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STATE-LEVEL ESTIMATES SHOW STARK CONTRASTS UNDER PROPOSALS TO EXTEND CUT IN ESTATE TAX WHILE FAILING TO EXTEND IMPROVEMENTS IN TAX CREDITS FOR WORKING FAMILIES

By Chye-Ching Huang and Nathaniel Frentz

In recent proposals to extend expiring tax cuts beyond the end of the year, Republican leaders in the House and Senate have called for extending an estate-tax cut enacted in 2010 that provides a large tax break to the estates of the wealthiest 0.3 percent of Americans who die each year — about 7,000 people — while *ending* a provision of the same 2010 tax legislation that makes improvements in the Earned Income Tax Credit (EITC) and Child Tax Credit (CTC) that benefit 13 million moderate-income working families.[1]

Legislation that the House passed on August 1, and similar legislation that Senators Hatch and McConnell have introduced in the Senate, would undo a compromise enacted in late 2010. At that time, the Obama Administration had acceded to Republican demands to extend *all* of the expiring Bush tax cuts, including those for people making over $250,000 a year. The White House sought also to extend several improvements in tax credits for low- and moderate-income working families with children that had been enacted as part of the Recovery Act and were similarly slated to expire at the end of 2010. Independent analysts such as the Congressional Budget Office and Moody's Analytics rated the improvements in these tax credits as having much more "bang for the buck" in boosting the weak economy than the high-end Bush tax cuts.[2] However, in the negotiations in December 2010, Republican Congressional leaders refused to accept the extension of these tax-credit improvements — unless that extension was accompanied by a costly new reduction in the estate tax. That is how the estate-tax break came to be enacted.

Analysis by the Urban Institute-Brookings Tax Policy Center shows that only the top 0.3 percent of estates receive the estate-tax cut enacted in 2010; the estates of the other 99.7 percent of people who die already will be exempt from the tax if the 2009 parameters for the estate tax are reinstated as the Obama Administration has called for, and as the Bowles-Simpson plan issued in late 2010 assumed would be done. Relative to the 2009 estate-tax parameters, the estate-tax break enacted at

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[1] For more on the proposals see Chye-Ching Huang, "Senate and House GOP Leaders' Tax Proposals Would Provide Windfall for Heirs of Largest Estates," Center on Budget and Policy Priorities, revised July 24, 2012, http://www.cbpp.org/cms/index.cfm?fa=view&id=3810.

[2] See Mark Zandi, "U.S. Macro Outlook: Compromise Boosts Stimulus," Moody's Analytics, December 8, 2010 and Statement of Douglas W. Elmendorf, Director, Congressional Budget Office, prepared for the Joint Economic Committee, U.S. Congress, February 23, 2010.

the end of 2010 benefits only the heirs of estates that have assets in excess of $3.5 million for an individual and $7 million for a couple.

For the estates that receive it, the estate-tax break enacted in 2010 is worth an average of $1.1 million per estate, relative to the 2009 parameters, according to the Tax Policy Center. If made permanent, the estate-tax break would cost $119 billion over ten years in lost revenue, and would increase the deficit by $141 billion over the same period when the interest costs are included, according to estimates from the Treasury Department and the Office of Management and Budget.[3]

The current GOP proposals would extend the estate-tax cut, along with all of the Bush tax cuts, through 2013. But these proposals would let the refundable tax-credit improvements for low- and moderate-income working families lapse on December 31, even though their impact in boosting a weak economy would be far greater than that of the 2010 estate-tax cut (which would have virtually no impact on the slow economy because it would do little or nothing to increase consumer or business purchases in the year ahead).

The contrast in priorities in the GOP proposal is stark. Examined on a state-by-state basis, the proposal to extend the estate-tax break while letting the tax-credit improvements for working families lapse would, for example:

- Extend the estate-tax cut for roughly the largest 150 estates in Colorado in 2013, while ending EITC and CTC improvements for 190,000 modest-income Colorado working families.

- Provide the estate-tax cut to about the wealthiest 100 estates in Washington State while ending the EITC and CTC improvements for nearly a quarter-million working families in that state, which contain nearly 500,000 children.

