



The Economic Effects of the Estate Tax

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Estate Tax and Estate Planning

- Kopzcuk and Slemrod (2000)
 - Wealth responds to the estate tax that prevails during a saver's lifetime
 - A 50 percent estate tax lowers net worth by about 10 percent
 - Holtz-Eakin and Marples (2001) confirm the link, and even find an elasticity bigger than one
 - Large elasticities are plausible because large lawyer fees are present.

Estate Tax and Small Business

- The approach of an estate tax “event” significantly reduces employment growth in affected small businesses and the estate tax also reduces investment (Holtz-Eakin et al. (1999), Carroll et al. 2000).
- Estate funds get poured back into small businesses as well (Holtz-Eakin et al. 1993, 1994)

Theoretical Background

- Estate tax, like capital gains tax, can be best integrated with existing capital tax theory by using the notion of “accrual equivalence.”
- Since the estate tax hits the whole thing, not just the income, it implies enormous accrual equivalent rates, depending on the time period over which the rate is calculated.
- The capital tax equivalent is pretty indefensible on theoretical grounds.

Table 4

Current Law - Death Tax Exemption and Top Marginal Rate

<i>Year</i>	<i>Exemption (Millions)</i>	<i>Top Marginal Rate</i>
2008	\$2	45%
2009	\$3.5	45%
2010	--	0%
2011	\$1	60%

Table 5

Top Tax Rates under Current Law and Obama Proposal

	Top Tax Rate 2009-2010	Top Tax Rate 2011	Top Tax Rate Obama Proposal
Personal Income	35%	39.6%	39.6%
Capital Gains	15%	20%	20%
Dividends	15%	39.6%	20%

Table 7

Annual Capital Income Tax Rates Equivalent to Death Tax (Percent)							
Policy Option		Expected Life					
		5	10	15	20	25	30
Eliminate Death Tax (0%)	Level	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	Change from 2009	-152.1%	-78.3%	-52.7%	-39.8%	-31.9%	-26.6%
2009 Law Permanent (45%)	Level	152.1%	78.3%	52.7%	39.8%	31.9%	26.6%
	Change from 2009	73.9%	39.9%	27.3%	20.7%	16.7%	14.0%
Current Law (60%)	Level	226.1%	118.2%	80.0%	60.5%	48.6%	40.6%
	Change from 2009	73.9%	39.9%	27.3%	20.7%	16.7%	14.0%

Conclusion

- The estate tax, like a wealth tax, is an especially damaging capital tax because the income tax equivalent rates are higher than you might think. It is analogous to the tax inclusive vs. tax exclusive sales tax problem.
- Extending current law will likely offset a healthy chunk of the stimulus effect next year

Table 1

Recent Structure of the Estate Tax

Taxable Estate	Tax Liability
Not over \$10,000	18 percent of such amount
Over \$10,000 but not over \$20,000	\$1,800 plus 20 percent of excess over \$10,000
Over \$20,000 but not over \$40,000	\$3,800 plus 22 percent of excess over \$20,000
Over \$40,000 but not over \$60,000	\$8,200 plus 24 percent of excess over \$40,000
Over \$60,000 but not over \$80,000	\$13,000 plus 26 percent of excess over \$60,000
Over \$80,000 but not over \$100,000	\$18,200 plus 28 percent of excess over \$80,000
Over \$100,000 but not over \$150,000	\$23,800 plus 30 percent of excess over \$100,000
Over \$150,000 but not over \$250,000	\$38,800 plus 32 percent of excess over \$150,000
Over \$250,000 but not over \$500,000	\$70,800 plus 34 percent of excess over \$250,000
Over \$500,000 but not over \$750,000	\$155,800 plus 37 percent of excess over \$500,000
Over \$750,000 but not over \$1,000,000	\$248,300 plus 39 percent of excess over \$750,000
Over \$1,000,000 but not over \$1,250,000	\$345,800 plus 41 percent of excess over \$1,000,000
Over \$1,250,000 but not over \$1,500,000	\$448,300 plus 43 percent of excess over \$1,250,000
Over \$1,500,000 but not over \$2,000,000	\$555,800 plus 45 percent of excess over \$1,500,000
Over \$2,000,000 but not over \$2,500,000	\$780,800 plus 49 percent of excess over \$2,000,000
Over \$2,500,000 but not over \$3,000,000	\$1,025,800 plus 53 percent of excess over \$2,500,000
Over \$3,000,000	\$1,290,800 plus 55 percent of excess over \$3,000,000
Over \$10,000,000 but not over \$17,184,000	Additional 5 percent surtax

