# Where Not to Die

*by Diana Furchtgott-Roth*

Is it a sad commentary on our federal and state tax systems that where to die influences the location decisions of families and small businesses? Or does it show that tax competition between states is alive and well, fulfilling the goals of the Founding Fathers, who envisaged the power of states offsetting the power of the federal government?

Whatever the reason, the U.S. federal and state estate tax systems need repair. Although relatively few Americans are subject to federal estate taxes (fewer than 1 percent paid federal estate taxes in 2009, according to the IRS), individuals spend substantial sums not only on tax planning and avoidance but also on moving to low-estate-tax jurisdictions.

***Between 2000 and 2010, Maryland lost $5.5 billion in AGI; almost $3 billion went to its four neighboring states.***

The federal government gradually reduced its estate tax between 2002 and 2010 (Table 1), but 14 states and the District of Columbia have their own estate taxes (Table 2) and seven states have inheritance taxes (Table 3). If you have to die — and most of us do — do not die in New Jersey or Maryland before consulting top-notch estate planners. Those two states levy not only estate taxes, but also inheritance taxes.

Also steer clear of Washington, which has a 19 percent estate tax on assets of at least $2 million. And if that was not bad enough, the state eliminated the spousal exemption from the tax during its last legislative session. So without careful tax planning, families could pay 19 percent in estate taxes on a father's death and again when a mother dies.

It is difficult for one state to sustain a high rate of estate taxation when surrounding states have lower taxes. Perhaps that is why New York, New Jersey, Connecticut, and Massachusetts, which are in close proximity, have been able to sustain high estate taxes.

Data on state migration from the Tax Foundation show that states that had an estate tax in 2013 had a net outflow both of filers and adjusted gross income between 2000 and 2010. Nine of the 14 states and the district had net outflows totaling $92.7 billion. Five of the seven states with an inheritance tax had net outflows totaling $22.8 billion between 2000 and 2010.

Maryland has seen an exodus of taxpayers to Virginia, West Virginia, Pennsylvania, and Delaware. Between 2000 and 2010, it lost $5.5 billion in AGI; almost $3 billion went to its four neighboring states.

**Table 1.**
**Top Federal Estate Tax Rates by Year**

| Year | Exemption Amount | Rate (percent) |
|---|---|---|
| 1997 | $600,000 | 55 |
| 1998 | $625,000 | 55 |
| 1999 | $650,000 | 55 |
| 2000 | $675,000 | 55 |
| 2001 | $675,000 | 55 |
| 2002 | $1 million | 50 |
| 2003 | $1 million | 49 |
| 2004 | $1.5 million | 48 |
| 2005 | $1.5 million | 47 |
| 2006 | $2 million | 46 |
| 2007 | $2 million | 45 |
| 2008 | $2 million | 45 |
| 2009 | $3.5 million | 45 |
| 2010 | $5 million or N/A | 35 or 0 |
| 2011 | $5 million | 35 |
| 2012 | $5.12 million | 35 |
| 2013 | $5.25 million | 40 |

*Sources*: IRS, "The Estate Tax: Ninety Years and Counting" (2008).
McGuireWoods LLP, "Estate Tax Changes, Past, Present and Future" (2013).

Successful states are choosing not to have estate or inheritance taxes. Nineteen of the 31 states without either had a net inflow of tax filers and AGI.

The current federal estate tax rate is 40 percent on estates of at least $5.25 million. That rate is higher than it was in 2010, when the rate temporarily was zero under phaseouts in the Economic Growth and Tax Relief Reconciliation Act of 2001. Proposed legislation in the House and Senate would eliminate the federal estate tax. The Death Tax Repeal Act of 2013 (H.R. 2429), sponsored by U.S. Rep. Kevin Brady, R-Texas, would repeal the estate and generation-skipping transfer taxes, make permanent the 35 percent gift tax rate and the $5 million gift tax exemption, and adjust for inflation. The bill has 141 cosponsors. The parallel Senate bill (S. 1183), sponsored by Sen. John Thune, R-S.D., has 33 cosponsors.

Without fundamental tax reform, it is unlikely the bills will pass in this Congress. The legislation might pass the House, but it is not likely to pass the Senate Finance Committee, chaired by Max Baucus, D-Mont., or be brought to the Senate floor by Majority Leader Harry Reid, D-Nev.

Another solution has been proposed by Americans Standing for the Simplification of the Estate Tax, or ASSET, headed by Jack Fitzgerald, owner of Fitzgerald Auto Mall, a Maryland auto dealership.

ASSET has suggested that estates be taxed when families dispose of the assets, rather than when the assets are inherited. Estate taxes levied on family farms and businesses can require the sale of those entities to pay the tax, so changing the timing of taxation would enable families to pass their businesses on rather than sell them.

**Table 2.**
**Top Estate Tax Rates by State (2013)**

| State | Exemption Amount | Rate (percent) |
|---|---|---|
| Connecticut | $2 million | 12 |
| Delaware | $5.25 million | 16 |
| D.C. | $1 million | 16 |
| Hawaii | $5.25 million | 16 |
| Illinois | $4 million | 16 |
| Maine | $2 million | 12 |
| Maryland | $1 million | 16 |
| Massachusetts | $1 million | 16 |
| Minnesota | $1 million | 16 |
| New Jersey | $675,000 | 16 |
| New York | $1 million | 16 |
| Oregon | $1 million | 16 |
| Rhode Island | $911,000 | 16 |
| Vermont | $2.75 million | 16 |
| Washington | $2 million | 19 |

*Source*: Commerce Clearing House, "State Inheritance, Estate and Gift Tax Reporter" (2013).

**Table 3.**
**Top Inheritance Tax Rates by State (2013)**

| State | Exemption Amount | Rate (percent) |
|---|---|---|
| Iowa | N/A | 15 |
| Kentucky | $500 | 16 |
| Maryland | $150 | 10 |
| Nebraska | $10,000 | 18 |
| New Jersey | N/A | 16 |
| Pennsylvania | N/A | 15 |
| Tennessee | $1.25 million | 9.5 |

*Source*: Commerce Clearing House, "State Inheritance, Estate and Gift Tax Reporter" (2013).

Implementing the ASSET proposal would temporarily reduce tax revenue because estate tax collections would be postponed, or, if the business stayed in the family, never collected. Estimates of transition costs range from 1 to 2 percent. To smooth the transition, Fitzgerald has proposed a surtax on those with AGIs of more than $1 million. The amount of the surtax would depend on the transition cost.

***'Intelligent tax policy preserves the goose that lays the golden egg,' Fitzgerald said.***

Fitzgerald recently told me that individuals with AGIs of more than $1 million would be willing to pay a surtax to avoid the estate tax and the planning it entails. "Intelligent tax policy preserves the goose that lays the golden egg," he said.

The ASSET solution might catch on in individual states before Congress acts on it. Bills reforming the estate tax have a habit of passing the U.S. House and dying in the Senate. But there is room for state legislatures to pave the way and make their states a better place to live — and die. ✰

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