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CBPP STATEMENT

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STATEMENT OF CHUCK MARR, DIRECTOR OF FEDERAL TAX POLICY, ON HOUSE CONSIDERATION OF THE ESTATE TAX

In recent years Congress has greatly reduced the federal estate tax, which affects only the nation's very largest estates, and the House should reject any effort this week to reduce it beyond its current parameters.

The country is suffering from the worst economic crisis since the Great Depression, with more than one in ten Americans unemployed and many of them out of work for more than six months. About one in seven homeowners with a mortgage is either behind in payment or in the process of losing his or her home through foreclosure. Many people are worried they will lose their foothold in the broad middle class. Moreover, the income gap between top end and the middle of the income spectrum has widened dramatically in recent decades, a gap that will only grow if Congress reduces the estate tax burdens for those at the very top.

Meanwhile, the nation's budget is on an unsustainable path, with the deficit already at record levels and projected to rise to once-unimaginable levels in the coming decades. Those deficits would rise even further if Congress were to further weaken the estate tax.

In the aftermath of Hurricane Katrina in 2005, Iowa Senator Charles Grassley stated that "it's a little unseemly to be talking about doing away with or enhancing the estate tax at a time when people are suffering."[1] What the senator said remains true today: given the current economic crisis and the human anguish it has caused, it would be more than "a little unseemly" to shrink what remains of the estate tax.

Going Beyond 2009 Rules Would Be Unjustified, Inequitable, and Irresponsible

- **The tax already has shrunk significantly over the past decade.** Since 2001, when Congress enacted legislation phasing out the estate tax, the amount of an estate's value that is exempt from the tax has jumped from $675,000 to $3.5 million per person. As a result, the number of estates that pay any tax at all has shrunk from 1 in 50 to 1 in 500. For 99.8 percent of Americans who die, the assets they leave to their heirs are entirely exempt from the tax under current (2009) law.

"House, Senate Approve Tax Breaks to Help Katrina Victims," Gannett News Service, September

Consider a wealthy couple with two children. Each child could inherit a trust fund of $3.5 million tax free when the couple dies. This is more money than a middle-class family making $70,000 a year would make in a *lifetime*, and the middle-class family would pay taxes on that income every year. Furthermore, the wealthy couple can give additional sums to its children as tax-free gifts each year while the couple is still alive.

- **The few estates that pay any tax owe less than 20 cents on the dollar, on average.** This is because of the high exemption level and various estate tax breaks. Also, in the case of very large estates that pay the tax, a substantial share of the estate often is in the form of unrealized capital gains that have never been taxed.[2]

- **Shrinking the tax further would add billions to deficits.** The leading proposals to shrink the tax would raise the exemption to $5 million per person ($10 million per couple) and reduce the rate to 35 percent. Senators Lincoln (D-AR) and Kyl (R-AZ) propose to move to these levels next year, while Representative Berkley (D-NV) proposes to phase in these reductions over ten years.

  Over the 2012-2021 period, the Lincoln-Kyl proposal would add $153 billion more to the deficit than making the 2009 rules permanent; the Berkley proposal would add $82 billion more than continuing the 2009 rules.[3] (These figures include the added interest payments on the debt that the Treasury would have to pay.) Moreover, the latter estimate masks the true long-term cost of the Berkley proposal, which would not phase in fully until 2019; over the long term, it would lose almost as much revenue as the Lincoln-Kyl proposal.

- **Such proposals, hard to justify at any time, are particularly hard to justify now.** The nation's unemployment rate stands at 10.2 percent. Five and a half million Americans have been looking for a job for more than six months and cannot find work; another 8.5 million are working part time because they cannot find full-time work. The Mortgage Bankers Association recently reported that 14.4 percent of mortgages are either in foreclosure or delinquent.[4]

  In addition, the nation is on an unsustainable fiscal path. In the past decade, policymakers have enacted large tax cuts, a new Medicare prescription drug benefit, and increased military commitments — none of which they paid for. Health care costs are also continuing to rise, and the population is getting older. Based on Congressional Budget Office estimates, we project that interest on the federal debt will reach $900 billion, or 4.3 percent of the U.S. economy, by 2019.[5] This is more than the country is expected to spend on national defense in that year.

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[2] According to a 2000 study, unrealized capital gains comprise 56 percent of the value of estates worth more than $10 million. See James Poterba and Scott Weisbenner, "The Distributional Burden of Taxing Estates and Unrealized Capital Gains At the Time of Death," p. 19, NBER, July 2000.

[3] Based on estimates from the Joint Committee on Taxation. Relative to current law, which calls for the estate tax to return in 2011 to its levels under pre-2001 tax law, the Lincoln-Kyl proposal would cost $544 billion over the 2012-2021 period, while the Berkley proposal would cost $473 billion and continuing the 2009 rules would cost $391 billion.

[4] The MBA defines mortgages as delinquent if they are at least one payment past due.

[5] The most recent Congressional Budget Office forecast (in August 2009) projects that under current law, interest payments will reach $722 billion in 2019. This projection, however, assumes (among other things) that policymakers will allow all of the 2001 and 2003 tax cuts to expire. Using more realistic policy assumptions, CBPP estimates that interest payments will total $902 billion in 2019.

The tens of billions of dollars in new tax cuts under the Lincoln-Kyl and Berkley proposals would flow entirely to the wealthiest 0.2 percent of estates — and would come on top of the very large tax cuts these estates would receive if Congress extended the 2009 rules. It would be both inequitable and fiscally irresponsible to expand the tax cuts for the nation's wealthiest estates heading into a decade in which policymakers will face wrenching fiscal choices that will require millions of ordinary Americans to tighten their belts.

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