Joint Economic Committee Democrats

Representative Pete Stark (D-CA) – Ranking Member

Economic Policy Brief

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Revisiting Myths About the Estate Tax: Rhetoric versus Reality

Fact Sheet

Repeal of the estate tax has been an essential element of the Republican tax-cutting agenda. When repeal of the estate tax was first proposed by the Bush Administration in early 2001, the Democratic staff of the Joint Economic Committee analyzed the arguments used by advocates of repeal and pointed out that these arguments were based much more on myth than on reality ("Myths About the Estate Tax: Rhetoric versus Reality," May 2001). Now, as Republicans in the House have just voted to make permanent the repeal written into the 2001 tax act, we have revisited that analysis and found that the rhetoric remains unchanged. The economic evidence continues to point to the following sharp contrasts between Republican myths and the reality of the estate tax:

Myth: *The estate tax is a "death tax."*

Reality: The overwhelming majority of Americans are not subject to the federal estate tax when they die. In 2001, 98 percent of adult deaths involved no estate tax liability. With the increases in the estate tax exemption already scheduled to take effect, only about 10,000 estates (or less than one-half of one percent) will have estate tax liability in 2009. Only very large estates are taxed. Estates valued at $2.5 million or more paid nearly three-fourths of the total estate taxes in 2001.

Myth: *The estate tax is especially burdensome on family-owned businesses and farms.*

Reality: There are already special provisions to ease the burden of the estate tax on small businesses and farms, and only a small fraction of taxable estates consist primarily of small business or farm assets. Tax return data from 1998 indicate that only 642 or 1.4 percent of taxable estates had farm assets making up a half or more of their gross estate, and only 776 or 1.6 percent of taxable estates had business and partnership assets comprising half or more of their gross estate. A Congressional Research Service analysis concludes that less than one percent of small businesses and farms would be forced to liquidate assets to pay the (current level of) estate tax.

Myth: *The estate tax is a "double tax" that significantly reduces the size of the capital stock and hampers economic growth.*

Reality: Unrealized capital gains that have never been taxed are a significant amount of the wealth in estates. Estate taxes can result in either more or less saving and investment, depending upon the reasons for saving. Empirical evidence does not support the claim that estate taxes have an important impact on investment and growth.

Myth: *Evasion and avoidance of the estate tax greatly reduce the amount of revenue that is collected, rendering the tax both inefficient and regressive.*

Reality: The estate and gift tax raises significant revenue. Prior to the 2001 tax act, the Congressional Budget Office (CBO) projected that the federal tax alone would have raised $380 billion over ten years. CBO's latest baseline, incorporating the scheduled reductions in the estate tax, estimates the tax will still raise $258 billion over 2004-13. But the actual revenue cost of repealing the estate tax would be much greater than this baseline projection, because without an estate tax, taxpayers would increase tax avoidance strategies, reducing income tax collections. Analyses of the distribution of estate tax burdens consistently show the tax is highly progressive.

Myth: *Charitable giving would be unaffected by repeal of the estate tax.*

Reality: The most recent empirical evidence suggests that eliminating the estate tax would reduce both charitable bequests and charitable contributions by about $10 billion per year — an amount equivalent to the total grants currently made by the largest 110 foundations in the United States.

Myth: *The estate tax can be easily replaced by a change in capital gains taxation.*

Reality: Modifying capital gains rules to more fully tax gains at death would add its own complexities and induce new forms of tax shelters.

Myth: *Repeal of the estate tax is affordable and is necessary to grant significant tax relief.*

Reality: The true cost of permanent estate tax repeal was grossly underestimated by the official cost of the estate tax changes in the 2001 act, because the act contained only one year of full repeal. The Joint Committee on Taxation now estimates that the cost of permanent repeal would be $64 billion in 2013 alone. If the annual cost of permanent repeal were to grow only at the same rate as the economy, the revenue loss in the decade after repeal would be around three-quarters of a trillion dollars.

Because the estate tax is highly progressive, tax receipts are highly concentrated in the highest income categories. Therefore, repealing the estate tax would grant significant tax relief to only the wealthiest estates.

Policy Conclusion

Raising the exemption level of the estate tax would be a wise alternative to repealing the tax. A higher exemption level would cut the revenue loss substantially while still benefiting *all* current estate taxpayers, and for all but the very wealthiest of current estate taxpayers, it would have the same effect as outright repeal. For example, retaining the estate tax while allowing the exemption level to rise to $3 million starting in 2004 would cost less than a fifth as much as full repeal. The revenue saved is considerable—in present-value terms it is equivalent to about 30 percent of the long-term shortfall in Social Security.

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