Source: U.S. Tax Code

Note: Over the life of EGTRAA, successive lower brackets have been removed. Depending on the tax code and year, various combinations of exemption amounts and rates exist. In 2009, for example, the only rate is 45 percent on the excess of \$3.5 million, and in 2010, no rate applies. For 2011 (should EGTRAA expire), the first dollar taxed is \$1,000,001, at a rate of 41 percent, and the subsequent rates apply. For example, with an estate valued at \$2,750,000, the total liability would be \$1,157,500.

Table 2

The Role of the Estate Tax in Federal Revenues
(Millions of Dollars)

Year	Total federal collections	Individual Income Tax	Estate Tax	Gift Tax
<i>1995</i>	1,375,731 (100%)	675,779 (49.1%)	13,326 (1.0%)	1,818 (0.1%)
<i>1996</i>	1,486,546 (100%)	745,313 (50.1%)	15,350 (1.0%)	2,241 (0.2%)
<i>1997</i>	1,623,272 (100%)	825,020 (50.8%)	17,595 (1.1%)	2,761 (0.2%)
<i>1998</i>	1,769,408 (100%)	928,065 (52.5%)	21,314 (1.2%)	3,316 (0.2%)
<i>1999</i>	1,904,151 (100%)	1,002,185 (52.6%)	23,627 (1.2%)	4,758 (0.2%)
<i>2000</i>	2,096,916 (100%)	1,137,077 (54.2%)	25,618 (1.2%)	4,103 (0.2%)
<i>2001</i>	2,128,831 (100%)	1,178,209 (55.3%)	25,289 (1.2%)	3,958 (0.2%)
<i>2002</i>	2,016,627 (100%)	1,037,733 (51.5%)	25,532 (1.3%)	1,709 (0.1%)
<i>2003</i>	1,952,929 (100%)	987,208 (50.6%)	20,887 (1.1%)	1,939 (0.1%)
<i>2004</i>	2,018,502 (100%)	990,248 (49.1%)	24,130 (1.2%)	1,449 (0.1%)
<i>2005</i>	2,268,895 (100%)	1,107,500 (48.8%)	23,565 (1.0%)	2,040 (0.1%)
<i>2006</i>	2,518,680 (100%)	1,236,259 (49.1%)	26,717 (1.1%)	1,970 (0.1%)
<i>2007</i>	2,691,537 (100%)	1,366,241 (50.8%)	24,557 (0.9%)	2,420 (0.1%)

Source: IRS and author computations

Table 3

Number and Revenue by Size of Estate

Size of Taxable Estate	2007		2005		2003	
	Number	Amount (Millions)	Number	Amount (Millions)	Number	Amount (Millions)
< \$2.0 million	3,681	4,586	17,792	21,889	47,598	46,171
\$2.0 < \$3.5	18,953	36,324	13,462	23,571	12,463	19,474
\$3.5 < \$5.0	5,718	14,687	4,084	9,993	3,982	9,077
\$5.0 < \$10.0	5,265	19,832	3,836	14,098	3,591	12,796
\$10.0 < \$20.0	1,844	12,455	1,264	8,434	1,247	7,966
> \$20.0 million	997	18,817	719	18,223	695	13,606
Total	36,458	106,701	41,158	96,209	69,576	109,091

Source: IRS