



ESTATE TAXES

by Ron Kirk

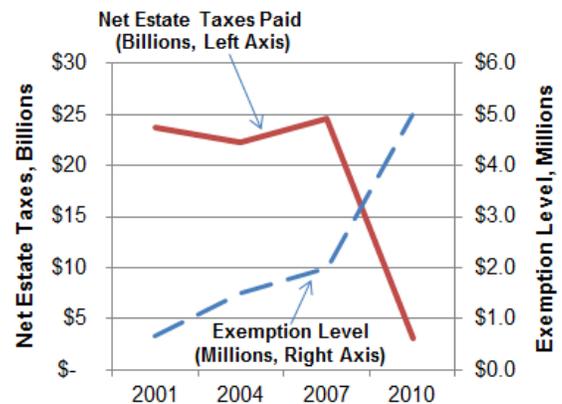
This issue brief provides information on the federal estate tax and the state tax credit that generates revenue for Colorado under the federal estate tax. The estate tax is levied by the federal government on the transfer of property at death. The federal estate tax includes a credit for state estate taxes paid, which allows individual states to collect estate tax revenue without increasing a taxpayer's combined federal-state estate tax liability. Many states, including Colorado, *received* estate tax revenue from the credit before it was phased out by Congress in 2005. Under current law, the credit will be reinstated in 2013. Seventeen states levy a separate estate tax, independent from the federal estate tax structure. Information on these states, as well as an overview of the impact of the estate tax on agricultural returns is also provided in this *issue brief*.

Federal estate taxes. In 2001, Congress altered the course of the federal estate tax by enacting the Economic Growth and Tax Relief Reconciliation Act (EGTRRA). This act phased out the tax by 2010. It also raised the exemption amount or value of an individual's estate that is exempt from federal estate taxes from \$675,000 to \$3.5 million. Finally, the legislation lowered the top estate tax rate from 55 percent to 35 percent. In 2010, the tax was reinstated with a \$5.0 million exemption and a top rate of 35 percent. The tax was extended through 2012, and the exemption was raised to \$5.12 million. Decedents having an estate with a gross taxable value less than this amount do not pay federal estates taxes.

Figure 1 shows the relationship between federal estate taxes paid and changes in the exemption level. The increase in the exemption meant that fewer estates were subject to estate taxes and fewer taxes would be paid. For example, the number of estate tax returns filed

decreased from 108,000 in 2001 to 4,588 in 2011. Net federal estate taxes paid in 2001 were \$23.7 billion, compared with \$3.1 billion in 2011.

Figure 1
Net Federal Estate Taxes Paid and Exemption



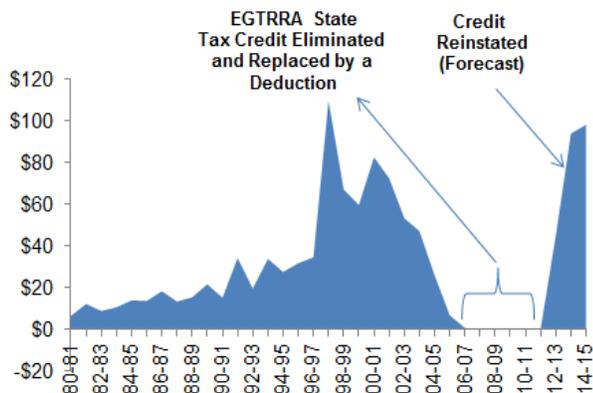
Source: Internal Revenue Service, *Statistics of Income*.

Colorado's estate tax. In 1980, Colorado's estate tax replaced the inheritance tax established in 1927. Revenue from Colorado's estate tax is equal to the maximum credit for state estate taxes allowed under federal law. The credit *reduces* federal estate taxes by the amount of estate taxes paid to a state. Thus, Colorado's estate tax **does not increase** the combined federal and state estate taxes owed.

Figure 2 shows the level of estate tax revenue collected by Colorado from the tax's inception in 1980 through the Legislative Council Staff revenue forecast period in FY 2014-15. Colorado received revenue from the state credit through tax year 2004. EGTRRA repealed the state tax credit in 2005 and replaced it with

a deduction, thus eliminating Colorado's estate tax. Colorado has not received estate tax revenue for deaths occurring in 2005 and afterward. Under current law, the credit will be reinstated for deaths that occur in 2013. If Congress does not act, Colorado will collect estate tax revenue in 2013.

Figure 2
Colorado's Estate Tax Revenue
(in millions)



Source: LCS September 2012 Revenue Forecast.

States with separate estate taxes. Currently, 17 states (other than Colorado) levy an independent *state* estate tax separate from the federal estate tax structure. These states have decoupled from the federal tax. Exemptions in these states range from \$338,333 in Ohio to \$5.12 million in Delaware, Hawaii, and North Carolina. Estate tax rates vary by state.

In FY 2010-11, these states collected \$4.5 billion in estate taxes. Four of these 17 states collected nearly two-thirds of all estate taxes, as shown in Table 1. Of the \$4.5 billion, New York collected \$1.2 billion, or 27.2 percent. Pennsylvania collected the second-largest amount at \$779 million, or 17.3 percent. In terms of the highest estate taxes, Pennsylvania ranked first, with a rate of \$1.51 per \$1,000 of personal income.¹ For all 17 states that levy independent estate taxes, the average amount of tax paid was \$0.36 per \$1,000 of personal income.

¹The rankings for estate taxes are based on tax collections per \$1,000 of personal income. This measure is used because it provides a way to measure taxes paid across different geographic regions with varying costs of living and is more aligned with the ability of taxpayers to pay taxes than per capita tax collections.

Table 1
State Estate Tax Collections (FY 2010-11)

State	Percent of Total	Estate Taxes (in millions)
New York	27.2%	\$1,219.2
Pennsylvania	17.3%	\$778.6
New Jersey	14.3%	\$642.2
Massachusetts	6.9%	\$309.6
Other 13 States	34.3%	\$1,539.2
Colorado*	0.0%	\$0.00
Total	100.0%	\$4,488.8

Source: U.S. Census Bureau.

*Colorado did not collect estate tax revenue in FY 2010-11.

Estate Taxes on Agricultural Estates

Colorado's General Assembly has debated concerns about the effect of estate taxes on family farms. This includes the possibility that heirs may be forced to liquidate the farm to pay taxes. Generally, farm estates have value from land and farm equipment, so they are less likely to have sufficient liquid assets to pay estate tax bills than other non agricultural estates.

EGTRRA's exemption also affected the number of federal estate tax returns filed for farm estates. The number of farm estate tax returns filed nationwide declined from 6,880 in 2001 to 677 in 2011. Of the 677 returns filed, 228, or 33.7 percent, were on taxable farm estate returns, down from prior years. In contrast, 40 percent of farm estate returns filed were taxable in 2001.

The Congressional Research Service indicates that about 1 percent of the heirs of family-owned farms are forced to liquidate in order to pay estate taxes. Factors affecting the ability to pay federal estate taxes include location, ratio of assets to liabilities, and the liquidity of the asset base. Federal law allows for estate taxes to be paid in installments over a period of nearly 15 years, with interest due for only the first five years.