



It's Not About Economic Equality

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Response to New York Times Debate:

Do Estate Taxes Matter?

Estate taxes have long generated political heat. Would other kinds of taxes work just as well?

Congress created the estate tax nearly 100 years ago in an effort to increase economic equality by preventing the rich from passing all of their wealth to subsequent generations. But the tax never achieved that goal.

One reason we need the estate tax is to encourage charitable giving.

Few estates pay any tax: Just under 8 percent paid in 1976 and that percentage has fallen steadily. In recent years, it has dropped from 2.3 percent in 2001 to zero this year as the levy's exemption rose from \$675,000 to \$3.5 million. And in spite of being the most progressive federal tax with rates ranging as high as 55 percent, the levy has [never claimed even a quarter of decedents' wealth](#) in a given year because of the exemption as well as smart estate planning.

Given the estate tax's failure to meet its original goals, why not let it rest in peace?

Three reasons: First, it taxes income that has escaped tax over a wealthy person's lifetime. Investors pay no tax on capital gains until they sell their appreciated assets. For example, the owner of a small businesses or a long-held stock portfolio never pays tax on their growing value unless he sells these assets. Those substantial unrealized gains are taxed only through the estate levy. Get rid of the estate tax and people will find even more ways to avoid income taxes.

Second, the estate tax has raised more than \$20 billion annually in recent years. That's a small fraction of federal revenue — less than 1 percent — but every little bit helps if we want to shrink our huge deficit.

Third, the tax encourages charitable bequests because giving away assets cuts what estates owe. One study concluded that ending the tax would reduce charitable giving by 12 percent.

But the estate tax has its downsides. People spend substantial time and money organizing their financial affairs, buying insurance policies, and constructing wills and trusts to minimize taxes on their estates, all an unproductive waste of resources.

Other objections are less convincing. Some very wealthy people may work and invest less because the tax will claim some of the return to those activities. On the other hand, some may work harder to increase their after-tax bequests. And their heirs may loaf if they anticipate substantial inheritances.

While some estates may have to sell assets to pay the tax, this happens very rarely. Family farms and businesses are the political poster children for this claim, but it is hard to find a real example. Still, these risks may matter a lot to a few of the very wealthy.

No one likes paying taxes. But our fiscal needs demand both spending cuts and increased revenue. Estate taxes fall only on the wealthiest, who have benefited most from our economy and have the greatest ability to pay. As such, it still has an important role to play in federal tax policy.