TALKING POINTS MEMO
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FIXING & EXPANDING THE ESTATE TAX: Intervening to Reduce Wealth Inequality

The estate tax is America's only levy on substantial wealth. Sometimes called the "inheritance tax" or "death tax," the estate tax requires the wealthy to pay a levy on wealth they leave their heirs, after a substantial exemption.

The estate tax is paid only by multi-millionaires and billionaires. In 2014, the federal tax is levied on estates with assets (cash, real estate, stocks, or other assets) exceeding $5.34 million (or effectively $10.68 million per married couple).[1] Fewer than 2 out of every 1000 people who die will owe estate tax in 2014.[2]

Much of the tax is levied on appreciated assets, wealth that has grown over a lifetime and not subject to any prior taxation.

The Origins of the Estate Tax

Instituted in 1916, the federal estate tax has multiple purposes that remain relevant today: 1) raise revenue from those with the greatest capacity to pay; 2) encourage charitable giving and dispersal of wealth; and 3) put a brake on the concentration of wealth and power, with its threat to democracy and social

[1] Chye-Ching Huang and Nathaniel Frentz,"Myths and Realities About the Estate Tax," Center on Budget and Policy Priorities," (Revised, Aug 29. 2013) http://www.cbpp.org/cms/?fa=view&id=2655
[2] Tax Policy Center, Table T13-0019

stability. In the aftermath of the First World War, the estate tax was viewed as a means to pay down war debt and prevent wealthy dynasties.

Proponents of an estate tax, ranging from President Theodore Roosevelt to populist farm organizations, viewed the extreme concentrations of wealth during the first Gilded Age, 1890-1915, as a threat to our self-governing democracy.

States instituted estate and gift taxes prior to the federal estate tax. By the 1920s, rules and rates varied in different jurisdictions. Over time, this was fixed as state and federal estate taxes were synchronized to have uniform rates and allow states to "piggy-back" on the federal tax, simplifying the process for both tax filers and government.

Over the last century, the estate tax has served its stated purpose. When it was protected from loopholes, it raised substantial revenue from those with the greatest capacity to pay. It encouraged the dispersal of wealth, through incentives for charitable giving and widely gifting to heirs and others. Most important, it ensured that during the years 1930 to 1975, the intergenerational transfers of wealth discouraged wealthy dynasties, unlike the previous era and our present Second Gilded Age.[3]

The Movement to Eliminate the Estate Tax

In the 1990s, a right-wing movement organized to eliminate the "death tax." Funded by wealthy families and anti-tax groups, these organized efforts spent millions to enable the wealthy few to dodge billions in taxes.[4] They mounted phony PR campaigns to confuse the public about the tax and who paid it. In 2000, Congress outright repealed the tax, but President Clinton vetoed the bill urging Congress to "reform the estate tax, not repeal it."

In 2000, George W. Bush campaigned for the presidency on tax cuts, including a call to "eliminate the death tax." In 2001, a counter-movement was formed including pro-estate tax leaders such as Bill Gates Sr., Warren Buffett, and Paul Newman. This movement educated the wider public that the tax was only paid by 3 out of 200 households and did not put family farms and small enterprises

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[3] See Bill H. Gates, Sr., and Chuck Collins, *Wealth and Our Commonwealth: Why America Should Tax Accumulated Fortunes* (Boston: Beacon Press, 2003).

[4] Chuck Collins, Conor Kenny, Lee Farris and Lincoln Taylor, "Spending Millions to Save Billions: The Campaign of the Super Wealthy to Kills the Estate Tax," Public Citizen & United for a Fair Economy, April 2006, http://www.citizen.org/documents/EstateTaxFinal.pdf

out of business. In June 2001, the tax was modified but not eliminated. Certain provisions were added to weaken the tax — and to delink the federal estate tax from state estate taxes.[5]

The Estate Tax Today

The most recent rules governing the estate tax were passed in January 2013 as part of the American Taxpayer Relief Act (ATRA). Under ATRA the estate tax wealth exemption was set at $5.25 million and indexed to inflation. The rate was fixed at 40 percent, the lowest rate since the 1930s.