- Provide the estate-tax cut to roughly the wealthiest one-tenth of 1 percent (0.1 percent) of estates in Alabama, Alaska, Arkansas, Idaho, Indiana, Iowa, Kentucky, Maine, Mississippi, New Mexico, North Dakota, Ohio, Pennsylvania, Tennessee, Utah, West Virginia, and Wisconsin, while ending EITC and CTC improvements for over 5 million working families in these states.

In states such as Idaho, Tennessee, and West Virginia, roughly 7,000 times as many families would lose from the failure to extend the Child Tax Credit and Earned Income Tax Credit improvements as would benefit from extension of the 2010 cut in the estate tax.

Table 1 provides estimates of the numbers of families affected in each state. The state-by-state estimates of the number of families who would be adversely affected by letting the tax-credit improvements expire are from Citizens for Tax Justice. The estimates of the number of estates in each state receiving the estate-tax cut enacted in 2010 are based on the Tax Policy Center's estimate of the total number of such estates nationwide. We allocated that estimate across the states based on data from the Internal Revenue Service's Statistics of Income database and data from the Centers for Disease Control and Prevention. (See Appendix.)

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[3] *Budget of the United States Government, Fiscal Year 2013*, Office of Management and Budget, Table S–9: Mandatory and Receipt Proposals, page 220. If policymakers do not act, the estate tax will revert in 2013 to the rules in place before the 2001 tax cut, with an exemption of $1 million per estate (effectively $2 million for couples) and a top estate-tax rate of 55 percent.

For many lower-income working families, the impact of losing the tax-credit improvements would be substantial. For instance, a married couple with three children that has earnings at the estimated poverty line for 2013 ($27,713 for a family of that size) will receive $1,934 less in combined CTC and EITC benefits next year if policymakers let the improvements expire. Similarly, a single mother with two children working full time at the minimum wage — and earning about $14,000 — will receive a CTC of just $173 in 2013 instead of $1,725.

Table 1				
	Estates receiving 2010 estate-tax cut, relative to 2009 law, in 2013		Families adversely affected by not extending EITC and CTC improvements in 2013	
	Number of estates	Percentage of all estates in the state	Number of families	Number of children in these families
Total	**7,450**	**0.3%**	**13,115,145**	**25,715,649**
Alabama	50	0.1%	287,044	512,996
Alaska	*fewer than 10	*fewer than 0.1%	20,710	42,274
Arizona	110	0.2%	305,417	709,091
Arkansas	30	0.1%	156,164	297,695
California	1480	0.6%	1,524,618	3,165,250
Colorado	150	0.5%	190,845	344,865
Connecticut	140	0.5%	75,033	147,285
Delaware	*30	0.4%	31,954	52,384
District of Columbia	20	0.4%	17,035	37,907
Florida	900	0.5%	977,480	1,718,069
Georgia	180	0.3%	587,100	1,139,543
Hawaii	40	0.4%	52,371	102,592
Idaho	*10	0.1%	73,774	150,347
Illinois	240	0.2%	467,109	992,167
Indiana	50	0.1%	268,296	525,069
Iowa	40	0.1%	86,321	190,553
Kansas	60	0.3%	98,227	201,089
Kentucky	50	0.1%	183,209	332,944
Louisiana	80	0.2%	231,482	405,915
Maine	*10	0.1%	35,042	64,730
Maryland	140	0.3%	154,285	306,142
Massachusetts	140	0.3%	165,143	299,374
Michigan	170	0.2%	428,298	770,922
Minnesota	90	0.2%	115,656	271,368
Mississippi	40	0.1%	233,824	399,191
Missouri	120	0.2%	256,829	480,545
Montana	*30	0.4%	39,239	68,801
Nebraska	80	0.6%	62,532	119,840
Nevada	80	0.4%	113,535	246,673
New Hampshire	30	0.3%	22,301	36,092
New Jersey	220	0.3%	218,863	442,175
New Mexico	20	0.1%	115,222	214,788
New York	700	0.5%	724,949	1,414,333
North Carolina	140	0.2%	522,645	1,114,261
North Dakota	*fewer than 10	*fewer than 0.1%	19,809	35,579
Ohio	140	0.1%	498,603	997,137
Oklahoma	110	0.3%	207,145	383,857
Oregon	90	0.3%	133,792	258,389
Pennsylvania	170	0.1%	387,740	773,274
Rhode Island	*40	0.4%	30,284	58,252
South Carolina	100	0.3%	262,996	501,775
South Dakota	*60	0.9%	29,034	60,425
Tennessee	40	0.1%	330,797	594,954
Texas	540	0.3%	1,463,192	2,952,035
Utah	20	0.1%	120,838	288,122
Vermont	*10	0.2%	16,682	29,348
Virginia	220	0.4%	275,089	493,667
Washington	110	0.2%	246,432	492,169
West Virginia	*fewer than 10	*fewer than 0.1%	77,050	128,835
Wisconsin	40	0.1%	155,112	319,798
Wyoming	10	0.2%	17,998	30,763

