

WebMemo



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Now Is (Still) the Time to Permanently Repeal Federal Death Taxes

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Editor's Note: *In the movie "Groundhog Day," Bill Murray's character suffers a perpetual Groundhog Day—every morning he awakes, the same day, the same circumstances, the same pitfalls greet him almost anew. But only when he learns to measure up to the day is he redeemed.*

Wednesday, April 13, is Groundhog Day for the House of Representatives. On that day, the House will consider H.R. 8, a bill to permanently repeal the federal death taxes. The House considered this same bill, identically numbered, in 2003, and the same reasons that made repeal of the death taxes good policy then still apply today. The House passed H.R. 8, but the Senate balked. Heritage's William Beach wrote this piece in 2003, and we republish it today. Heritage will continue to circulate it each time that Congress considers correcting, as Beach put it, "the peculiar way it dealt with death tax repeal in 2001"—unless and until, that is, this Groundhog Day finally passes.

The House of Representatives will likely vote this week on legislation—H.R. 8—to permanently remove estate taxes from the tax code beginning in 2011.

By doing so, Congress will correct the peculiar way it dealt with death tax repeal in 2001, as well as fulfill its promise of ending this tax on economic virtue and productivity that has done considerable damage to the nation's economic and community life.

Towards Good Tax Policy

The Economic Growth and Tax Relief Reconciliation Act of 2001 increased the amount that taxpayers can exempt from estate and gift taxes and slowly reduced the rate over the period 2002 through 2009. Then, the Act repealed death taxes for one year, 2010, before restoring them at their 2003 levels in 2011.

Congress created this bizarre fiscal hiatus in order to enact all of the tax policy changes given the amount of money it had set aside through its budget resolution for tax relief. Compounding this difficult task was

a last-minute estimate by the staff of the Joint Committee on Taxation (JCT) of how much federal revenue would decrease if Congress permanently repealed all federal death taxes. By using static rather than dynamic scoring and by making assumptions about how federal income and gift tax payments would interact, the JCT significantly increased the "cost" of repeal, thus forcing congressional tax writers to create this on-again, off-again tax policy.

When President Bush signs legislation eliminating this peculiar hiatus and making death tax repeal permanent, taxpayers will likely do two things:

1. Cease economically wasteful federal estate tax planning,

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2. Focus more on running their businesses and personal affairs knowing for certain that they do not have to look over their shoulder for the death tax collector.

Good tax policy is known for its certainty, if for no other characteristic. Without predictability, tax policy can create confusion and have a lethal effect on economic activity.

Problems With the Death Tax

The number of threats posed to economic activity, by the death tax, will be eliminated with the passage of H.R. 8.

The death tax hinders economic activity in the following ways:

1. Discourages savings and investment;
2. Undermines job creation and wage growth;
3. Prevents economy from achieving investment potential;
4. Contradicts central promise of American life: wealth creation.

Discourages savings and investment. For those Americans who think that their estates may one day pay federal death taxes, the tax sends a signal that it's better to consume today than invest and make more money in the future. Instead of putting their money in the hands of entrepreneurs or investing more in their own economic endeavors, the unmistakable message of federal estate taxes is to consume it now, not pay it later.

Undermines job creation and wage growth. Not only does this message have a corrosive effect on the virtue of savings and prudent investment, but also it directly undermines job creation and wage growth; and these latter effects make death tax repeal everyone's concern. Heritage Foundation economists estimate that the federal estate tax alone is responsible for the loss of between 170,000 and 250,000 potential jobs each year. This additional employment never appears in the U.S. economy because the investments that would have resulted in higher employment are not made.

Prevents economy from achieving investment potential. Further, the effect of the estate tax on preventing the economy from achieving

its investment potential holds down wage growth. Workers are more productive when they have new tools, machines, and factories; and increased productivity boosts wages and salaries. It is through productivity growth that enhancements to economic and social well-being are and the virtues of our form of economic organization are most abundantly seen.

Contradicts central promise of American life: wealth creation. Indeed, the support for permanent repeal of federal death taxes stems generally from the appreciation of this last feature of our economy. Most Americans oppose death taxes because they seem so un-American. The death tax appears to many people as a clear contradiction to a central promise of American life: that if you work hard, save, and live prudently, you will be assured the enjoyment of your economically virtuous life. There are few other places on the planet where this promise is made (let alone kept), and it along with companion promises of political and religious freedom has attracted millions of immigrants to the United States.

Death taxes eat away at this promise. Some Americans, like farmers, ranchers, homeowners, face the threat of death taxes because they have improved the land upon which their other assets sit or because factors beyond their control, like the population growth of cities, drive up the price of their property. Many Americans save in their businesses in order to pass an asset along to their children; and, for millions of African-Americans and others for whom the economy is not always benign, the threat of seeing their life savings absorbed in a single tax bill is reason enough to demand permanent repeal.

Still others are just starting out or, like many women, returning to the labor force after raising families or taking care of other obligations. There before them is an economy that welcomes their enterprise and creativity, that promises a living in exchange for meeting the needs of people in their community. Small businesses offer a way around the corporate glass ceiling, and the language barriers that immigrants face in larger organizations are seldom-insurmountable obstacles in a business you own yourself.

Repeal the Federal Death Tax

As fresh and progressive as this economic picture appears, at the end of a life of economic struggle still stands the nightmare of the American dream. Without swift and decisive action by Congress, the death tax withers over the next decade but does not die. The uncertainty in tax planning will grow, the econ-

omy will consistently under perform, and the hypocrisy of the economic promise of American life will reverberate louder than ever. Now is the time to bring this sorry chapter in U.S. tax policy to a close.

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