There were some technical fixes, such as allowing the "portability" of the estate tax exemption between married couples, so the full exemption passes to the surviving spouse. The gift tax and estate tax were also aligned with parallel rules.[6] But Congress failed to address the disconnection created in 2005 between state-level estate taxes and the federal tax. As a result, some states presently have no estate tax and others retained their tax, but with different rates and exemptions, adding unnecessary complexity.[7]

Many wealthy families deploy teams of tax planners to circumvent or reduce taxes, including the estate tax. The Tax Policy Center estimates that only 3,780 households (0.14 percent of all estates) will owe estate taxes from 2013. Their average payment will be $3.8 billion on estates worth $227 billion — an effective rate of 16.6 percent. The effective tax rate on estates over $20 million is 18.8 percent.[8] This is far below the 40 percent statutory rate.

Many estates are reduced through different valuation techniques.[9] Recent uses of the Granter Retained Annuity Trust (GRAT) enable aggressive avoidance of the estate and gift tax system. Richard Covey, the lawyer who pioneered the

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[5] This history is fully discussed in Gates & Collins, Ibid.

[6] Deborah L. Jacobs, "After the Fiscal Cliff Deal: Estate and Gift Tax Explained," *Forbes*, February 1, 2013. http://www.forbes.com/sites/deborahljacobs/2013/01/02/after-the-fiscal-cliff-deal-estate-and-gift-tax-explained/

[7] Elizabeth McNichol, "State Taxes on Inherited Wealth Remain Common: 21 States Levy an Estate or Inheritance Tax," Center on Budget and Policy Priorities, Updated March 12, 2013. http://www.cbpp.org/cms/index.cfm?fa=view&id=337

[8] Tax Policy Center, Chart T13-0020. http://taxpolicycenter.org/numbers/displayatab.cfm?DocID=3776

[9] Tax attorney Bob Lord cites a classic example of our porous estate tax code. In this lawsuit with the IRS, an estate is able to reduce the value of publicly traded securities in the estate by close to 40 percent. The effect was to reduce the maximum estate tax rate from 40 percent to 25 percent. This is before using trust loopholes. https://www.courtlistener.com/tax/eACE/estate-of-helen-p-richmond-amanda-zerbey-v-commiss/

loophole, believes these tax shelters have resulted in $100 billion in lost federal revenue since 2001. *Bloomberg News* recently documented how billionaire casino mogul Sheldon Adelson exploited the GRAT provision to pass nearly $8 billion to family members and avoid $2.8 billion in estate taxes.[10]

The Present Case for An Estate Tax

We are now living in a period of extreme wealth inequality. The concentration of wealth is at its greatest point since the first Gilded Age before 1929. These wealth disparities undermine our democracy, health, social mobility, and economic stability.[11] A robust federal estate tax is needed now more than ever for the same reasons behind its original passage in 1916.

1. Break up Wealth Dynasties. The estate tax is possibly the single most important intervention the U.S. could use to break up concentrated wealth and discourage wealth dynasties. Between the 1930s and 1970s, the estate tax was more effectively designed to discourage loopholes and disperse wealth. By eliminating loopholes and instituting a graduated rate structure, the estate tax could be a more powerful brake on wealth concentration.

2. Federal Revenue. The estate tax has the potential to raise substantial revenue from multi-millionaires and billionaires. Even in its present weakened state, the estate tax is expected to generate $200 billion over 2013-2022.[12] This is equivalent to what our nation will spend over the same decade on the Centers for Disease Control, the Environmental Protection Agency and the Food and Drug Administration combined.

