

# Issues Surrounding the Federal Estate Tax: Impact of Repeal vs. Reform

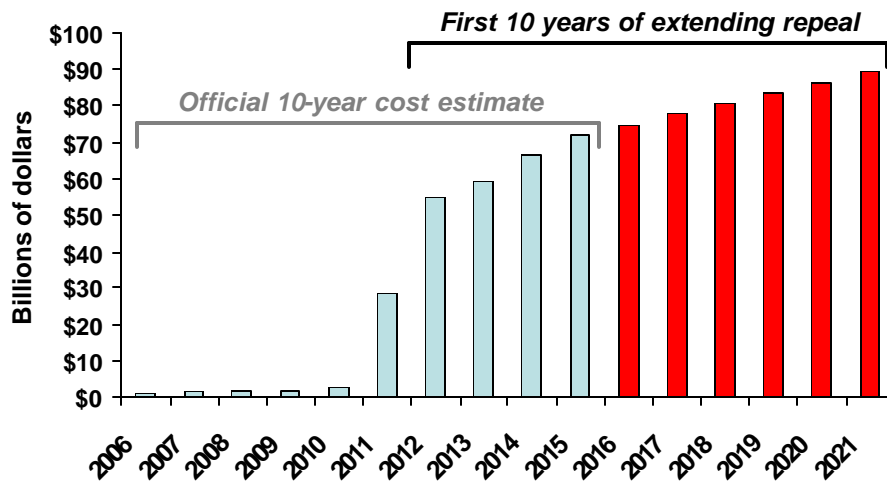
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## Background on Estate Tax Issue

- Under the tax-cut law enacted in 2001, the estate tax will be reduced in coming years, repealed in 2010, and then reinstated in 2011 at pre-2001 law levels. The Administration has called for making repeal permanent after 2010.
- Permanent repeal of the estate tax would be extremely costly. Yet few support returning to pre-2001 law (which would set the estate tax exemption at \$1 million and the top tax rate at 55 percent). So there is a push to find an appropriate reform.
- The goals of reform should be to preserve a significant amount of revenue, given the nation's serious fiscal problems, and reduce the number of estates facing the tax.
- The following slides examine the impact of estate tax repeal and different reform options.

## Official 10-year Cost Estimate Masks True Cost of Extending Estate Tax Repeal

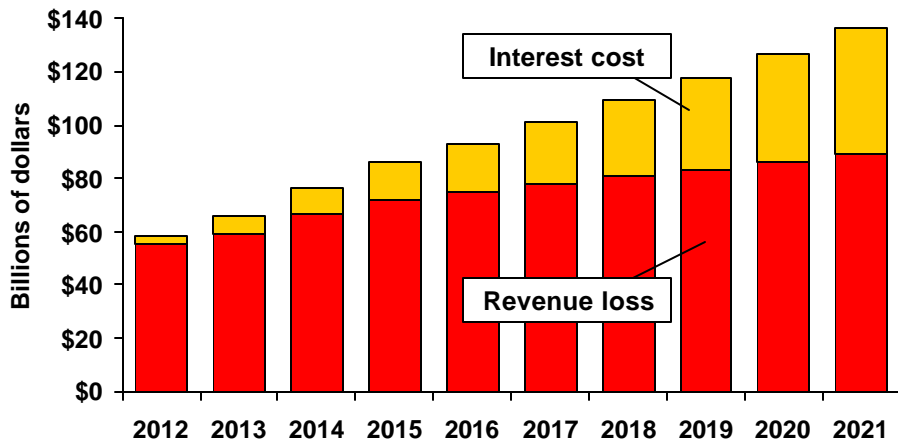


Note: Joint Committee on Taxation estimates through 2015; CBPP projections through 2021

The full cost of extending estate tax repeal only shows up in fiscal year 2012. Because the official 10-year cost estimate of extending repeal covers fiscal years 2006-2015, it captures only the first few years of the cost of repeal. Examining the first 10 years of extending repeal (fiscal years 2012-2021) yields a more accurate picture of the sizeable long-term cost associated with repealing the estate tax. See <http://www.cbpp.org/3-16-05tax.htm>.