Sources: Citizens for Tax Justice for families and children affected by EITC and CTC improvements.
CBPP calculation of estate numbers from Tax Policy Center, IRS, and CDC data (see Appendix).

NOTE: Estate estimates are approximate and include significant margins of error. Entries with an asterisk should be used with particular caution because of the small number of sample returns on which they were based.

Only Wealthiest Three in 1,000 Estates Would Receive Estate-Tax Cut

The legislation that the House passed in August 2012, and the similar proposal from Senators Hatch and McConnell, would continue an estate-tax cut enacted at the end of 2010 that is due to expire at the end of 2012. The Obama Administration has proposed that, at the end of this year, the generous estate-tax rules that were in effect in 2009 go back into effect. The deficit reduction plan that Erskine Bowles and Alan Simpson, co-chairs of a bipartisan deficit-reduction commission, issued in late 2010 also assumed reinstatement of the 2009 estate-tax rules.

Tax Policy Center analysis shows that only the wealthiest 0.3 percent[4] of estates nationwide would face any tax in 2013 under the 2009 rules, which exempt estates worth up to $3.5 million for an individual — effectively $7 million for a couple — from the tax. Because the top 0.3 percent of estates are the only ones that would owe any tax under the 2009 rules, going *beyond* the 2009 rules and shrinking the estate tax further benefits only those estates.

For example, in Colorado, only about the wealthiest 150 estates of people who die in 2013 would have any estate-tax liability under the 2009 rules. Hence, only these estates would receive further cuts in the tax.[5]

The 2009 rules already are very generous, reflecting eight years of reductions in the estate tax between 2001 and 2009, as required under the Bush tax cuts enacted in 2001. By 2009, the amount of an estate exempt from the tax had more than quadrupled; a wealthy couple with two grown children could pass on $3.5 million to each child tax-free. This tax-free exemption amount of $7 million is more than a middle-class family making $70,000 a year earns in a lifetime. Moreover, because the estate tax applies only to the value of the estate that exceeds the exemption level — and because of other tax breaks built into estate-tax law — the effective tax rates faced by those estates that are taxable are generally much lower than the statutory estate-tax rate. The Tax Policy Center estimates that under the 2009 rules, estates that would owe any tax at all would face an average effective tax rate of 19.1 percent in 2013 (in other words, the tax would, on average, equal 19.1 percent of the value of the assets in the estate), far below the official statutory rate of 45 percent.[6]

As noted, the 2010 legislation shrunk the estate tax beyond its 2009 parameters, raising the amount of an estate that is entirely exempt from the tax from $3.5 million to $5 million (effectively, from $7 million to $10 million for a couple) and reducing the tax rate on the value of an estate above that threshold from 45 percent to 35 percent. Compared to the 2009 estate-tax parameters, these changes provide an additional tax cut averaging $1.1 million per estate to the affected estates.

Although the 2010 estate-tax cut has only a small number of beneficiaries, its cost is high. Continuing it rather than reverting to the 2009 rules would cost $119 billion over ten years in lost revenue and increase the deficit by $141 billion over the same period when the interest costs are included, according to estimates from the Treasury Department and the Office of Management and Budget.[7]

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[4] CBPP calculation using data from Tax Policy Center, IRS, and CDC. See Appendix.

[5] CBPP calculation using data from Tax Policy Center, IRS, and CDC. See Appendix.

[6] Tax Policy Center table T11-0161.

[7] *Budget of the United States Government, Fiscal Year 2013*, Office of Management and Budget, Table S–9: Mandatory and

Lack of Extension of Tax-Credit Improvements Would Affect 13 Million Working Families

Policymakers enacted several improvements in tax credits targeted primarily on lower-income working families with children in 2009 and extended them through 2012 in the tax-cut extension legislation enacted at the end of 2010. These measures:

- reduce the level of earnings a working family must have before it can qualify for any Child Tax credit;

- reduce the "marriage penalty" that some families face under the EITC by improving the credit for married families; and

- raise the maximum EITC by about $650 for families with three or more children to reflect their higher living costs.

