180 from the Education Commission of the States at http://www.ecs.org/html/Document.asp?chouseid=7824. $2.93 a lunch for 180 days = $527.40 for a school year. $104,497,615 in tax subsidies divided by $527.40 = 198,137 lunches for a school year or 33,023 lunches for six school years.

[14] As noted in ATF's "Walmart on Tax Day" report, there is no systematic record of the number of people, by employer, who utilize various public assistance programs. The USDA states, "Children from families with incomes at or below 130 percent of the poverty level are eligible for free meals. Those with incomes between 130 percent and 185 percent of the poverty level are eligible for reduced-price meals, for which students can be charged no more than 40 cents. (For the period July 1, 2013, through June 30, 2014, 130 percent of the poverty level is $30,615 for a family of four; 185 percent is $43,568.)" As many as 825,000 Walmart workers make less than $25,000 a year. Source: http://makingchangeatwalmart.org/2013/10/23/825k-living-on/

[15] Center on Budget and Policy Priorities, "Policy Basics: Introduction to the Supplemental Nutrition Assistance Program (SNAP)" (March 19, 2014). http://www.cbpp.org/cms/index.cfm?fa=view&id=2226

[16] For this calculation we used the average cost of SNAP benefits per person per month – $133 in 2013, or $1,596 a year – taken from the Center on Budget and Policy Priorities at

http://www.cbpp.org/cms/index.cfm?fa=view&id=2226. $40,526,100 in tax subsidies for Michael Duke divided by $1,596 = 25,392 people served in one year, or 4,232 people served for six years.

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[20] Sen. Reed News Release.

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[22] Sen. Reed News Release. Sen. Reed's staff has not released the legislation's score by the Joint Tax Committee.

[23] Chairman Dave Camp, House Committee on Ways and Means, "Tax Reform Act of 2014 Discussion Draft" (Feb. 26, 2014). http://waysandmeans.house.gov/uploadedfiles/ways_and_means_section_by_section_summary_final_022614.pdf

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