## Estate Tax Repeal Costs Nearly \$1 Trillion Over 10 Years

*Cost, with interest, fiscal years 2012-2021*

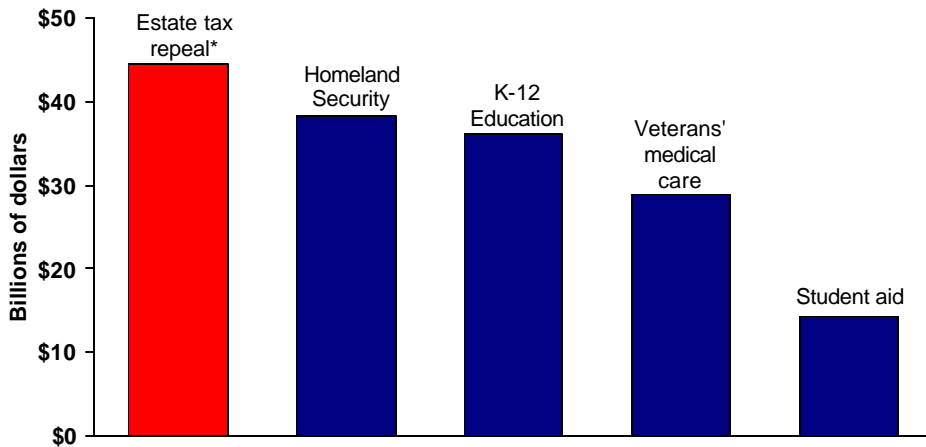


*Source: Joint Committee on Taxation and CBPP*

Extending estate tax repeal will add nearly \$1 trillion to the debt over the first 10 years (fiscal years 2012 to 2021) — \$745 billion in lost revenues and \$225 billion in higher interest payments on the debt. See <http://www.cbpp.org/3-16-05tax.htm>.

## Estate Tax Repeal Costs More Than Funding for Key Policy Priorities

*One-year cost of estate tax repeal vs. 2005 program funding levels*



\*Reflects annual revenue loss when estate tax is repealed, in billions of 2005 dollars.

Source: CBPP calculations of CBO data

The revenues that would be lost as a result of estate tax repeal would exceed what the federal government currently spends on many popular programs. Further, those programs serve millions of Americans, while the benefits of repealing the estate tax would flow exclusively to the wealthy heirs of a few thousand estates.

## How Much Revenue Would A Reformed Estate Tax Preserve?

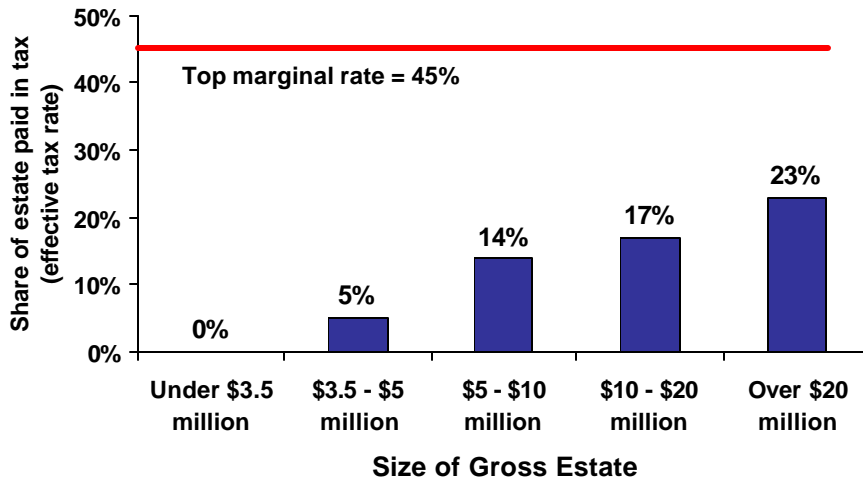
<i><b>If the top tax rate were:</b></i>	<i><b>... and the exemption level were:</b></i>	<i><b>... the share of estate tax revenue that would be preserved is:</b></i>
<b>45%</b>	<b>\$2.0 million</b>	<b>68%</b>
	<b>\$3.5 million</b>	<b>44%</b>
<b>15%</b>	<b>\$2.0 million</b>	<b>21%</b>
	<b>\$3.5 million</b>	<b>13%</b>
	<b>\$5.0 million</b>	<b>10%</b>

*Source: Urban-Brookings Tax Policy Center*

Cutting the top estate tax rate from 45 percent to 15 percent — the rate currently levied on capital gains income — would sharply reduce revenues. As a result, a redesign of the estate tax that relies on a 15 percent rate would lose nearly as much revenue as permanent repeal of the tax. See <http://www.cbpp.org/4-20-05tax.htm>.