3. State Revenue. States have been big losers in the various reforms of the state tax. 29 states failed to preserve their estate taxes after the 2001 estate tax cut, losing billions in revenue. The 21 states that have retained an estate tax collect roughly $4.5 billion per year.[13]

4. **Encourage Charitable Giving.** The estate tax encourages donations and bequests to charity.

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[10] Zach Mider, "Accidental tax break saves wealthiest Americans $100 billion," Bloomberg, December 17, 2013. http://www.bloomberg.com/news/2013-12-17/accidental-tax-break-saves-wealthiest-americans-100-billion.html

[11] See www.inequality.org and Chuck Collins, *99 to 1: How Wealth Inequality is Wrecking the World and What We Can Do About It* (Berrett Koehler, 2012).

[12] Tax Policy Center Table, T13-0019

[13] op cit. McNichols.

Bill Gates Sr. argued that the estate tax is a fair and fundamentally "all-American tax." We should tax millionaires and billionaires who have disproportionately benefited from our nation's public investments, laws, infrastructure, and property rights protections. These funds should be invested in ways that ensure equal opportunity for all. Bill Gates Sr. called the estate tax an "economic opportunity recycling program."

Progressive Reforms to the Estate Tax

There are a number of estate tax reforms that would make the tax more effective as a tool to reduce wealth inequality and strengthen the economy.[14] Here are several progressive reforms to the estate tax.

Eliminate the "Billionaire Loophole" such as GRAT. Congress should act immediately to eliminate the GRAT as a mechanism for estate and gift tax avoidance. President Obama has included a proposal to reform the GRAT in each of his annual budgets, but he has not used any political capital to press it.

Institute a Graduated Rate Structure. The estate tax presently has one rate — 40 percent — whether a total estate wealth is $12 million or $12 billion. Congress should institute a graduated rate structure, with rates starting at 40 percent and rising incrementally as estate size increases. For example, estates over $20 million should pay a 45 percent rate. Estates over $50 million should pay a 50 percent rate on wealth over that threshold. Estates over $1 billion should have a steeply progressive rate. Billionaire Warren Buffett suggested that the estate tax should be 100 percent on such estates.

Re-link State to Federal Estate Taxes. Allow states to piggy-back on the federal estate tax, with a portion of revenue (say 16 percent, which was the rate prior to 2001 estate tax cuts) flowing to state treasuries. 21 states presently have estate taxes, but their rules are all different, and this makes them vulnerable to state repeal efforts.[15] States without estate taxes could pickup additional revenue — without increasing taxation — because estates would receive a dollar-for-dollar credit to reduce federal taxes owed by the amount paid to states. States could "opt out" of the estate tax, in which case 100 percent of estate taxes from their state residents would go to the federal government.

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[14] Paul L. Caron & James R. Repetti, "Occupy the Tax Code: Using the Estate Tax to Reduce Inequality and Spur Economic Growth," Tax Notes, Volume 142, March 18, 2014 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2410985

[15] op cit. McNichols.

Conclusion

The national conversation about the estate tax has gone back underground. Fixing the estate tax –and expanding its scope –could be the single most important intervention in reducing wealth dynasties in the U.S.

RESOURCES

"Myths and Realities About the Estate Tax"
Chye-Ching Huang and Nathaniel Frentz, "Center on Budget and Policy Priorities," (Revised, Aug 29. 2013).
http://www.cbpp.org/cms/?fa=view&id=2655

State Estate Taxes: See:
"State Taxes on Inherited Wealth Remain Common: 21 States Levy an Estate or Inheritance Tax"
Elizabeth McNichol, Center on Budget and Policy Priorities, Updated March 12, 2013. http://www.cbpp.org/cms/index.cfm?fa=view&id=337

Tax Policy Center –Estate and Gift Tax Research
http://taxpolicycenter.org/taxtopics/estatetax.cfm

Tedx Talk: "**The Case for Taxing the Wealthy,"** Chuck Collins, October 15, 2011. https://www.youtube.com/watch?v=1sgaDbg2RLE

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