

Where, Oh Where, Has the Estate Tax Gone?

By Roberton Williams

Unless Congress changes the law, the federal estate tax will disappear on January 1, 2010. For the first time since the 1916 inception of the tax, the estate of anyone dying in 2010 will go to heirs tax free, a result of the 2001 tax law that phased out the estate tax over 10 years. But that law itself expires in 2011 and the estate tax will revert to pre-2001 law.

The Economic Growth and Tax Relief Reconciliation Act of 2001 increased the effective estate tax exemption in steps from \$675,000 in 2001 to \$3.5 million in 2009 and reduced the top tax rate from 55 percent to 45 percent. Raising the exemption cut the share of estates subject to tax by nearly 90 percent — from 2.14 percent in 2001 to a projected 0.23 percent in 2009. That percentage is the lowest since at least 1934 (see figure).

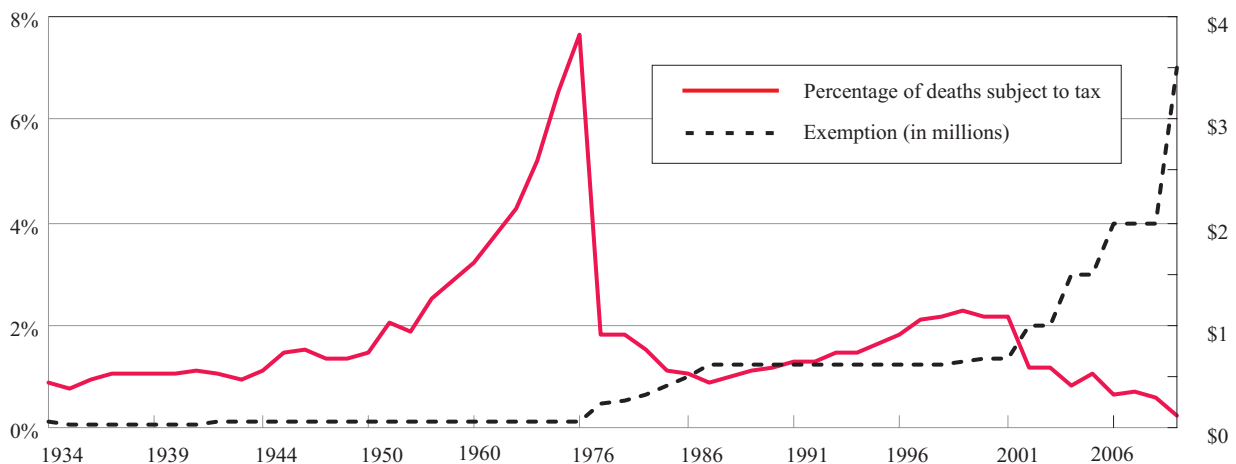
With the 2009 exemption of \$3.5 million, an estimated 5,500 estates will pay the estate tax, yielding revenue totaling nearly \$14 billion. Revenues will drop to zero in 2010 (but a sharp increase in gift tax collections will make up some of the loss, albeit at the cost of lower estate taxes

in future years). If the estate tax reverts to pre-2001 law and its \$1 million exemption, an estimated 44,000 estates — representing just under 2 percent of all deaths — will owe tax totaling more than \$34 billion.

Congress is currently debating various options to change the estate tax in 2010 and subsequent years. One approach would make the 2009 parameters permanent, thus imposing the tax on about one-quarter of 1 percent of estates in 2010. That share would grow slowly over time if the \$3.5 million exemption were not indexed for inflation, rising to about 0.4 percent by 2019. Revenues would roughly double over the decade from \$14.8 billion in 2010 to \$28.9 billion in 2019. Indexing the exemption would slow but not halt that growth as wealth will likely increase faster than prices.

Other proposals in Congress would increase the exemption to \$5 million and reduce the tax rate to 35 percent, either immediately or by 2019. The higher exemption would cut the number of estates subject to tax and, in combination with the lower tax rate, would slash revenues by nearly half. The Tax Policy Center has projected the effects of those and other proposals at <http://www.taxpolicycenter.org/numbers/displayatab.cfm?Docid=2506>.

Estate Taxes: Deaths Subject to Tax and Exemption Level, Selected Years, 1934-2009



Source: IRS, *Statistics of Income* Historical Table 17 and Tax Policy Center simulation, available at <http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=52>.