## Estate Tax Burden Much Lower Than Typically Portrayed

(assumes \$3.5 million exemption, 45% top rate in 2011)

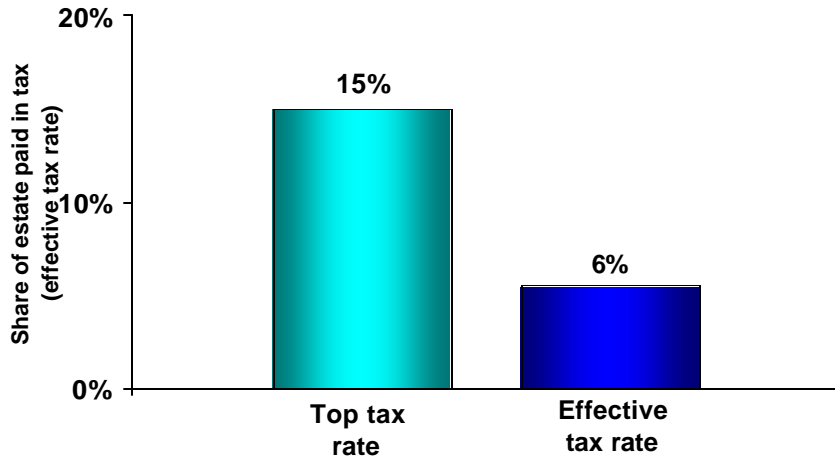


Source: Urban-Brookings Tax Policy Center

Some argue that the estate tax forces families to pay half of the value of an estate in tax. But given the up-front exemption and available deductions, the “effective” estate tax rate — the percentage of an estate paid in taxes — is much lower. This graph shows that if the estate tax were retained in its 2009 form, even the largest estates would on average pay less than one-quarter of their value in estate taxes, and estates worth less than \$10 million (which make up nearly three-quarters of all taxable estates) would on average pay only 12 percent. See <http://www.cbpp.org/4-20-05tax.htm>

## With a 15% Top Rate, Taxable Estates Would Face an Effective Rate of Only 6%

*(assumes \$3.5 million exemption, 15% top rate in 2011)*

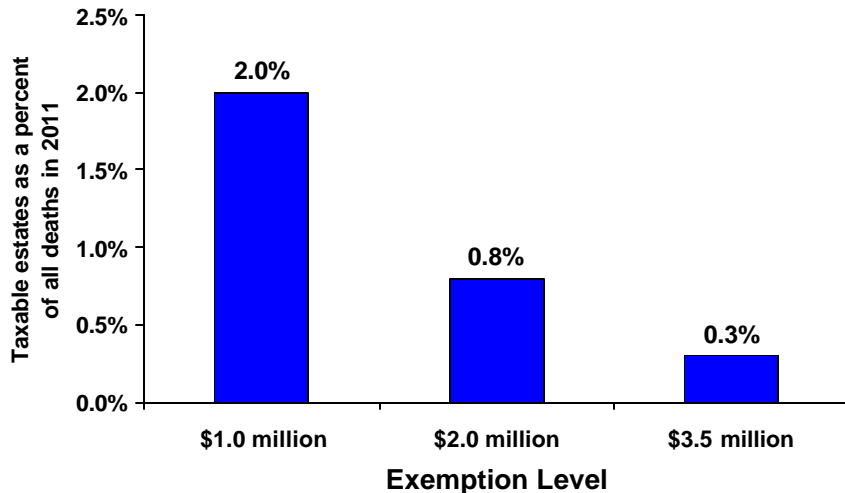


*Source: Urban-Brookings Tax Policy Center*

If the top rate were 15 percent, taxable estates would, on average, pay only 6 percent of their value in tax because of the availability of the up-front exemption and other deductions. With an “effective rate” of only 6 percent, it is not surprising that so little revenue would be collected if the top rate were 15 percent. See <http://www.cbpp.org/4-20-05tax.htm>