The package of tax-credit improvements also includes a measure to make college more affordable by replacing the Hope Credit with the American Opportunity Tax Credit, which provides a larger maximum credit to help offset college costs (a maximum tax credit of $2,500 instead of $1,800), can be claimed for up to four years of qualifying postsecondary education instead of only two, and is partially refundable (up to $1,000) for families that don't earn enough to owe federal income tax.

If the improvements in the EITC and the Child Tax Credit expire, a single mother with two children working full time at the minimum wage and earning $14,500 will face a reduction of about $1,550 in her child tax credit. A married couple with three children with earnings equal to the estimated 2013 poverty line ($27,713 for a family of that size) will face a loss of $1,934 in combined EITC and CTC benefits as a result of the failure to extend the improvements in these credits.

Citizens for Tax Justice estimates, for example, that failure to extend the CTC and EITC improvements would affect 156,000 Arkansas working families with nearly 300,000 children. Of these,[8] 81,000 families would lose some or all of their EITC, and 96,000 families would lose some or all of their CTC. Some families would face reductions in both credits.

Nationally, failure to extend the improvements in the CTC and EITC would increase the number of people living below the poverty line by approximately 1.6 million and increase the number of children living in poverty by 900,000.[9] It would also end the work and marriage incentives these improvements provide.[10]

Receipt Proposals, page 220.

[8] Citizens for Tax Justice, "The Debate over Tax Cuts: It's Not Just About the Rich," July 19, 2012, http://ctj.org/pdf/refundablecredits2012.pdf.

[9] These figures are based on the effects of the EITC and CTC in 2010, calculated by CBPP using Current Population Survey data.

[10] Jimmy Charite, Indivar Dutta-Gupta, and Chuck Marr, "Studies Show Earned Income Tax Credit Encourages Work and Success in School and Reduces Poverty," Center on Budget and Policy Priorities, June 26, 2012, http://www.cbpp.org/cms/index.cfm?fa=view&id=3793.

As noted above, the Recovery Act and the 2010 legislation also established the American Opportunity Tax Credit to help students afford college. A state-by-state analysis of the effects of expiration of that credit is beyond the scope of this paper.[11]

Conclusion

Providing costly tax windfalls to the country's wealthiest estates is difficult to justify in the best of times. It is particularly questionable at a time when the nation faces serious fiscal problems, policymakers are starting to make substantial cuts in a number of government functions (particularly in discretionary programs), and policymakers are considering deeper cuts in areas ranging from education to infrastructure to Medicare to programs that help the poorest Americans meet basic necessities or have a better chance at lifting themselves out of poverty.

For some policymakers to propose extending an exceedingly generous estate-tax windfall for the wealthiest Americans while allowing tax-credit improvements for low- and moderate-income working families with children to expire is striking.

[11] The White House National Economic Council has estimated that expiration of this credit would affect 11 million families with incomes below $250,000. See National Economic Council, *The President's Proposal to Extend the Middle Class Tax Cuts*, July 2012.

Appendix

CBPP estimated the number and percentage of estates in each state that benefit from the 2010 estate-tax cut, relative to 2009 law, as follows:

IRS Statistics of Income data (http://www.irs.gov/pub/irs-soi/10es02st.xls) provide the number of taxable estates in 2010. These were estates filing in 2010 from deaths in 2009, so these estates faced the 2009 estate-tax parameters.

We assumed that if the 2009 parameters of the estate tax were made permanent, each state's share of the total taxable estates would be the same in 2013 as it was in 2009. This is a simplifying assumption (as the wealth of estates in each state, relative to all estates nationwide, may change between 2009 and 2013) and is one reason these estimates are approximate.

We applied the share of taxable estates in each state from the IRS data to the Tax Policy Center's estimate of the number of estates nationally — 7,450 — that would owe any estate tax in 2013 under the 2009 parameters (TPC Table T11-0161).

To calculate the *percentages* of estates in each state that would pay any estate tax at all in 2010, we used Centers for Disease Control and Prevention data on estimated deaths in 2009 of people aged 20 and above.