## Raising Exemption Can Further Reduce Already Small Number of Taxable Estates

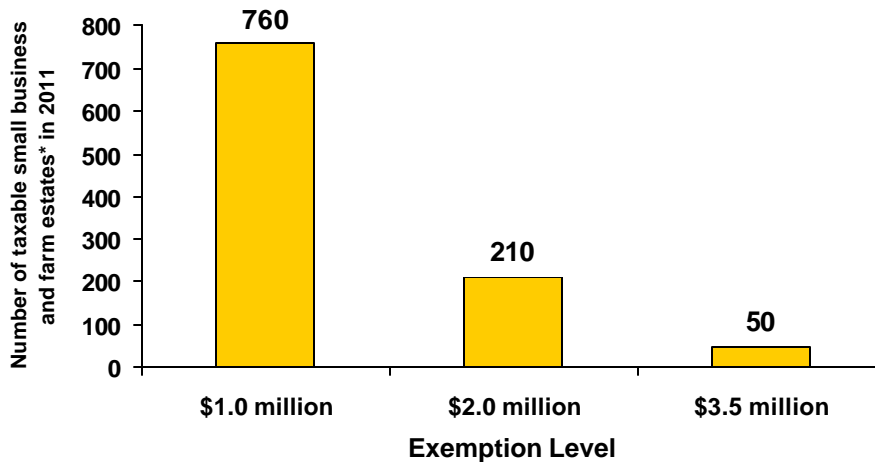
(taxable estates as a percent of all deaths, 2011)



Source: Urban-Brookings Tax Policy Center

Raising the exemption level can reduce further the already small number of estates subject to the estate tax. For instance, raising the exemption from \$1 million to \$2 million would reduce the number of taxable estates by 61 percent, from about 54,000 estates (or 2 percent of all deaths in 2011) to 21,000 (or 0.8 percent of all deaths that year). Yet an estate tax with a \$2 million exemption level would still retain a substantial amount of revenue if the rate were maintained at 45 percent. See <http://www.cbpp.org/3-16-05tax.htm>

## Tiny Number of Small Farms and Businesses Owe Any Estate Tax

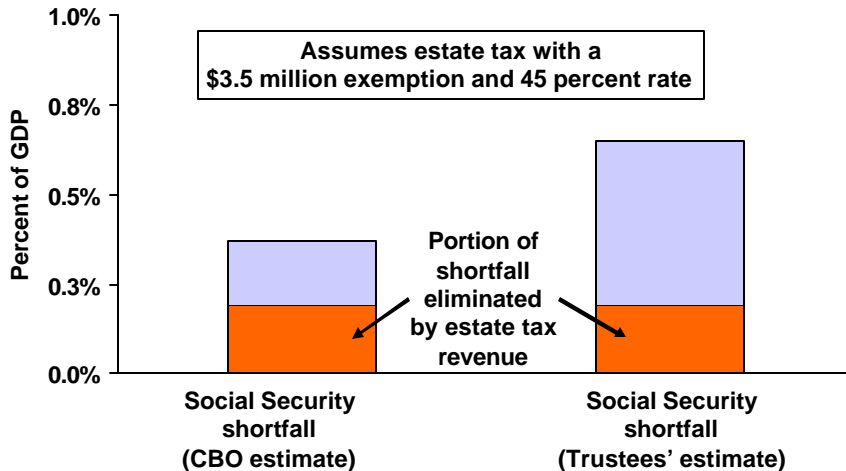


\*Estates comprised primarily of farm or business assets worth less than \$5 million.

Source: Urban-Brookings Tax Policy Center

Some argue that the estate tax poses particular problems for farmers and business owners. In reality, very few estates subject to the estate tax are comprised *primarily* of small businesses or small farms (that is, farms and businesses worth less than \$5 million). Yet it is only in those situations where the farm or business represents a majority of the estate that some part of the farm or business might potentially need to be sold because the estate lacks other assets that can be used to pay the tax. With a \$2 million exemption, there would be only 210 taxable estates nationwide in 2011 in which a small farm or small business comprises a majority of the estate; with a \$3.5 million exemption, there would be only 50 such taxable estates. See <http://www.cbpp.org/3-16-05tax.htm>

## Revenues from a Reformed Estate Tax Could Cover One-Quarter to One-Half of the 75-year Shortfall in Social Security



Maintaining the estate tax at its 2009 level (with a \$3.5 million exemption and a 45 percent rate) rather than repealing it would preserve an amount of estate tax revenue that is equivalent to *more than one-quarter of the Social Security shortfall* over the next 75 years, as measured by the Social Security Trustees, and about half of the Social Security shortfall as measured by the Congressional Budget Office. See <http://www.cbpp.org/4-20-05tax.htm>